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CONSTRUCTION INDUSTRY ADVISOR

A collection of brief topics relevant to people and businesses that operate within the construction sector, brought to you by

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The Consolidated Appropriations Act was signed into law on December 27, 2020, providing relief to individuals and businesses affected by the COVID-19 pandemic. In addition to reducing 2020 tax bills, the act provides several tax benefits for 2021. This article covers highlights that contractors should know about. A sidebar notes that expenses paid with Paycheck Protection Program loan proceeds are deductible.

Tax planning - Don't forget about the CAA

Remember the Consolidated Appropriations Act (CAA)? It was signed into law on December 27, 2020, providing relief to individuals and businesses affected by the COVID-19 pandemic. In addition to reducing 2020 tax bills, the act provides several tax benefits for 2021, so be sure to keep it in mind as the year rolls along. Here are some highlights that contractors should know about.

PPP loans expanded

The CAA permitted eligible small businesses that received forgivable Paycheck Protection Program (PPP) loans last year to apply for a "second draw" loan by March 31, 2021. The act also opened the program to first-time PPP applicants, who could apply for loans by that same date. The federal government announced the availability of even more PPP funding for forgivable loans to eligible businesses under the American Rescue Plan Act (ARPA), signed into law in March.

The CAA expanded the ways borrowers may use PPP loan proceeds without jeopardizing their eligibility for loan forgiveness. Under previous law, to qualify for loan forgiveness, at least 60% of PPP loan funds had to go toward payroll expenses, while the remaining 40% could be used for mortgage, rent or utilities. Now, borrowers may also use that 40% for:

- "Covered operations expenditures," such as software or cloud computing services,
- "Covered property damage costs" — that is, unreimbursed costs related to vandalism or looting in connection with public disturbances in 2020,
- "Covered supplier costs" for goods that are essential to operations and meet certain requirements, and
- "Covered worker protection expenditures" — that is, costs incurred to comply with health guidelines, such as expenses for personal protective equipment, physical barriers or air filtration systems.

Furthermore, the CAA clarified that payroll costs, for purposes of meeting the PPP's 60% requirement, includes employer-provided group life, dental, vision or disability insurance. In addition, the act gave borrowers the flexibility to choose a "covered period" of any length between eight and 24 weeks. (This is the period during which PPP funds must be spent to qualify for forgiveness.) And it streamlined the forgiveness application process for businesses that borrow less than $150,000.

Employment credit enhanced

The CAA enhanced the employee retention credit created by last year's CARES Act. This fully refundable credit is designed to encourage businesses affected by the pandemic to retain employees on their payrolls. The act eliminated the CARES Act's ban on the credit for companies that received PPP loans. So, loan recipients are eligible, provided the credit isn't claimed for wages paid with proceeds of a forgiven loan.

Under the CAA, the employee retention credit is equal to 70% of up to $10,000 in qualified wages per quarter, compared to 50% of up to $10,000 per year under previous law. That means your maximum credit for the first two quarters of 2021 is $7,000 per eligible employee per quarter. In 2020, the maximum credit was $5,000 per eligible employee for the year.

Qualified wages are those paid while your operations are fully or partially suspended by a COVID-19-related government order or during a quarter in which your gross receipts have declined by at least 20% (previously, 50%) compared to the same quarter in 2019.

The employee retention credit is available to companies of all sizes, but smaller businesses have a significant advantage: They're permitted to claim it for qualified wages regardless of whether the recipients continue to work. Larger companies, on the other hand, may claim the credit only for wages paid to employees who aren't working.

Last year, this advantage was available to businesses with 100 or fewer employees, but the CAA increased the threshold to 500 employees for 2021. In other words, all businesses with 500 or fewer employees may claim the credit for qualifying wages, regardless of whether employees continue working.

The ARPA retained the CAA's enhancements to the employee retention credit and extended its availability to eligible employers through December 31, 2021. This includes "recovery startup businesses" — companies that launched after February 15, 2020, with average annual gross receipts of $1 million or less.

Other items of note

The CAA extended the work opportunity tax credit through 2025, so consider taking advantage of its benefits if you hire new workers. The credit can offset up to $2,400 in taxes per new hire from specified disadvantaged groups, including certain welfare recipients, disabled workers and ex-felons. Higher amounts may be available for eligible veterans. Keep in mind that, to qualify, you must follow certain procedures before extending a job offer.

In addition, the act extended tax incentives for certain work performed in economically disadvantaged "empowerment zones" through 2025. Eligible employers may claim a 20% tax credit on up to $15,000 in wages paid to employees who work and reside within an empowerment zone.

Tax breaks available

The CAA and ARPA provide a variety of intriguing tax- and financial-planning opportunities for construction companies. Work closely with your tax advisors to ensure you receive all the tax breaks to which you're entitled.

Sidebar: Expenses paid with PPP proceeds are deductible

When Congress authorized Paycheck Protection Program (PPP) loans in last year's CARES Act, it gave borrowers an extra gift by allowing them to exclude the amount of PPP loan forgiveness from their gross income for tax purposes. Unfortunately, in a ruling later in 2020, the IRS undid this tax benefit by prohibiting borrowers from writing off otherwise deductible expenses paid with forgiven PPP loan proceeds.

To clarify its original intent, Congress provided in the Consolidated Appropriations Act that otherwise deductible expenses remain deductible regardless of whether the PPP loan used to pay those expenses is forgiven.

A buy-sell agreement is a critical tool for owners of closely held construction companies. To be effective, however, construction business owners need to review it periodically and, if necessary, modify its language to reflect changing circumstances. This article explores the importance of scrutinizing the valuation provision, which establishes the purchase price for a departing owner's shares.

Is your buy-sell agreement up to date?

A buy-sell agreement is a critical tool for owners of closely held construction companies. It ensures an orderly ownership and management transition when an owner dies, becomes disabled or otherwise leaves the company. And it creates a market for departing owners' shares, providing them and their families with liquidity and ensuring that the business stays in the family or other tight-knit ownership group.

For a buy-sell agreement to be effective, however, you need to review it periodically and, if necessary, modify its language to reflect changing circumstances. Of particular importance is scrutinizing the valuation provision, which establishes the purchase price for a departing owner's shares.

Depending on the mechanism for valuing interests in the business, a valuation provision drafted years ago may understate or overstate the company's value. This can lead to undesirable outcomes or disputes. And the risk is especially acute now, given the significant impact the COVID-19 pandemic has had on the financial performance — and, therefore, value — of many construction businesses.

Valuation approaches

Valuation provisions in buy-sell agreements typically use one or more of the following approaches:

Negotiation. At the time an owner leaves the company, the parties negotiate the buyout price. This approach has some advantages: It's cost-effective and allows the parties to consider recent events in determining a fair price for the shares of the business. The risk, of course, is that the parties fail to negotiate in good faith, can't reach an agreement and end up in court. One way to mitigate this risk is to provide for a negotiated price but bring in an independent appraiser if the parties are unable to agree within a certain time frame.

Appraisal. Valuation by one or more independent professional appraisers at or near the time of the buyout is usually the most accurate approach — however, it can be costly. Some buy-sell agreements call for periodic appraisals (for example, once every year or two) and use the resulting price for any shares transferred between then and the next valuation date. Others require the parties to conduct an appraisal on the occurrence of a "triggering event," such as an owner's death or disability.

Be sure your agreement provides unambiguous valuation guidelines for appraisers. For instance, it should spell out the:

- Valuation standard (such as fair market value, fair value or investment value),
- Premise of value (for example, controlling interest or noncontrolling interest), and
- Valuation date.

Some agreements provide that the valuation date is the date of the triggering event, but this type of provision is susceptible to manipulation by an owner who, for example, times his or her resignation to maximize the buyout price. A better approach is to set the valuation date as the last day of an accounting period (for instance, the end of the most recent fiscal year or quarter).

Formula. Using a valuation formula tied to book value, earnings or other benchmarks has the advantage of simplicity and predictability. However, it's also quite risky. Book value, for example, may reflect a company's fair market value at formation, but it tends to significantly undervalue established companies with consistent track records of earnings.

Formulas based on earnings multiples may or may not be reliable indicators of value, depending on a company's particular circumstances at the time of the valuation. One potential solution is to revisit the formula annually and adjust it to produce a price the parties view as fair.

Review your agreement

Valuation provisions that rely on independent appraisals typically don't need to be reviewed as frequently as formula provisions. If your agreement calls for a negotiated buyout price, consider using a different method or providing for an independent appraisal in the event negotiations fail to prevent litigation.

Whatever approach or combination of approaches you and your fellow construction business owners decided on, review your buy-sell agreement regularly. Everyone will benefit from avoiding unpleasant surprises and ensuring the agreement will work as intended to yield a fair price for ownership shares.

General contractors must work hard to recover from project shutdowns/slowdowns caused by the pandemic and capitalize on what could be a stronger economy ahead. In this environment, vetting subcontractors for quality work and financial stability is more important than ever. This article reviews some basic tenets of prequalification.

Vetting subcontractors is more important than ever

General contractors now face two primary challenges: 1) recover from project shutdowns and slowdowns caused by the pandemic, and 2) capitalize on what could be a much stronger economy in the months ahead. In this environment, vetting subcontractors for quality of work and financial stability is more important than ever.

Strength of ownership

The first thing to look at in prequalifying a sub is its company history. When did the business get started? What kind of projects has it worked on? Generally, a sub that's been around for a while (say, more than five years) is probably doing something right.

Then again, a recent ownership change could affect this rule of thumb. So, check into the sub's owners and managers. Are they reputable individuals with strong track records of being easy to work with? A good way to gather such information is to ask for trade, financial and business references. Have your attorney check into any legal actions the sub might be involved in as well.

Of course, if a prospective sub happens to be a relatively recent startup, you shouldn't necessarily dismiss it out of hand. Maybe a star project manager has struck out on his or her own. In this case, you may need to rely on financial projections and direct interactions.

Pertinent numbers

As mentioned, a sub's financials can and should play a critical role in your prequalification effort. Although the raw dollar amounts associated with the company may not tell you the whole story, they'll give you a strong foundation on which to build a reasonably accurate assessment.

Request at least the most recent year's worth of financial statements and go over the numbers with your CPA. Look at metrics that give you an idea of the sub's cash flow and how well capitalized it is, such as current ratio (or quick ratio) and debt-to-equity ratio. Also examine its overhead expenses and total revenues.

In addition, inquire about the sub's bonding capacity. Is its surety willing to give the company a thumbs-up? Other types of insurance are important, too — a subcontractor that skimps on coverage may be a legal disaster waiting to happen should something go wrong on the job site.

Ease of scheduling

As part of the prequalification process, inquire about a subcontractor's scheduling capacity. Ensure the company can smoothly join a project, complete its work and exit without costly, time-consuming mistakes.

How tech-savvy is the subcontractor? Look for subs who can provide multiple means of communication (voice mail, e-mail, text messaging and so forth) and are comfortable with web-based project management if you use it. This can make a big difference when you need to make last-minute schedule adjustments.

In addition, use your interactions with a sub during prequalification to gauge how receptive it may be toward reminders about job scheduling. A company that responds quickly and in a friendly manner should earn points in the "easy to work with" category. And scheduling reminders and updates play a big role in getting a job done right.

Many ways

These are just a few of many ways to vet subcontractors. The changes and economic struggles of the past year or so make now a good time to reassess your prequalification process.

Customer relationship management (CRM) systems offer many benefits to businesses, including stronger customer relations, service and retention. This article explains how CRM systems may be most valuable to construction companies in managing the business development process and focusing a company's limited resources on winnable, profitable projects.	

CRM systems offer intriguing benefits

Customer relationship management (CRM) systems offer many benefits to businesses, including stronger customer relations, service and retention. For construction companies, this software can provide all these advantages. However, it may be most valuable in managing the business development process and focusing your company's limited resources on winnable projects that will most likely generate profitable returns.

Data at your fingertips

CRM systems don't necessarily create new data. Generally, they gather information you already have — either on paper or in multiple spreadsheets or databases — and organize it into a centralized, widely accessible database.

By placing critical data about customers and jobs at everyone's fingertips, the system improves communications and minimizes the chances that anything will fall through the cracks. For construction businesses, this includes:

- Consolidating information about customers (current and past), projects (existing and prospective), business partners (such as subcontractors, architects and lenders), vendors and suppliers, and even competitors,
- Tracking bidding and sales activities — including job details, the status of leads or bids, and relevant communications — and alerting key personnel to critical tasks or deadlines, and
- Maintaining a library of past projects and bids, with data such as "won-loss" records on previous bids and success of previous projects by client, industry, sector, location and other factors.

This information can help you identify the characteristics of bids you're most likely to win and projects that are most likely to be profitable, enabling you to concentrate your efforts and resources on those types of jobs.

Better project management

Once you've won a bid, a CRM system can help improve project management in various ways. For example, if the owner or developer contacts your company with a question or complaint about the job, the CRM system provides your personnel with instant access to relevant facts and any recent communications on the subject.

You may also be able to better coordinate relationships with subcontractors, engineers, architects, consultants and other business partners. This includes managing requests for proposal and any necessary prequalification requirements.

Of course, among the most powerful features of CRM systems is the ability to access all this information remotely. Cloud-based technology allows your construction company's authorized personnel to access data about customers, business partners, bids, contracts and projects using their laptops, smartphones or other mobile devices in real time — and to update that data instantly.

Homework is necessary

There are many CRM products available, so do your homework before buying. Look for a secure, well-supported solution that meets your needs, is usable by employees, integrates with your existing systems, and is compatible with those of vendors and other partners.