When starting a business, one of the first recommended steps is creating an overall financial budget for the company. And perhaps you did that when you established your construction company. But in the hustle and bustle of moving from one project to the next, you may have let your budget slip onto the back burner or out of sight completely. If so, now is a good time to start rebuilding your budget from the ground up. Why? Because today’s fragile economy has made managing revenue and cash flow more important than ever.

Look at your income

To get started, first look at your income statement to analyze your sales, margins, operating expenses, and profits or losses. If times have been tough, you may not even want to know how little income you’re pulling in, but it’s important to look at the specific numbers.

Once you do look at the income statement, however, your natural tendency may be to get hung up on it — particularly if your construction company is showing a profit. Yet bear in mind that this part of your budget doesn’t reflect cash-related activities such as buying new equipment or borrowing money from the bank. Just because your business appears profitable now doesn’t mean it’s out of the woods, because the cash you’ve earned may be dangerously tied up in other financial assets or obligations.

An important number to focus on from an overall budgetary standpoint is your gross profit margin. If your margin is declining, you may need to adjust or increase your contract revenues or try to lower your contract costs.

Check your cash flow

In today’s cash-conscious economy, the center point of your budget is surely the cash flow statement. It begins where the income statement leaves off — with your net income. From there, the cash flow statement is typically divided into three subsections:

1. Operating (activities associated with running the business),
2. Investing (activities associated with growing the business), and
3. Financing (activities associated with obtaining money).

Cash flow is important for any business, but construction companies can all too easily be undone by a lack of available dollars at critical times. So your budget needs to account for cash flow at the time you re-establish your budget as well as your projected cash flow for the coming year.
To integrate a cash flow projection into your budget, take your current and anticipated projects and estimate your expected revenue by month. Naturally, predicting exactly when cash will come in is tricky — especially if you’re working with an unfamiliar project owner or undertaking a spec job. But you can use your historical payment data to calculate an average for planning purposes.

Bring in your balance sheet

With your income and cash flow down on paper, a third critical aspect of your budget is the balance sheet. Think of it as a snapshot of your construction company’s financial condition on a given date. The balance sheet usually lists assets, liabilities and shareholders’ equity. Elements such as these can help you realistically shape your budget going forward.

For instance, if your balance sheet shows a substantial amount of debt, you’ll likely need to curtail discretionary expenses (such as company parties) in your budget. You can also use your balance sheet to calculate your debt-to-asset ratio. It can tell you how many of your assets (heavy equipment, office technology) are owned by your lender(s) and how this could impede your budget for the year.

Lay the foundation

Think of the three elements discussed above — income statement, cash flow statement and balance sheet — as the foundation of your budget. Work with your CPA to generate these documents and you’ll have the basis for a solid plan of attack for the coming year (or whatever time frame to which you’d like to apply your budget).

Of course, there are other elements you might include in your budget, such as your mission statement and an executive summary. But if, like many contractors, you’ve gotten away from budgeting in recent years, it’s probably best to start with the basics and work up from there.

An idea for staying within budget: Pay-for-performance

It’s one thing to create a budget (see main article), another to stay within its parameters. One expense that often drives up a contractor’s budget is labor costs. If your workers are leaving the job site early or working inefficiently while they’re there, even the soundest budget can become unattainable.

One way to keep your labor costs in line is to switch to a pay-for-performance model for some or all of your employees. Under this compensation paradigm, a worker’s pay comprises a base component set by what the competitive market pays for a comparable position (factoring in skills and experience) and a variable component determined by whether and how well he or she meets specific goals.

For construction companies, pay-for-performance can motivate workers to keep up with ambitious job schedules while creating clear accountability for what you’re trying to accomplish on each project. It can also help weed out unmotivated workers who hang around job sites putting in a bare minimum of work and looking for ways to cut corners.

Of course, there are risks to consider. Some workers may feel that the pay-for-performance model pits team members against each other. This may foster unrest and poor morale on job sites. In addition, employees may work more sloppily to beat deadlines and, thereby, qualify for incentives.

To mitigate these dangers, you’ll need to design variable components that trigger performance pay specifically to each project role or phase based on reasonable scheduling and including quality checks. In addition, you might provide some performance pay on a team basis, rather than just on an individual basis.
In these uncertain economic times, many construction projects have been put on hold — sometimes indefinitely and other times for a relatively short duration. If you find yourself in such a predicament, here are four steps to stopping and restarting a project effectively:

1. Demobilize in an organized manner. When a job shuts down, you may rush your people, materials and equipment off site, leaving any existing project elements exposed to the weather. This could lead to safety concerns and increased work time when the job restarts.

   Instead, create a formal demobilization plan that outlines withdrawal procedures, names those responsible for the removal of assets and materials, and mandates the inspection of existing job elements. Also look into negotiating with the project owner to allow you to perform compensated work to stabilize the job site.

   You may want to remove signage reflecting your company’s logo to prevent bad PR.

2. Secure the project. The weather isn’t the only thing that could damage a dormant job site. Thieves and vandals could seize the opportunity to take or destroy elements that are in place, again creating safety pitfalls and additional work should the project restart. Minimal or no security measures could also allow children (or others) to wander on-site and into harm’s way.

   Your first defense against intruders is proper fencing. Be sure the job site is completely closed off with stable fencing, secure gates and plenty of warning signs. (On a related note, you may want to remove signage reflecting your company’s logo to prevent bad PR.) In addition, consider fire protection measures if remaining elements could be set alight.

3. Check your insurance. One of the biggest challenges of a stopped job doesn’t happen on-site but back at the office. That is, you’ll need to ensure that your insurance is both in effect and effective.

   If you’re participating in an owner-controlled insurance program, check with the owner about whether it intends to continue coverage. You may need to contact your own broker to negotiate...
Health care reform

What the new law could mean for contractors

The health care reform debate went on for so long that you may have given up on following the details. Of course, on March 23, the details were finalized when the president signed into law the Patient Protection and Affordable Care Act (PPACA). Let’s take a look at some of PPACA’s major business-related provisions and how the act may affect the construction industry.

Points to know

First things first, the new law doesn’t require contractors to provide health care coverage. Beginning in 2014, however, it will impose tax penalties on certain employers that don’t provide it.

Namely, employers with 50 or more “full-time-equivalent workers” (FTEs) that don’t offer coverage and have at least one full-time employee who receives a health care premium tax credit (a new break under PPACA for certain individuals who buy coverage themselves) will be subject to an annual fee of $2,000 per FTE (not including the first 30 FTEs). An FTE is defined as an individual who works 30 or more hours weekly, excluding full-time seasonal employees who work less than 120 days a year. Clearly, this would affect larger construction companies more than smaller ones.

There is some immediate good news for smaller contractors, too. Beginning in 2010, eligible small businesses may qualify for tax credits for buying group health coverage.

For tax years 2010 to 2013, the maximum credit is 35%, provided the employer contributes at least...
50% of the total premium or 50% of a benchmark premium. In 2014, a maximum credit of 50% will be available for two years for employers that buy coverage through a state exchange and contribute at least 50% of the total premium.

The rules governing what businesses qualify as “small” and whether a business is eligible for the maximum credit or a partial credit are complex. So check with your financial and benefits advisors for details.

**Effect on the industry**

Owners of construction businesses with fewer than 50 employees could conceivably drop their health insurance benefits, lowering their operational costs and perhaps enabling them to better compete with larger construction companies. But such a move appears dubious because eliminating health care benefits could estrange employees and even lead to mass defections. Plus, many construction bids are won based on expertise rather than costs.

Regarding the work opportunities PPACA may bring, those remain uncertain as well. If health care use grows as more people are covered, medical organizations may expand their facilities. But many of the newly covered may turn out to be relatively healthy young adults, which could curb demand for new projects.

Still, in an official statement released soon after PPACA’s signing, the Associated General Contractors of America stated, “It seems likely that health care construction will rise initially.” Keep an eye on this locally if your construction company is a good fit for such jobs.

**HIRE is still HERE**

Signed just before the health care reform law, the Hiring Incentives to Restore Employment (HIRE) Act may have gotten lost in the shuffle. But at the center of the act are two valuable incentives for hiring and retaining workers:

1. **Payroll tax forgiveness.** This provision essentially exempts qualified employers (including contractors) from having to pay the 6.2% Social Security portion of Federal Insurance Contributions Act (FICA) taxes through year end on certain new hires who were unemployed. Various limitations apply.

2. **Tax credit for retention.** The HIRE act offers a tax credit for retaining for 52 consecutive weeks workers who qualified for payroll tax forgiveness. The tax savings per worker are the lesser of 6.2% of the wages paid to the worker in 2010 or $1,000.

Your tax advisor can explain the finer points of the HIRE act and how it might benefit your construction company.

**An evolving situation**

PPACA is a big law with many details. Be sure to revisit this topic regularly with your financial and benefits advisors to be sure you’re up to speed on what’s required of you and how you might turn health care reform to your advantage.
The Contractor’s Corner

Managing the risks of green building

There’s nothing particularly new about environmentally friendly construction. But some contractors still see certain risks and are hesitant to throw their hardhats into the ring of flowers. So what exactly are the risks of green building? Here are a few to consider — along with some tips on how to mitigate them.

Cost uncertainties
Among the most significant risks to green construction has been cost. And the initial cost of a sustainable project can be higher than that of a conventional one.

This has been changing, however, as the popularity of sustainable components is driving down their costs. Today, the first cost of a sustainable building is often the same as or lower than that of a traditional structure. Much depends on establishing an efficient and trustworthy procurement system.

Design confusion
If sustainable building elements are added to a project during construction, it can create confusion and conflict. Why? Because those elements may not add up to what’s stipulated in the contract. Thus, significant green efforts must begin at the design stage to be cost-effective.

If you begin working with the owner and architect early in the process, you can collaborate on how to structure the building envelope and HVAC systems to take maximum advantage of the climate and positioning of the building. Increased use of south-facing windows for natural light may, for example, help lower heating costs in Maine but drive up cooling costs in New Mexico.

Certification challenges
Establishing your construction company’s green reputation will likely call for obtaining Leadership in Energy and Environmental Design (LEED) certification. LEED is the most widely recognized measure of excellence in sustainable construction, both for buildings and for the professionals who design and build them. Because LEED building accreditation is based on a point system, having LEED-certified employees on staff can help ensure you don’t lose points because you didn’t follow required procedures.

So what’s the risk? Well, learning LEED requirements and how to adapt them to your construction company’s procedures will take much time and effort. And all this could go to waste if your workforce doesn’t follow through on the sustainable plan. Getting a project certified will also take extra time out of your schedule.

It’s game on
So is your construction company game for a sustainable project? In our current, fragile economy, it’s likely not easy to turn down any jobs. But that doesn’t mean you should jump at any green project that comes along, because sustainable building does have its risks. Then again, this is one approach to construction that’s probably not going away.
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