

Subcontractors seek financial transparency

Bill would require notification if a project is in financial trouble

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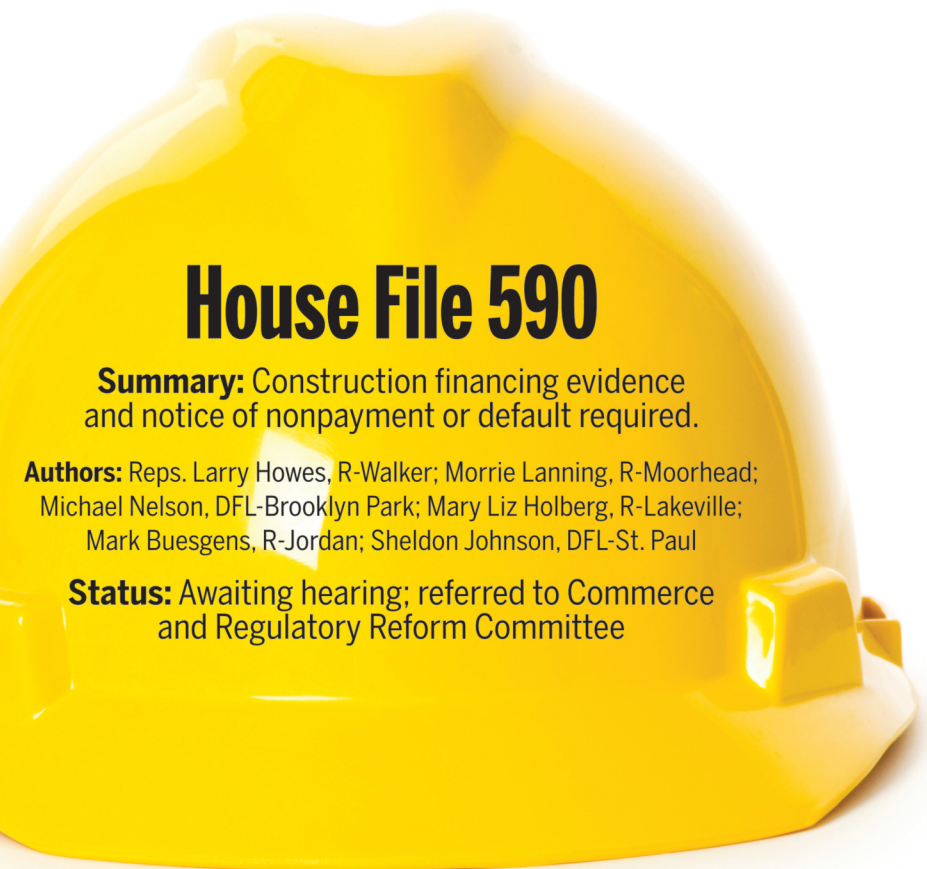
Minnesota subcontractors are saying, "Show us the money." Better yet, "Show us if there is *no* money."

That is the sentiment behind a bipartisan bill in the state House of Representatives that would require owners to provide "satisfactory evidence" of project financing before work begins, and would force lenders to notify subcontractors and suppliers of a construction loan default.

Subcontractors say they need that information to assess business risk and avoid situations where they get stiffed or are forced to settle for dimes on the dollar on a financially distressed project.

Lenders are not keen on the bill, saying that it would saddle them with inordinate administrative burdens and that it is not their contractual role to provide such information.

But for people like Tony Grazzini, president of the American Subcontractors Association's Minnesota chapter and a project manager at WTG Terrazzo & Tile in Burnsville, the notification require-



ments are overdue.

In some cases, a subcontractor may complete a job before discovering that the project had financial problems, he said. This comes after the sub has already paid for materials and labor.

"Now you have to deal with being paid 50 cents on the dollar, or maybe not at all," he added.

Some subcontractors ask for financial data, but others do not even bother because "there is not a willingness to give it," Grazzini said.

One contractor, who asked not to be identified for fear of losing business, told Finance & Commerce that he lost \$35,000

on a job a few years ago. If he had known the project was on shaky financial footing, he would have pulled out and cut his losses, he said.

Subcontractors put their own money into projects upfront, but may have to wait more than 90 days to be paid, he added. For smaller companies, he said, that "crushes their cash flow."

Another concern: Subcontractors increasingly must provide financial data about their companies to "pre-qualify" to bid on projects, but the same flow of information is not expected from the top of the project chain, Grazzini noted. While subcontractors are not required by state law

Financing ‘The problem they have is with the contractor, not the lender’

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to submit that data to contractors, it has become standard practice in the industry.

The bill, which has not had a hearing yet, addresses that issue in part by requiring the “owner or other persons making payment under the contract” to provide “satisfactory evidence” of project financing.

Moreover, if there is “any material change” in the financing, the party responsible for making payments must “notify any contractor of the nature of that change,” the bill states.

Mike Schmaltz, executive director of ASA-Minnesota, said it is often difficult for subcontractors to get that information.

“All we are doing is saying, ‘What is good for the goose is good for the gander,’” Schmaltz said. “For subcontractors to make good business decisions, they should know where things stand on the financing of a project.”

In general, the Associated General Contractors of Minnesota supports the goals of the bill, said Tim Worke, director of AGC-Minnesota’s highway division.

“We generally agree that it’s something that has merit,” Worke said.

But bankers have a problem with the

administrative burdens. Moreover, they say, it is not the lender’s job to give financial data to everyone involved in a project.

“I understand where the subcontractors are coming from,” said David Skilbred, vice president of government

“For subcontractors to make good business decisions, they should know where things stand on the financing of a project.”

— Mike Schmaltz, ASA-Minnesota

relations for the Independent Community Bankers of Minnesota. “But the problem they have is with the [general] contractor, not the lender.”

Skilbred said the bankers he represents are particularly concerned about a provision that requires lenders to give written notice of a construction loan default to “all known contractors, subcontractors and suppliers.”

“That is an ominous task and would be overly burdensome, because it would be very difficult to know all of those players and to be sure that they are the right players,” he said. “It would be very easy to all of a sudden notify the wrong supplier or the wrong subcontractor.”

Subcontractors are unmoved by those arguments. Being paid in a timely manner has long been a concern for subcontractors, but they say it is especially urgent in a slow economy.

According to ASA’s talking points on the bill, the “perverse reality is that sometimes it’s in the best interest for project lenders, owners and prime contractors to have subcontractors do work even if they know that they cannot pay the subcontractors for their work. And subcontractors only find out after it’s too late.”

“In a nutshell, we are asking for greater transparency in financing on projects,” Schmaltz said.