Eight Common Problems for Entrepreneurs

Most entrepreneurs start their business because they really enjoyed some craft be it cooking for restaurateurs or auto mechanics for garage owner or pharmacy for neighborhood drug store owners. Their companies grew because they not only enjoyed it but were very good at it as well. Word of mouth is all the advertising that they need. They work hard, take care of their customers, and the company becomes successful. The company is making money and it is fun to come to work.

But then something starts to happen. It gets so successful that they need to add staff to support all of their work. The work gets harder. Employees aren't as good as the founder. More customers mean more peaks and valleys. The added infrastructure increases your costs. AR lags AP so the company is always in a cash crunch. Sales are up but profits are down. Where the entrepreneur used to get great satisfaction in his little enterprise, what was fun now seems a lot like work.

The problems are really all based on small companies growing beyond the ability of the founder to keep the business in his head. He adds employees and the structure of the business is simply not in place to handle it all. He has more customers, many of whom he doesn't know personally. Whereas he could easily predict his receivables collection in the past, it is more complicated now. He has a broader set of suppliers and the volume of his payables has grown proportionally. And of course the payables come due before the receivables are paid.

In my work with over 50 consulting clients, I have encountered a set of problems that are common to virtually every entrepreneurial company. It doesn't matter what the company does for a living – be it a restaurant, a steel fabricator, or law office. I have isolated them to the following 8 problems:

1. Charlotte's Web Syndrome
2. Presumption of Profit
3. Poor Record Keeping
4. No Post Mortems
5. Lack of Accountability
6. Inconsistent Processes
7. Lack of Urgency
8. Lack of Strategic Planning

In this paper, I will describe the problem, its root cause, and finally the best course of action to solve it.

Charlotte's Web Syndrome

Failure to properly delegate is the single biggest problem I run into in virtually all of my clients. I call it the "Charlotte's Web Syndrome". Charlotte sits in the middle of her web all day long and does nothing but takes care of flies. They hit the web, she goes and processes them and then she goes back to the middle again. At the end of the day, she rebuilds her web so that she will be ready to do it all again tomorrow.

Then she gets the idea "If I build a bigger web, I'll get more flies". So at the end of that day, she builds a bigger web. She works a little harder, but by golly, she gets more flies. Feeling good about her accomplishments, she builds a bigger web that night, and again gets more flies.

She keeps doing this and it works great for a while, but she starts to find out that she is staying up later each night to build her web and the lack of sleep starts to get to her. So she stops rebuilding her web each night but rather only patches the bad spots. Her web is just as big but now it isn't as effective. Flies hit the web but they don't get stuck and they start to get away before she gets to them.

Imagine that Charlotte represents company management. The web represents your sales. And the flies are the profits. When the company was small, sales were low and management could easily handle the load by itself. Every opportunity for profit was realized because management had the time to address each opportunity. But the company grew. And for a time, management could continue its hands-on approach. They had to work harder and longer hours but the work was successful and they learned how to keep multiple projects running. In the past, they were able to keep everything in their head and for a time they were able to continue to do that.

But size brings complexity. There are more details and "stuff happens". There are more fires to put out. There are conflicting priorities. To keep up, short cuts are taken. And things start to slip through the cracks. You find yourself going back to pick up the pieces of the things that were missed. There is rework. Change orders aren't documented. Work is done but not invoiced. Invoices are disputed because of lack of documentation. Materials aren't delivered so shop floor workers sit idle. Poor scheduling results in idle workers in one area of the shop while other areas have bottlenecks because the demand exceeds capacity. Projects fall behind. Deliveries are delayed. Billings go out late. And collections don't occur. Cash flow is pinched and you can't always pay your bills on time.

Then you start to wonder, where is all of the profit that the increased sales was supposed to produce? You are working your tail off. Revenue is up. But you are not getting the profit that you expected. In fact, your profit has actually gone down.

Cause of "Charlotte's Web Syndrome"

The root cause of Charlotte's Web Syndrome is failure to effectively delegate. While you may hire people to relieve the load, you maintain tight controls on any decision making processes. People need to come to you before doing anything. You need to bless every action. But you are the only one with the expertise to make the right decision and because all of the pertinent data is in your head, you are the only one with the necessary information to make a good decision. However, you become the bottleneck. Everyone has to wait until you have the time to get to each individual problem.

Conversely, you may delegate activities but fail monitor them. Lack of coordination makes people lone rangers making decisions without knowing the bigger context. So you find yourself getting dragged into issues after they have escalated into full scale problems.

Solution to "Charlotte's Web Syndrome"

In the early stages of a company, the "Charlotte" approach is clearly an efficient operating approach. Most small companies assume that management style because it is easy. You indeed are the "expert" in your field and you have your finger in every area from sales to delivery. You know your customers intimately and have a clear understanding of what they want and delivery is much easier. But the business model of central expert reaches its capacity limit fairly early. You need to develop a different model. You need a paradigm shift.

This is where most entrepreneurial companies mess it up. They recognize that they need to hire people to do the work but they either handcuff their employees so that they can't do their job or they turn them loose without coordination.

Proper delegation means that people are not just given the responsibility to perform a task but are also given the resources to accomplish them. And they have the authority to utilize those resources.

But effective delegation isn't just turning people loose. It requires controls and accountability.

- **Policy is our friend.** Good policies set the boundary conditions for the work to be done. Your employees know what they can and cannot do and what limits must be maintained.

- **What gets measured gets done.** Make sure that you keep your fingers on the pulse. You don't do the work but you do make sure that it is being done properly. You get involved only when it is not being done right. This is called "management by exception" and will be discussed in depth later.

Presumption of Profit

The second problem that I find at virtually all of my clients is a presumption of profit. When companies are small, overhead is low, and the vast majority of gross margin ends up on the bottom line.

But as a company grows, investments in plant and equipment are made. Administrative infrastructure is built and the cost of sales goes up. Staff are added with their accompanying costs of taxes, workers compensation, benefits and other expenses.

So, you bid a job the way you always did. Your customer pushes back on price. But you "know" that you have room to cut your costs and you do so. You do a good job but for some reason at the end of the year, you didn't produce the profit that you expected. And you don't know why.

Cause of Presumption of Profit

What has happened is the cost structure has changed but the pricing strategy hasn't. The easy process simply isn't appropriate anymore. Where you "knew" you were making a profit in the past, you really aren't anymore. And what you thought you could cut and still make a profit may actually be reducing your income below your breakeven point.

Because you don't cost out your projects and don't do overhead allocation, your true profitability is obscured. Other jobs may carry the overhead for a period of time but virtually every customer pushes back on price at some point and without proper cost data, you will begin to give back profit on those jobs as well.

Solution for Presumption of Profit

The solution for presumption of profit is to "engineer" profit into each job. It recognizes the difference between pricing and costing.

Pricing is a "what the market will bear" process. You must not price yourself out of a market but then you also don't want to leave money on the table. This is the "black art" of salesmanship. This is where a good salesman distinguishes himself from a bad one. A good profit oriented salesman is worth every penny you pay him.

However, selling is only half of the process. You need to cost out your projects to determine whether you can afford to take the work. No one is a non-profit by choice. But many companies unwittingly become non-profits because they don't do the costing step.

Costing looks at your projects and asks: "How much is it going to cost me to deliver this project and am I actually going to make money on it?"

Costs include materials costs, direct labor, other expenses (subcontractors, freight, machinery rental, and the like) plus your overhead (cost of sales, buildings and grounds, equipment expenses, administrative expenses, insurance, utilities, and the like).

It is fairly easy to calculate the materials costs. Except that if you don't do a good job in project execution, you may have to buy more. Rework can eat up your profit very quickly. Yield is also a key factor. If you don't get as many parts as you expect, you waste material which frequently cannot be recovered. When materials are heavy or bulky or cannot be locally sourced, then shipping expenses become a major component of the cost of your materials.

The single biggest problem in labor costing is not recognizing that an employee's wage is just one component of his cost. You must also pay the employers component of social security taxes, Medicare taxes, unemployment taxes, and workers compensation insurance. If overtime is needed, their base wage is increased 50%. But this is rarely taken into consideration when pricing strategies are created. Benefits packages are another major component of costs that are easily overlooked.

But how much an employee costs you is further exacerbated by the fact that you employees are never 100% productive. Paid vacations and holidays represent time where employees are paid but don't produce anything. Sick days, funerals, and other similar events reduce the time that an employee spends on the job without necessarily reducing your expenses. Finally, even the time they spend on the job is not 100% productive. Coffee breaks, lunches, and administrative time can reduce an employee's effective work day by a half hour to 2 hours a day.

In the end, your true cost per hour is the sum of all of the costs for that employee over the course of a year divided by the number of hours of actual production that he produces. This is an employee's burdened labor rate. The burdened labor rate for an employee can easily exceed his base wage by 35% or more.

Other expenses are usually pretty straight forward. They are usually pass through expenses. But like all expenses they must be identified and accounted for.

The place where most companies fall short is overhead allocation. Overhead is a hidden expense to most jobs because they are simply ignored. Companies mark up their materials by x% and labor by y% and other costs by z%. All of those mark ups across all of the project for the year are expected to produce enough margin that we will make money after overhead expenses are taken out. This approach is all well and good if it actually happens.

But the trouble is that virtually no one knows how much overhead they need to capture on each job in order to cover all of the overhead by the end of the year.

Overhead allocation is the ratio between overhead costs that a profit center must carry in order for the company to make a living and the cost of goods sold for that profit center. It becomes a mark up percentage which recognizes that for every dollar of cost incurred by a project, you also have to cover $n of overhead. In capital intensive environments, the cost of overhead can easily exceed the variable costs of a job. When you include this factor in your job cost, you get the breakeven point of given job. You need to charge at least this amount simply to break even on an individual job.

But the company also needs to make a profit and you do this one job at a time. If you want to make 15% profit before taxes, then you need to average 15% profit margin on each job. Thus you engineer a profit by dividing the breakeven point by .85 (100%-15%). This is the minimum acceptable sale price.

It really doesn't matter how you come to the price that you charge your customers. Again, this is the black art of selling. However, it does matter that the price you sell the job for is higher than the minimum acceptable sale price. It is also absolutely critical to know this number because customers always push back. Calculating the minimum acceptable sale price sets the floor for your negotiations.

You only go below that point as a conscious decision based on good business logic knowing that you will need to make up the difference in profit on another job to cover the shortfall on this project.

Poor Record Keeping

Poor record keeping is a corollary to the first two problems. Documentation is generally the first casualty when shortcuts are taken to be able to handle the load. Since it is all being kept in your head and you are the only one who needs to know it, you don't need to write it down. The trouble is that human brain isn't foolproof.

Failure to record important information means that there is no paper trail. You can't go back to determine that key activities occurred in a timely fashion. You also don't have the records needed to resolve potential disputes. Finally, you don't have the data to compare planned vs. actual results. And it starts at the estimating process. If you didn't do a formal costing process, how do you determine whether a project came in on budget or not?

Cause of Poor Record Keeping

Poor record keeping is simply a matter of poor processes. If your business process doesn't include documentation, it is a flawed process. But probably more interesting is the "why" question which gets to the root cause. As mentioned earlier, the first casualty of time constraints is usually documentation.

A second and more subtle issue is the subconscious desire to avoid accountability. It is basic human nature. We have an innate tendency to want to assess blame when things go wrong and an equally great desire to avoid having to answer to mistakes. It started in the Garden of Eden when Adam blamed Eve and Eve blamed the serpent. If you don't write it down no one can prove that you were wrong. If things go well you simply remind your coworkers that you got it right. And if things go wrong there is no proof that it was you.

Solution for Poor Record Keeping

First and foremost remember that "Policy is your Friend". Make sure that all processes include a documentation phase and that policy is followed as a matter of course.

Second, make sure that documentation is not primarily used as a stick to punish. Only a very small percentage of employees are deliberately trying to duck responsibility. The vast majority are trying to do a good job. Documentation is simply a way of measuring what a good job is. No one is perfect, documentation helps us to identify where we need to improve. This is covered in depth in the next section.

No Post Mortems

Another casualty of lack of time is variance analysis. But it is one of the key reasons why you keep records in the first place. Being able to go back to look at history is critical.

"The best predictor of future performance is past performance."

I learned this on my first day of my MBA classes. It has stuck with me ever since. One of the key corollaries is that if you don't like what you got and you don't do something to change it, you are bound to get it again as history repeats itself. Conversely, if you did get something you liked and you don't work to institutionalize it, you may be looking at a one-time event.

Post mortems are the key to accomplish this. Post mortems are simply reviews after the fact of what went right and what went wrong in a job. Done properly post mortems are done in the spirit of incremental improvement not to assess blame for shortfalls.

Cause of No Post Mortems

Like poor record keeping, few people want to have their shortcomings paraded for public display. They would much rather have them quietly disappear.

When time is tight, it is even easier to let them slip.

Solution for No Post Mortems

Like documentation, post mortems should be policy. If not on every job, they should at least be done on jobs that fit a certain profile. This may mean, jobs that varied from budget by a certain percentage. If they were over budget, we must determine where the overruns occurred, why they occurred in order to determine how to prevent it from happening again in the future.

If they were under budget, we want to find out why again. Was it serendipity or can we repeat it again in the future. If we can institutionalize things that work, then we can improve performance across the board.

It also makes sense to analyze a sampling of jobs that met budget to see if there is any way to improve the process in the future.

But the key to successful post mortems is to avoid assessing blame. Good post mortems are about improving processes. By focusing on improving processes, you can avoid the emotional component of individual performance. Again, the key is to recognize that the vast majority of employees want to do a good job. If you approach post mortems from the standpoint of improving the next time, then people will be much more willing to go through the process. In many ways, you become a coach whose interest is developing his players. Everyone wants to be a winner. If you take the losses as an opportunity to learn, you will see better performance in the future.

But interestingly you will also see better performance now as well. It shouldn't be surprising that people want to report on their successes. If there is a forum for displaying their successes, you will find that your people will work harder to make sure that what they have to report is positive.

Lack of Accountability

Another common problem in many companies is the lack of accountability. Having just spent time talking about not assessing blame, that doesn't mean that people are not held accountable for their performance. If you continue to pass over consistent shortcomings, you are not helping that person to improve.

Humans don't like change. Improvements, however, are by definition change. The key is to make improvements in the best interest of the employee.

Cause of Lack of Accountability

Frequently, this is the result of management that does not like confrontation. They don't want to make waves or they want their employees to like them or they are afraid that if they bring up an issue, the employee will quit and leave them in a bind.

Another common cause is centered on the fact that there isn't any real data to base an assessment on. You just don't *feel* that an individual is doing a good job but you have no facts to back up your gut instincts. Or you know that the person isn't doing a good job but you have no data to quantify its effect.

Solution for Lack of Accountability

You need to recognize that staying the same cannot be an option. If your employee is not performing, you need to correct it. Remember that the best predictor of future performance is past performance and if you don't like what you are getting, then you better change something or else you will see history repeating itself.

You have to bite the bullet and risk offense to hold people accountable. Here, how you approach it makes all the difference in the world.

Base every thing on **FACTS**. This is one of the reasons why you need to document processes. It is a lot easier to deal with someone when the discussion is about facts. The measurement criteria must be recognized by both parties as a legitimate measurement of performance. A salesperson has a sales quota at a profit margin. Did he reach his sales goal or not? The only question will be "Is the quota reasonable?" A machine operator is given a task that takes 1 hour to perform. Did he get it done in the prescribed time? By working from facts that both parties recognize are appropriate and reasonable, you remove much of the emotion from the process. Nobody likes being called to task for shortcomings but not achieving against a standard is a pill that is much easier to swallow than saying "I don't think you are not doing a good job".

The other key to successful accountability enforcement is your attitude. We are seeking a win-win relationship. Improved performance is certainly in the best interest of the company. Incentive plans are a key to improved performance. It is a matter of carrot and stick. While you still need to keep the stick around in terms of discipline, improved performance is best realized when it is 85% carrot and only 15% stick. Then improved performance becomes in the best interest of the employee as well as the company.

The key to a good incentive plan is to make sure that while measuring and rewarding the behaviors that are good for the company, you do not at the same time encourage dysfunctional behavior. The classic example involves salespersons who are rewarded simply on sales without regard for profit. A salesperson will discount all of the profit out of a job in order to close it. He reaches his quota and makes his bonuses but the company loses money.

Inconsistent Processes

A common problem that results from improper delegation is inconsistent processes. When every employee is given free reign to do their job as they see fit, you will inevitably end up with inconsistent performance. People will do what feels best or what is expedient.

As a result, each person develops his own approach to a common business process. While it may seem logical to the individual, it is usually localized. That is the process works for the individual but it may not necessarily be good for the overall operation.

Without harping on sales, if one estimator uses one pricing strategy and a second estimator has his own pricing approach, what will happen when that person is on vacation and the first salesperson creates a bid for one of the second person's customers.

Another outcome of inconsistent processes is poor communications and coordination. When standard procedures don't exist, each event requires developing a separate approach to handle passing control to the next process and communications is tailored on a case by case basis.

Cause of Inconsistent Processes

The base cause of inconsistent processes is lack of standardization.

Solution for Inconsistent Processes

One of the keys to management by exception is documented standard process flows for all key business processes.

Every business process must be examined holistically. Processes must flow cleanly from one stage to the next. Clear roles, responsibilities, and information requirements must be determined and people trained to perform them. When multiple people perform the same task, they must collect the same information, perform the same tasks, provide the same work products and hand off to the next person in the chain in the same fashion.

When processes are dependable, it is a lot easier to determine the status of a project throughout its life cycle. Problems are identified earlier and corrective action taken faster. And mistakes are minimized because a well thought out process is virtually always more comprehensive. Finally, key steps (like invoicing) don't fall through the cracks.

Two real benefits are that accountability is intrinsically built in and when a post mortem improves a process, it improves that process across the board.

Lack of Urgency

The old cliché goes:

> "There is never enough time to do it right but always enough time to do it over."

Every day the opportunity arises to fix a problem. But because of time pressures, it is put off until tomorrow. Virtually every problem discussed previously is perpetuated because there wasn't an urgency to fix it.

I have heard it said that the definition of complacent management is the tolerance of a problem beyond the point of discovery. Complacency in management has a devastating byproduct – indifference by your employees. If management doesn't care, why should the employees. Indifference once entrenched in your employees is a very hard attitude to break and it tends to spread into all areas of performance including your customer service. We all know what effect indifference toward your customers has on sales.

Cause of Lack of Urgency

In general, the root cause of lack of urgency is the belief that the problem isn't that big and that it will take care of itself. Consistently, I find that my clients simply were not aware of just how much a problem is costing them in terms of operational efficiency. They may or may not know of its impact on customer satisfaction. And they virtually never have quantified a problem's impact on their bottom line. Because if they had truly understood its effect on an organization, they would never have let a problem fester for any period of time.

Solution for Lack of Urgency

You need to develop a "bias for action". But not just any action.

Start by identifying the problem. Sometimes the surface problem is only masking the root cause. Surface examinations result in Band-Aid type resolutions. A Band-Aid may address the immediate problem but you need to get to the source to effect long-term improvement.

Then, quantify the effect of the problem. This is a critical step because it identifies just how big a problem is. It helps to prioritize the problems and to set a budget on how much time, effort, and money you are willing to spend on a solution. Remember, that if you are not funding the solution, you are funding the problem. If you have determined that a problem is costing you $100,000 per year, doesn't it make sense to dedicate $50,000 to fix it?

Next, examine alternatives. There is rarely only one way to solve a problem. You have to consider all of the alternatives recognizing the resources that you have at your disposal and the impediments to effectively implementing the solution. You also have to consider the hidden effects of a solution. Some times a solution in one area creates other problems elsewhere. You need to make sure that the cure in not worse than the disease.

Finally, prioritize and implement. There are always an infinite number of tasks to do and a finite set of resources. You cannot do everything. But you can do what you can do. Once you have identified the solution, put it in the queue to fix it. The highest priority tasks take precedence. Direct resources to fix your problems in the order that has the greatest impact on the company. Prioritizing is proactive and the 80/20 rule applies universally. 80% of your improvements will come from addressing 20% of your problems. Just don't put off until tomorrow what you can do today.

Lack of Strategic Planning

Most entrepreneurs had an idea of what they wanted to accomplish when they went into business. Some may have even written a business plan. But it was generally aimed at getting bank financing. If a business plan exists, it rarely was comprehensive and certainly has never been updated.

For most companies, business is what happens. They have customers that they do their best to satisfy. They go with the flow and take what the get. But, is what they get what they want? Is the flow taking them where they want to go?

A strategic plan is a vision of where you want to be in 5 years. With that kind of horizon, you can get to almost anywhere. A $10 million company can become a $100 million company in that time – if the management wants it to happen and takes the steps to get there.

Cause of Lack of Strategic Planning

It is a recurring theme, but many companies are so busy just staying where they are that they don't make time to concentrate on where they want to be. In so many companies, strategic planning is measured in months if not weeks.

Besides, they are so busy servicing the business that they are currently doing that they don't need to plan. And they think that they don't have any control over the process. Because of this, they will take any business that comes their way without really questioning it. In the end, creating a strategic plan seems an exercise in futility.

Solution for Lack of Strategic Planning

There is simply no other way to do strategic planning than to simply carve out the time to do it. But its effect will be dramatic. Without a plan, you are simply being blown around by the winds of the market. You take what you can get and are happy that you have it. But if you have a plan you take those same market winds and use them to position your company where you want to go.

The process starts with setting a vision for the company. Why does the company exist in the first place? It can't simply be about making money. If that were the sole goal of the company, you could become drug dealers or run a chain of brothels. There was a reason for choosing to be in the business you chose. What was it? Where do you want to take your company?

Once you have a vision, create some goals. Goals are different from a vision in that they are quantifiable and they have a date assigned to them. If you are to achieve your vision, where can you get to in 5 years? In order to be there, where do you need to be in 3 years? In 2 years? And this time next year?

Then you need to determine what you have to do to get to each of those goals. This is tactical planning and frankly is the sanity check to your strategic goals. If you can't envision a way to get to a goal, then it probably is unattainable and needs to be rethought. But any reasonable goal can be achieved if you are proactive and take the steps it takes to get there.

The key is to recognize that a strategic plan must be a living document. Stuff happens that will affect your achieving your goals. Some times, they are expeditious, helping you to get there faster. Other times, they present road blocks that you need to get around.

I like to compare strategic planning to the pioneers on the Oregon Trail. They had a limited time to get across the prairie. And they had a limited budget. They couldn't pack everything they needed for the trip in their wagon. So they had to live off the land as they went. They had problems. Oxen needed care. Wagon wheels were broken. Rivers needed to be crossed. Weather presented challenges. But, regardless, they had to make 25 miles of progress every day toward Oregon or they were not going to make it through the mountains before winter.

In business, markets change. Key personnel leave. Equipment needs to be repaired. Customers come and go. Workloads can be feast or famine. But you must find a way to make progress against your goals.

Even if things don't happen in the timeframe that you envisioned, you will certainly be further along than if you simply let circumstances dictate where you end up.

Conclusion

In stating these problems, I realize that I am leaving myself open to some level of criticism that I am missing some. Every company adds unique issues to the mix and every company brings a unique spin to each problem. However, I have found these eight are universal to virtually every company.

Clearly, the causes are sometimes simplistic and don't capture the full story. And I haven't gone into great detail on the solutions. Waving a magic wand and chanting "Employee Accountability" will not magically correct these problems. It took years to get into the fix that most entrepreneurs find themselves and the problems will not disappear overnight. It takes work and time to change but the effort is worthwhile and if institutionalizes will create a permanent improvement. Once all processes are in place, then the company settles to a continuous improvement state where modifications are made as needed to address changes in the business environment. The forward looking nature of strategic planning will tend to identify problems while they are still small and small adjustments can be made to correct them.

