



Restoration Pricing

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Feature

Choose the right ingredients to keep your profits healthy.

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As with any important question or topic, there are a number of opinions, theories, ideas and approaches that should be considered.

The pricing of restoration and emergency services is no different.

It is important for all parties involved to understand both the goals and limitations of the project before realistic pricing can be determined.

The goal of restoration is to restore the property to the pre-loss condition as quickly and as economically as possible.

Although the responsibility to reach this goal is shared equally by the insured, contractor and the insurance company, each of these parties has different and sometimes competing priorities.

Competing priorities

The property owners (the insureds) are concerned with costs and quality.

The insureds are legitimately concerned about costs. Some questions that run through their minds during the restoration process often include:

- What is a reasonable settlement?
- What happens if the contractor charges more than the insurance settlement?
- Why do I have to pay the deductible?
- Should I accept restoration, or should I demand replacement?
- Is the insurance company out to avoid paying the loss?
- Why does the contractor charge so much?

The questions, both spoken and unspoken, are nearly endless.

If the insureds had a better understanding of the role of the insurance company and how claims and losses are handled, most of these questions would resolve themselves.

Without a doubt, many property owners do not understand the true role of the insurance company. They fail to realize that the policy they purchased has limits, both in terms of the total coverage and in the specific damages covered or excluded.

Often, the insured believes insurance will cover anything that happens to the property. In reality, a policy that covers any and all losses would be both unaffordable and counterproductive.

If that were the case, why would anyone maintain property or take steps to preserve and protect the property from potentially damaging circumstances?

The property owner is at a disadvantage when dealing with losses simply based on lack of experience with filing claims. This can lead to unrealistic expectations as to costs, the results and the insurance coverage.

Butting heads

Many people believe that the goal of the insurance company is to avoid paying for a loss entirely,

or to pay as little as possible.

Insurance companies clearly understand their role in the claims process — and they should. After all, they wrote the policy and evaluated the risks associated with coverage before offering the policy to the property owners.

In my experience, most insurance companies are ready and willing to pay for reasonable and customary costs — provided that proof of these costs is provided.

This means that the restoration contractor is torn between two masters.

On the one hand, we owe our allegiance to the customer — after all, it is the customer's home or place of business that we are restoring.

But, we must also work with the insurance company to see that the customer's loss is handled in a manner that both expedites the claim and does not alienate the provider of funds.

This can be a difficult tightrope to walk. The customer is ultimately responsible for all costs associated with the project, and because we work for the customer, we must follow their direction.

The customer's needs and wants may be significantly different than what the policy covers. If we place too much allegiance with the insurance company, we are really doing our customers a disservice.

We can suggest and direct the customer to actions that will both meet the customer's immediate and long-term needs and — at the same time — we must follow generally accepted insurance practices. I'm not suggesting that restorers act as adjuster for the loss, but we are often the only resource the insured has in the middle of the night. A simple explanation of the process goes a long way in calming the insured.

Limitations

The insured is limited by available funds, not only in total but in available cash flow to finance the project.

Sometimes even coming up with the deductible can put a strain on the household budget.

Questions about these limits abound:

- Will the insurance company cover all of the costs associated with the loss?
- Why repair/restore instead of replace?
- Does the insurance company really understand my needs and do they know the real cost associated with repair or replacement?
- Can I remodel the house during the repair or restoration, and how will the insurance-related costs be calculated?
- Why am I given an allowance for flooring that is less than what I originally paid?
- Does the insurance company have a special deal with the contractor that they recommend?
- What happens if I'm not happy with the work?
- Can they really get the odor out?
- If it's wet, isn't it ruined?
- My neighbor got a new roof, why can't I?
- I have a replacement cost policy, but the insurance only paid actual cash value (ACV) for the contents we decided to discard. Why?

The contractor's limitations produce a different set of questions, all related to the scope and related charges for the services to be provided.

Costing and estimating are two separate but related functions.

Estimating costs before the project begins appears to be a simple function of using unit pricing based on past experience factored to reflect current labor and material costs.

Unfortunately, most restoration contractors fail to accurately record all of the costs associated with a specific service or project. This means that their estimates will be inaccurate.

Unit pricing is simply a process of determining the average costs for labor and material.

Good unit pricing will also factor in economies of scale, setup time, travel time, availability of skilled labor, etc.

Unit pricing is one of the easiest and most accurate means of estimating job costs, provided that an accurate database of past costs is recorded.

Data services companies

There are several companies that provide broad-based unit costing services and databases to the insurance industry and contractors.

Information is compiled from actual losses, and then organized and averaged for postal codes or regions of the country.

Theoretically, any company should be able to take information from a database supplier and profitably complete any project.

Unfortunately, these databases only provide historical averages, not actual costs for individual contractors.

If unit pricing is compiled from data from a large loss restored by an exceptionally efficient contractor with no pressure to rapidly complete it (no extra evenings, weekends or overtime work), total costs may be lower than a smaller project restored by a different contractor.

If my head is in an oven and my feet are in the refrigerator, it doesn't mean I'm at the right temperature. Averages don't accurately represent the actual cost of any specific job.

Competitive pressures can also compromise validity of pricing data. If a contractor bids and completes a job at less than cost — which is sometimes done simply to keep a crew together during a slowdown in business — the database averages will be inaccurate.

Overhead costs

Individual companies' overhead (annual fixed costs and job-specific costs) vary significantly.

Companies with total revenues of less than \$1 million will typically have a higher overhead (as a percentage of sales) than larger companies.

Fixed overhead is nearly the same for a company with revenues less than \$1 million, as compared with companies doing five or 10 times more business.

Fixed overhead costs are general and administrative expenses such as rent, insurance, office expenses (bookkeeping and office labor expenses), officer salaries, management salaries and legal and accounting expenses.

Smaller companies' fixed overhead, as a percentage of income, is often higher than larger companies.

Hours of service also have a bearing on costs. Companies that deliver emergency services 24 hours a day have higher overhead than companies that operate only Monday through Friday.

Emergency service companies have higher costs associated with the risk of not having a steady or reliable work schedule.

Following "the herd"

Following "the herd" can be dangerous to your restoration business.

One of the least discussed limitations of broad-based pricing databases is the self-feeding, self-referential nature of data collection and distribution.

If a contractor uses a pricing database for pricing work and that data is then fed into the system, it then reproduces itself back into the system to provide the next price list.

Most contractors are reluctant to change the prices unless they are completely inaccurate.

Insurance companies and adjusters use the databases to limit the amounts paid to contractors.

There is an endless cycle of a price being provided, used and then fed back into the system to produce the new price, which — due to price averaging — limits the accuracy of the pricing used and provided by the insurance companies.

If one out of a 100 contractors in a region reports adjusted pricing, the net effect is a 1 percent influence on the average pricing.

There are only two valid reasons to use a broad-based data collection service.

One reason is to allow new companies a starting point for determining restoration and repair charges. Unfortunately, most of these companies simply keep these prices without doing any cost accounting to verify the accuracy of the unit prices.

This continues the self-feeding cycle.

The second reason to use a data collection service is to help insurance companies monitor costs and rein in excessive charges. An unfortunate side effect is that the data is often misused against legitimate contractors' charges. Those misuses include:

- Failure to include profit and overhead in costs
- Not including certain line items with associated services
- Taking the definition for services out of context
- Inaccuracy of service definitions
- General lack of proper costing and charges.

A typical example is providing the cost for painting a room, but not including masking, painting the trim and openings and furniture moving.

Simply applying one unit pricing where there may be four or five tasks involved to complete the assigned work invalidates the accuracy of the unit price. Blame is due on both the contractor and insurance parties for this weakness.

Value or quality?

The debate about fair and reasonable costs seldom considers the quality of the work.

Society in general assumes that all costs are the same; therefore, all work is of the highest quality.

McDonald's[®] hamburgers are certainly different than those at a Ruth's Chris[®] restaurant, but they are both just hamburgers!

Most restoration contractors view their work as premium quality and price work accordingly.

Sadly, some firms wouldn't know quality service if they stepped on it. It is unrealistic to charge premium prices for substandard work.

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