

# PERSPECTIVES ON THE CONSTRUCTION INDUSTRY



*Certified Public Accountants*

26 Computer Drive West, Albany, NY 12205

Tel: 518-459-6700/800-724-6700

[www.bstco.com](http://www.bstco.com)

Fall 2011

## The Value of Benchmarking

It may seem easy to figure out how well your company is doing — you just look at whether or not you made a profit this month or this quarter. But you need to dig deeper if your profits are erratic or not at the level you'd like or expect them to be. You need a way to measure your business's performance in key areas and to identify areas that can be improved.

with other contractors who might be interested in swapping information. And look into joining national industry and trade associations so you can access the financial and surety data they collect from their members every year.

### Financial Benchmarking

This is a critical area for measurement

- ✓ Backlog ratios let you know how long it will take to complete work under contract.
- ✓ Asset utilization ratios, such as a fixed asset ratio, measure how efficiently your company is using its assets.
- ✓ Debt utilization ratios help your business measure its liabilities in relation to its earnings ability and asset base.

**"The data and insights gained from this type of performance benchmarking exercise can be invaluable."**

For starters, you can compare current and past performance to identify trends. Another approach: Compare key metrics with those of successful construction firms of a similar size. The data and insights gained from this type of performance benchmarking exercise can be invaluable.

### Obtaining Data

Use credible data from similar sized companies within your geographic region for your analysis. Choose an industry group source — generally based on NAICS code — that best represents your business. Attending regional or state trade meetings can put you in contact

since access to bonding and credit will depend on your business's financial health. Important metrics include:

- ✓ Profitability ratios, such as gross profit margin, return on assets, and return on equity.
- ✓ Liquidity ratios, such as the current ratio, which measures your firm's ability to pay off short-term obligations as they become due.
- ✓ Underbilling ratios, such as the underbillings to equity ratio, which measures the percentage of your business's net worth represented by work performed but not yet billed.

You can also look at metrics such as gross profit per project manager to identify areas where employees may need additional coaching and training.

### Operational Benchmarks

This generally includes everything from staffing and productivity to office flow and analysis of procedures performed. Potential areas for analysis and comparison include:

- ✓ Job site accidents
- ✓ Number of change orders
- ✓ Productivity levels per employee

There are other areas in which comparing your company's performance with that of a competitor can be helpful. For example, look into sales and marketing issues and your firm's fuel and energy use.

If you would like advice and input on the most effective way to benchmark your company's performance, please call us. We can help you set up systems that will capture the data critical to your growth. ✓

# Use Caution When Classifying Workers

The construction industry has traditionally relied on a work force composed of full-time workers and independent contractors. Companies are generally required to withhold income taxes, withhold and pay FICA (Social Security and Medicare) taxes, and pay unemployment taxes on an employee's wages. However, these obligations generally don't exist when it comes to payments made to independent contractors.

Now, in an effort to capture delinquent taxes, the IRS is ratcheting up the pressure on taxpayers who misclassify employees as independent contractors. The IRS recently launched an audit initiative known as the National Research Project (NRP). NRP is randomly selecting 2,000 taxpayers for employment-tax examinations in 2011 and 2012. The audits are designed to measure compliance with employment-tax law and related reporting requirements and will also help the IRS select and audit future returns considered the greatest compliance risk.

To be on the safe side, you should familiarize yourself with certain factors the IRS reviews in determining whether a worker should be classified as an employee or as an independent contractor. Analysis of the entire relationship needs to be made. Important factors that provide evidence of the degree of control and independence fall into three categories:

## Type of Relationship

The independent contractor's services are typically for separate and distinct projects. However, employees also may be hired on a seasonal or project basis. What are the facts that show how the worker and business perceive their relationship? The permanency of the relationship, the existence of a written contract, the provision of employee benefits, and whether the services provided are considered a key activity of the business are factors to weigh.

## Behavioral Factors

Independent contractors are generally not

under the direct supervision and control of the business and do not receive detailed instructions about how work is to be performed. In short, the extent to which a business directs and controls what a worker does and how it is done is critical.

## Financial Matters

How the worker is paid, whether expenses are reimbursed, and whether the business or the worker provides tools and supplies are all important financial factors to be considered.

If you are still uncertain as to a worker's classification after weighing several factors in the three main categories, you can file Form SS-8, *Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*. The IRS will review the information and make an official determination.

If you need help in ensuring that your firm correctly classifies employees and independent contractors, please give us a call. ✓

# Recycle, Reuse, Boost Profits

Many contractors are literally leaving money on the ground when they don't recycle the waste materials their projects generate. Scrap concrete, wood, metals, glass, asphalt, and plastic can all be sold to recyclers. Asphalt and concrete can be recycled into aggregate or new asphalt and concrete products, while wood waste can be turned into composite decking or furniture. Recycling reduces the waste stream and has a positive environmental impact. It's a win-win situation for contractors and for the communities they do business in.

The financial — and other — advantages for contractors that recycle their waste materials are numerous. If you recycle, you can:

✓ Add to your firm's bottom line since a healthy market exists for scrap metal,

such as steel conduit pipe, rolls of wire, and HVAC materials.

**"Scrap concrete, wood, metals, glass, asphalt, and plastic can all be sold to recyclers."**

✓ Reduce the costs normally associated with hiring a haulage company to remove and dispose of worksite construction and demolition materials.

✓ Help lessen the burden on your region's landfills and reduce the environmental impact of creating new construction materials.

Just be sure you work with a recycler who is licensed by the proper local and state authorities and who will ensure that all materials are disposed of properly.

## Get Started

The Environmental Protection Agency's website ([www.epa.gov](http://www.epa.gov)) is a good resource if you are interested in learning more about reducing and recycling your construction and demolition materials. Your local builder's association, county solid waste department, or state environmental agency can give you information about certified and licensed recyclers and waste haulers in your area. ✓

# Obtaining Bonding in Difficult Economic Times

Contractors need bonding to work on many projects. Unfortunately, obtaining bonding is never a sure thing. Long-established contractors, as well as new and emerging contractors, are being asked by surety companies to meet more stringent requirements in order to get bonding. Before underwriting their projects, surety companies want contractors to provide detailed business plans, regularly updated financial statements prepared by CPA firms, and information on contract terms and conditions.

It's critical that contractors take the time to carefully prepare and gather data well ahead of any meetings with underwriters. While contractors may be bidding on fewer large projects than in the past, they have to be forward looking and ready

**"Underwriters generally require evidence that your business is in good financial health."**

to capitalize on the increased demand that often appears following the end of a recession. Here are some factors you should focus on when preparing an application for surety bonding.

## **A Strong Balance Sheet**

Underwriters generally require evidence that your business is in good financial health. They want certain assurances that it has the financial strength to undertake any project it is bidding on. One way they'll assess the strength of your balance sheet is by looking at the adequacy of your working capital. That means they'll examine the current ratio and the quick ratio. The current ratio is the amount of current assets divided by current liabilities. The quick ratio is the amount of cash, cash equivalents, and receivables divided by current liabilities — an indicator of your company's short-term liquidity.

Sureties will also look at the age of your accounts receivable to see if they may present problems in the future. Your firm's capitalization and debt will also be reviewed. Too little capital and excessive debt are warning signs to a surety that your balance sheet is unhealthy. Under-billings are another area that a surety will examine closely. High levels of under-billings can indicate that you are experiencing problems on one or more jobs.

## **Operational Strengths**

Sureties will want to know if your business is capable of handling the types of jobs it plans to bid on. It will look at prior projects to see if your business has the experience to complete the requirements of the to-be-bid-on contract.

In addition, you will have to provide evidence that you have the equipment and manpower to do the work.

## **Established Banking Relationships**

Another important factor sureties will focus on is whether your business has an established banking relationship. If applicable, be certain to let sureties know that your business has a sufficient line of credit and an excellent credit history.

## **Updated Business Plan**

A business plan helps your business define its goals, clarifies the steps you need to take to reach those goals, and provides markers along the way to help you measure your progress. Most sureties will want to review your business plan before they will consider underwriting a bond. That's why it's important that your business plan be reviewed yearly and updated when you hire key personnel.

## **Other Requirements**

Sureties are requiring more detailed information than in the past. Be prepared to be asked to supply information on:

- ✓ Your personal finances
- ✓ Any transactions between related parties
- ✓ The existence of a formalized continuity plan
- ✓ Employee turnover rates
- ✓ Any non-bonded work you plan to bid on

You can increase your chance of obtaining the bonding you need by putting effective financial reporting procedures in place. We can help in this and in numerous other areas. Please call us if you need assistance. ✓

Check out [www.sba.gov](http://www.sba.gov) to learn more about the two U.S. Small Business Administration Surety Bond Guarantee Programs. You'll find information on the small business eligibility requirements, the bond guarantee application process, and bond guarantee fees.

The general information in this publication is not intended to be nor should it be treated as tax, legal, or accounting advice. Additional issues could exist that would affect the tax treatment of a specific transaction and, therefore, taxpayers should seek advice from an independent tax advisor based on their particular circumstances before acting on any information presented. This information is not intended to be nor can it be used by any taxpayer for the purpose of avoiding tax penalties.

# BST



*Certified Public Accountants*  
26 Computer Drive West, Albany, NY 12205

ADDRESS SERVICE REQUESTED

Presorted STD  
U.S. Postage  
**PAID**  
Albany, NY  
Permit No. 700

## Developments in Tax and Business

### **Home Ownership Still the American Dream**

Almost three quarters (73%) of people who do not currently own a home say owning a home is one of their goals. Moreover, 75% of those polled said that owning a home is worth the risk of market fluctuations, according to a survey conducted by Public Opinion Strategies and Lake Research Partners on behalf of the National Association of Home Builders.

### **Benefits as a Percentage of Payroll Costs**

How do your firm's numbers compare to the national averages for wages and employee benefits? Employer costs for employee benefits provided to American workers in March 2011 averaged \$9.15 per hour worked and accounted for 30.4%

of total employee compensation costs, according to data released by the U.S. Department of Labor's Bureau of Labor Statistics. Wages and salaries in 2011 averaged \$20.91 per hour and accounted for 69.6% of total employee compensation. The data measured nonfarm private and state and local government workers.

### **Job Creation in Small Companies**

Small companies have traditionally been the engine of job creation in the U.S. However, economic uncertainty is holding back many small employers from investing in new employees, according to a survey conducted by the U.S. Chamber of Commerce. The survey found that 79% of small employers surveyed said that taxation, regulation, and legislation make it harder for them to increase hiring. ✓

### **Can We Serve You?**

Our firm provides a broad range of accounting, auditing, tax, employee benefit, and management consulting services to contractors.

Copyright © 2011

CON