

December 2017 Newsletter

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## Hiring Subcontractors: How to Vet Them & Protect Your Business

Information Provided by the Hartford Insurance Company

General contractors are like magicians. They create three-dimensional buildings out of two-dimensional drawings and manage the many details that make that happen – from ordering materials and inspecting completed work to coordinating schedules, handling paperwork and troubleshooting jobsite problems. They're also responsible for hiring and managing the specialized subcontractors who work under their direction.

Quality-minded general contractors understand the importance of choosing subcontractors with top-notch skills and exemplary work habits. The success of their projects depends upon it, and so do their reputations.

# Hiring Challenges in Today's Marketplace

"Today's market has fewer jobs with more people bidding on them, often without the necessary expertise," says David Maurice, Director of Commercial Marine Underwriting at The Hartford. "Subcontractors in need of work may bid low and come on to jobs that exceed their abilities."

A talent deficit isn't the only difficulty general contractors face. With the current shortage of available projects, general contractors themselves need to keep bid prices down and may hire lower-cost contractors in order to accomplish that. While this may be a prudent choice for fiscal reasons, it may not be in the best interest of the project overall. If the sub's workmanship is below par, the quality of the completed job may be at risk. Safety issues can lead to job-site incidents that affect the entire project. And costs can easily double as a result.

## Best Practices for Hiring Subcontractors

Prequalifying subcontractors is the best way for general contractors to hire the best workers for the job and reduce the risk of rework, delays, and quality or safety issues once the job is underway. This may require additional upfront time but pays off in the long run. Prequalification checklists or questionnaires can expedite the process and ensure that all bidders are providing comparable information.

These are recommended areas for general contractors to scrutinize:

- **Look for strong credentials and solid performance.** Request a report on the subs' credentials, management team, experience, expertise and geographic reach. Examine work history and any lawsuits, claims, disputes or bankruptcies. Also look at current projects underway and upcoming projects in the queue to ensure the sub will have the capacity to meet the demands of your job in the timeframe you require.
- **Ensure sufficient financial strength and stability to handle the job.** Request details such as the sub's annual contract volume, sales and net worth, or ask for two years of financial statements with the assurance that the information will be kept confidential. A review of these details can reveal red flags such as a lack of working capital, more debt than equity, or declining income with an increase in accounts receivable.
- **Require strong safety practices.** Over 20 percent of all workplace fatalities reported in 2014 were in the construction industry, according to the [Occupational Safety and Health Administration \(OSHA\)](#). While it may be impossible to eliminate entirely the risk of injury, lack of safety standards and procedures can result in higher instances of worker injuries. A local inspector who observes safety violations also can shut down a jobsite, leading to a potentially huge consequential loss.
- General contractors should ask potential subs about their safety plans and processes and examine their workplace injury incident rate or Experience Modification Rate (available through the sub's state rating bureau). An EMR of 1.0 or lower is considered the industry average and can be indicative of a strong safety program that's consistently enforced.
- **Require strong quality controls.** Quality control and quality assurance (QA/QC) programs help prevent rework and warranty work and reduce the potential for construction defect claims. When screening potential subcontractors, ask about their QA/QC programs and how they function.
- **Understand the demographics of the sub's workforce.** Ask about the subs' employees: are they permanent or temporary, and what are their age groups? Both young and aging workers statistically are more prone to injury on construction jobsites. Entry-level workers may not have the skills or tools required to meet performance expectations.
- **Ask for references and follow through on them.** This important step is an opportunity to speak with others who are familiar with the subs' quality of work, performance and work ethic.
- **Require the sub to be properly bonded and insured.** If the general contractor is required to have contractor's bonding, the subcontractor should be bonded, too, in order to guarantee their work performance and payment of all workers and suppliers. Subs should also maintain workers' compensation coverage for its employees for the project duration, and maintain minimum general and auto liability coverage. Ask potential subs to provide proof of insurance in the prequalification process.
- **Establishing the Contract.** Once subcontractors have been vetted and selected, a thorough [written construction contract](#) that clearly spells out expectations is essential to protect the general contractor's interests. Include a description of the services and materials the sub will provide as well as the scope and price of work, standards of quality, warranties for defective products or workmanship, and details such as the work and payment schedules and expectations for worksite cleanup and removal of debris. Also spell out [contractor insurance](#) requirements and indemnity agreements.

Submit all subcontractor agreements to an attorney for review and evaluation before signing. Your insurance provider can also be a valuable resource that can advise on clauses to include and ensure that insurance coverage falls in line with the contract.

## Insurance Protection for General Contractors

Given the risk associated with construction projects, insurance is essential. The following coverages protect the general contractor from the various forms of liability that can arise on a construction site:

- [General liability](#) provides protection from liability arising from accidents that damage property.
- [Workers' compensation coverage](#) provides protection for injured worker.
- Builder's Risk insurance covers damage to the building or materials during construction, no matter

what the cause, and automatically applies to subcontractors with respect to work they are performing under a general contractor's written contract.

- Owners and Contractors Protective Liability and Railroad Protective Liability protects the project owner or general contractor from liability due to bodily injury or property damage claims caused by a designated subcontractor. Coverage also extends to the named insured's alleged negligence in the hiring of or failure to adequately supervise the designed contractor.

From an underwriting perspective, general contractors who not only oversee the subcontractors but also exercise a degree of control over the subcontractor's work are viewed more favorably.

## In Summary

Good subs will show up when needed and work under the general contractor's direction with the need for minimal supervision. Prequalifying all candidates and setting standards and clear expectations will lay the foundation for smooth-running relationships, quality workmanship, greater safety on the job and a completed project that meets specifications and expectations. These steps combined with the right insurance and careful adherence to all contract and insurance provisions can stave off the risks that might otherwise jeopardize a general contractor's business..

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