

Brown Smith Wallace, LLC

The Balanced Scorecard

For Construction Industries

Aligning Strategies with
Everyday Performance

636.255.3000
www.bswllc.com



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Executive Summary

If you're tired of rah-rah planning sessions that result in your team leaving it all in the locker room, you're probably ready to consider the Balanced Scorecard approach to performance measurement.

You don't need a scorecard to know who the players are anymore, but someone still has to keep score to assess overall performance.

Balanced Scorecard is a proven method that aligns strategies with everyday performance. This key linkage will enable everyone in the organization to connect as a true team with common goals and a clear understanding of their roles – and how their performance affects the overall organization.

Balanced Scorecard will help:

- Employees better understand the organization's strategy
- Link employee's objectives to the overall organizational plan
- Focus effort on critical success factors rather than on less vital aspects
- Enable management to manage strategy, not just tactics

Background on the Balanced Scorecard in the Construction Industry

Many construction executives today cringe when they hear the words “strategic plan.” That’s likely because of previous bad experiences with strategic plans. Perhaps you recall a long detailed process involving significant time investment that yielded a generous binder, filled with glitzy diagrams and detailed graphs. There may have even been a big kick-off event where the entire company was invited to learn about the strategic future of the organization. The plan was met with great fanfare, and people left the meeting energized and excited.

But what happened? A few weeks after launch, the plan became less important than daily activities and meeting project delivery dates for a seething customer. Months may have passed before there was an update on the progress against the plan. People never really understood how they could contribute, and further, weren’t given any incentives to do so. And then finally, a year later, management looked at one another and wondered why such little progress had been made toward achieving the goals set within the strategic plan.

Four Barriers to Success

Strategic plans often fail because of four barriers to success:

1. **The vision barrier.** Few people in the organization understand the strategies of the organization.
2. **The people barrier.** Most people have objectives that are not linked to the strategy of the organization.
3. **The resource barrier.** Time, energy, and money are not allocated to those things that are critical to the organization. For example, budgets are not linked to strategy.
4. **The management barrier.** Management doesn’t spend enough time on strategy and, instead, focuses on short-term tactics. Management works in the business, not on the business.

These barriers are real. The cycle creates concerns across the country and around the world. Consider this from the *Balanced Scorecard Collaborative*:

- Only 5% of the workforce understands their company's strategy
- Only 25% of managers have incentives linked to strategy
- 60% of organizations don't link budgets to strategy
- 86% of executive teams spend less than one hour per month discussing strategy

Countless experiences like the above may have left you thinking, "There has to be a better way." There is! The balanced scorecard is a concept that was developed in the early 1990s, and it continues to enhance the financial performance of many businesses today.

Enhanced Performance Measurement

Essentially, the balanced scorecard is a "Management System" that enables organizations to clarify their vision and strategy and translate them into action. It provides feedback around both the internal business processes and external outcomes (double-loop feedback) in order to continuously improve strategic performance and results.

It is also a methodology for communicating strategy throughout all levels of an organization and gives construction executives and managers a comprehensive and focused view of business performance.

While measuring a company's performance is nothing new, the balanced scorecard approach focuses not only on financial outcomes, but also on the human issues that drive those outcomes.

The system forces construction executives and managers to focus on the performance metrics that drive success, which are often non-financial metrics.

Ultimately, the balanced scorecard looks comprehensively at employee needs, which drive internal processes, which enhance customer satisfaction, which yields better financial performance. This comprehensive process will enable you to make intelligent, strategic day-to-day decisions.

Performance Metrics

The Balanced Scorecard includes the following metrics:



The term, “balanced,” refers not just to the four metrics, but also to the fact that a successful implementation requires positive support from all segments of the company’s stakeholders.

An important aspect of the balanced scorecard approach to performance measurement is that it balances historical measures (lagging) with future predictive measures (leading).

Over time, this alignment will identify cause-effect relationships that will assist in fine-tuning future strategy. This provides for continuous improvement in critical processes leading to better performance results.

Three Phase Implementation Process

To implement the balanced scorecard, you need to execute three comprehensive phases. Let's review each phase and create an example of a balanced scorecard as we go.

Phase 1: The Strategic Foundation

Step 1 – Strategic Alignment

A clear strategy is essential to formulating the balanced scorecard. For a strategy to be clear, it needs two elements. First, it must have specific objectives that tell people what to do; and second, a clear set of targets for communicating what is expected.

Strategic Objectives Expressed in Relation to Action

- By January 1st, 2008, project cost data will be accessible in the field by 100% of project managers within the company through implementation of an ERP system.
- Hand tool loss will be reduced by 50% in the next six months through the implementation of a RFID system for single items valued at more than \$100.
- By June 1, 2009, we will have completely revamped our change order process and have developed benchmarks to measure our ability to secure approved change orders, enhancing job profitability and increasing cash flow.
- By 2010, we will be known as the most safety oriented construction company in the region.

Step 2 – Communicating Your Plan

Once you have clear objectives, you need to make sure you are able to communicate them to your stakeholders. Every individual in your organization needs to know the objectives and be able to internalize and visualize how their daily job performance supports the achievement of these objectives.

You need to ensure that your communication style is appropriate for each level of your audience. You should prepare a written communication plan that details how the message will be communicated to each segment of your audience.

| Sample Communication Plan | |
|---------------------------|-------------------------|
| Who | Method |
| Executive Management | Retreat w/Presentation |
| Project Management | Presentation w/handouts |
| Field Employees | Presentation w/handouts |
| Suppliers/Sub-contractors | Mailing/On-site visit |

Step 3 – Strategic Areas

Strategic areas are those identified and prioritized for inclusion in the balanced scorecard. Often, an organization finds itself trying to do too many things at once, resulting in marginal performance in all areas. The balanced scorecard requires a targeted focus in five or fewer areas.

Remember, the balanced scorecard revolves around specific stakeholder groups such as employees, customers and financial stakeholders.

One of the four elements of the balanced scorecard is improved financial performance. Below, you can see how to relate the strategic area of improved financial performance across all four elements of the balanced scorecard.

| Strategic Area: Improved Financial Performance | |
|--|--|
| Financial | More Revenue (Drives ↑) |
| Customer | Additional Customers (Drives ↑) |
| Processes | Customer Marketing Programs (Drives ↑) |
| Employees/Learning & Growth | Support Systems & Personnel (Drives ↑) Enhanced Safety (Drives ↑) |

Key strategic areas you might want to include in your scorecard include:

- Customer Service
- Depth/Breadth of Service Lines
- Efficiency
- Safety
- Innovation
- Philanthropy

Each strategic goal must drive toward a strategic area. So, to reference one of the strategic goals we established earlier, see below.

| Strategic Goal | Strategic Area |
|---|-----------------------|
| Hand tool loss will be reduced by 50% in the next six months through the implementation of a RFID system for single items valued at more than \$100 | Financial Performance |

Step 4 – Strategic Grids

Now that you’ve established your strategy and strategic areas, you need to build your strategic grids.

The strategic grids outline the specifics of your strategy. Remember, the four balanced scorecard perspectives or elements are employee/learning and growth, internal processes, customer satisfaction and financial performance.

This step, which links all strategic objectives together, is one of the most challenging parts of the entire process.

To illustrate a practical application, here is a strategic grid example for the strategic area of improved financial performance:

| | | | | |
|---|---|---|--|----------------------------------|
| Financial | Improved Financial Performance | | | |
| | Grow Revenues ↑ | | | |
| Customer | Acquire More Customers ↑ | | | |
| | Become the Price Leader ↑ | | | |
| Internal Processes | Improve Operational Efficiency ↑ | | | |
| | ↑ Cost Reduction Program | Knowledge Based System | Reduce Non-core Activities ↑ | Reduced work related accidents |
| Employees/ Learning & Growth | ↑ Training - Best practices in project management | Database network on operational performance | Re-align organization with core competencies ↑ | Develop safety incentive program |

In practice, you will actually build this grid one layer at a time. You start from the top and ask yourself what are the drivers for performance that will yield the desired result.

Once each grid is built, you need to make sure that everything fits with your overall strategy. Remember, you need to limit your objectives to a few critical strategic areas and keep the total number of objectives to no more than 25.

Phase 2: Three Critical Components

Step 5 – Measurements

Each strategic objective requires a measurement or key performance indicator. In addition, the measurement must meet several specific conditions, i.e., it must be:

- Linked to the strategic objective
- Repeatable, allowing comparisons over time
- An indicator of future targets and performance
- Accountable, reliable, verifiable and accurate
- Available when needed

In addition, you need to make sure your measurements are not all lagging indicators of performance. Most financial measurements, by default, fall into this category. However, there are literally dozens of measurements that can be taken that are leading indicators of future financial performance. These may include items such as customer satisfaction, new contracts, or service response time. These measurements all point to a future of increased financial performance. Remember, however, there could be dozens of measurements per strategic grid. You need to

make sure you are focusing on the most important and relevant measurements that point to your strategic objective. Measuring more than 25 items per scorecard will result in a cumbersome and unproductive scorecard.

Step 6 – Targets

Each measurement must have a target established in order for it to truly drive performance. For example, going back to your strategic objective of being safety-oriented, you would set a goal such as the following:

Strategic Goal: By 2010, you will be known as the most safety oriented construction company in the region, by providing continuous mandatory safety programs for your workers.

| Year | 2007 | 2008 | 2009 | 2010 |
|------------------------------|------|------|------|------|
| Hours of Training Per Person | 21 | 26 | 33 | 40 |

Step 7 - Programs

One of the most gratifying components of establishing the balanced scorecard (except of course, achieving your objectives!) is putting programs in place to achieve the strategic objectives.

An example would be to develop a safety program with defined safety awards to promote a firm wide culture of safety. Programs you should consider to help you achieve your objectives would:

- Require some level of resource commitment
- Have designated leadership
- Be supported and sponsored by executive management (very key to success)
- Benefit one or more strategic objectives (the more strategic objectives served per program, the higher priority the program should be)

Phase 3: Deployment

Step 8 - Launch

The deployment phase will include aligning the first developed scorecard with the other parts of the business. This is a critical component of the process to ensure there are no conflicts or competing agendas. Further, as you deploy your scorecards throughout the organization, it gives you the opportunity to introduce the concept and get buy-in across the organization. While many scorecards start

at the executive level, some of the best scorecards are developed by your employees at the unit level. This is because these scorecards touch more constituents, including customers, vendors, other employees, production, sales, etc.

Summary

This white paper is designed to give you an overview of the basics of the balanced scorecard, a total management system that leads to the achievement of your strategic plans. A successful implementation will ensure that all your employees know and are focused on the measurement and accomplishment of these plans in their day-to-day activities.

The balanced scorecard has proven its effectiveness for construction companies of all sizes. It can energize and transform an organization, resulting in significant performance improvement and company success in both the short and long term. We encourage you to contact us to learn more about how the balanced scorecard can benefit your organization.

Authors

William F. Willbrand, Jr., CPA

William (Bill) is a member and practice leader at Brown Smith Wallace. He has more than 25 years of experience in helping construction companies improve their operational and financial performance. In addition to audit and tax services, Bill has provided performance measurement and enhancement services and merger and acquisition assistance to contractors. Please contact Bill at 636.754.0200 or billw@bswllc.com.

John D. Wunderlich, CPA

John is a senior consultant with Brown Smith Wallace, who primarily serves clients in the construction industry. He has more than 30 years of experience working with the industry, including having served as the former CEO/EVP for a major St. Louis based construction company. John has significant experience in performance improvement, balance scorecard implementation, cash flow management, succession planning and financial planning, including ESOP analyses. Contact John at 636.754.0214 or johnw@bswllc.com.

Service Offerings for Contractors

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