



# ON-SITE

Summer 2009

PLUS

Midyear tax planning

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# Elliott Davis

Accountants and Business Advisors

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## Putting extended, expanded breaks to work for your construction company

**A**s expected, a new administration and Congress and a bad economy have led to significant tax law changes in 2009. Some extended and expanded breaks could help contractors reduce their tax bills this year; others may provide a much-needed infusion of cash. To maximize your benefit from many of the breaks, you must act soon to start putting them to work for your construction company.

### Depreciation-related breaks

Investments in equipment are often required to stay competitive. Fortunately, the extension of a

couple of key depreciation-related tax breaks may help make such investments a little more affordable.

First, there's the Section 179 deduction. Named after its place in the federal tax code, it allows many businesses to expense (that is, immediately deduct) some depreciable assets in the year they're placed in service. The increase in the Sec. 179 limit for initial year expensing to \$250,000 — up from \$133,000 — has now been extended. This higher limit is the same as the 2008 limit and is applicable to either the 2009 calendar year or your construction company's fiscal year beginning in 2009. The expensing election begins to phase out dollar for dollar when total asset acquisitions for the tax year exceed \$800,000 (up from \$530,000). If you qualify for the full election and are in the 35% tax bracket, this increase could mean more than \$40,000 in additional 2009 tax savings.

The special "bonus" allowance that was available last year also has been extended. That is, if you buy and place into service qualified new assets for your business before Dec. 31, 2009, you can depreciate 50% of their adjusted basis, in addition to the standard depreciation rate for each type of asset, on your 2009 tax returns.

Assets that qualify for 50% bonus depreciation must be new, not used, and generally need to be acquired this year. They include tangible personal property, such as business vehicles (limited to \$25,000 per vehicle with a gross weight of 6,000 pounds or more, or \$8,000



per “luxury” vehicle), computers and office machinery, manufacturing and production equipment, and unmodified consumer computer software.

### **NOL deduction**

Like many construction companies, yours may be struggling and facing losses this year. Keep careful track of those losses because, if your company’s allowable deductions turn out to be greater than its revenues, you’ll have what’s called “negative taxable income” and, thus, may be able to claim a net operating loss (NOL).

An economic downturn is one of a variety of criteria that can qualify you for an NOL deduction. If you’re eligible, you can generally either carry back the NOL and then carry forward any remaining amount, or elect to carry forward the entire loss. Carrying back an NOL can be particularly beneficial because you can get back some (or even all) of the taxes you paid in the carryback years. Such a refund can provide an infusion of cash in a time of need.

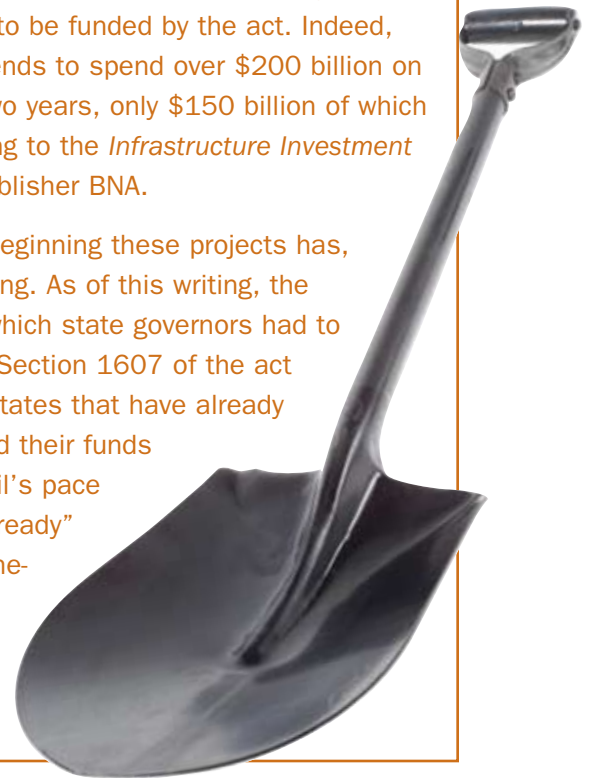
Previously, you could carry back a loss only two years in most cases. But the carryback period has now been expanded to up to five years for 2008. Qualified small businesses with average gross receipts of \$15 million or less over a three-year period ending with the tax year of the NOL in question are eligible for the new expanded carryback period.

If you had an NOL for 2008 and your construction company earned little or no income in the previous two years, having additional previous years available for the carryback may provide you with a tax refund that wouldn’t otherwise be available.

## **Infrastructure projects beckon contractors**

For contractors, perhaps the biggest news reverberating from 2009 legislation has been the signing of the American Recovery and Reinvestment Act (ARRA) in February. ARRA promised the forthcoming opportunity to bid on one of the many federal infrastructure projects due to be funded by the act. Indeed, the federal government intends to spend over \$200 billion on infrastructure in the next two years, only \$150 billion of which comes from ARRA, according to the *Infrastructure Investment and Policy Report* by the publisher BNA.

Of course, the process of beginning these projects has, by and large, been slow going. As of this writing, the certification period during which state governors had to request ARRA funds under Section 1607 of the act has just ended. And even states that have already requested and been allotted their funds have been moving at a snail’s pace with only the most “shovel-ready” jobs getting started. Nonetheless, check your state’s Web site to see whether and when any suitable projects are on the way.



On the other hand, a carryforward will offset income in future years. So if you expect business to rebound in the next few years, you may be better off forgoing the carryback. If you use it when you’re in a higher tax bracket, you’ll save more tax.

### **The Work Opportunity credit**

The construction industry finds itself at an odd crossroads, as the ongoing labor shortage runs head on into the recession. So you may need skilled laborers but may also hesitate to add the expense to your payroll. One way to mitigate this cost is by claiming the Work Opportunity credit.

Under this tax break, employers can claim a credit equal to 40% of the first \$6,000 of wages paid to employees in certain target groups, such

as ex-felons, food stamp recipients and disabled veterans. The eligible target groups have now been expanded to include unemployed veterans and disconnected youth. This expanded benefit generally applies to such workers hired in 2009 and 2010.

### Never too busy

No matter what the climate, the summer months are a hectic time for many contractors. But you should never be too busy to factor tax planning into your business activities. ☒

## Futurescope: *Construction Business Trends*

### BIM continues to win hearts, minds and disk space

The popularity of building information modeling (BIM) has been growing for some time. Just a couple of years ago, a survey conducted by the Construction Management Association of America found that BIM use had risen from just 3% of respondents in 2002 to 35% five years later. Now, two years down the road, BIM continues to win the hearts, minds and disk space of contractors nationwide.

#### Digitizing the process

In short, BIM is the digitization of the entire construction planning process. A BIM system generates computerized models of the structure to be built that you can view from any angle and at multiple levels of depth.

Make no mistake; these are not your father's 2-D computer-aided design plans. Nor are they even your big brother's 3-D project plans. Today's BIM folds 4-D (product specifications) and 5-D (cost estimating and procurement) capabilities into its output.

Among the two most prominent benefits of BIM are cost cutting and improved procurement. From a financial perspective, a BIM system can associate expense data with each and every project element, providing the design and building team with a detailed cost schedule, which they can then tweak as necessary.

When it comes to procurement, a BIM file can attach product specs, pricing and availability info to every girder, beam and joist. This capability gives project stakeholders the ability to order specific supplies far in advance, often saving money on bulk materials purchases.

#### Overcoming the challenges

When you're ready to give BIM a try, there are a variety of measures you can take to overcome the inevitable implementation challenges. Be committed to the transition from the get-go. Work with your financial advisor to target a system you can afford, and then meet with an IT consultant to help you find the right product. Finally, communicate BIM's advantages via thorough training of your employees and other stakeholders.

Also be prepared to adjust to a new way of conducting a project. BIM requires much more up front attention and discussion in the planning process because of its higher level of detail. Yet because the system does the actual drafting of the plans, you'll likely be ready to start gathering materials and putting boots on the ground much sooner.

#### Getting a feel

Naturally, there are other benefits — and challenges — to BIM. But these systems' prominence is growing. Now may be a good time to get a feel for BIM and determine whether and when you want to give it a try.

# Go ahead, sweat the little stuff

## 3 things you shouldn't ignore in today's tough economy

**A**ccording to the oft-cited self-improvement cliché, we shouldn't sweat the little stuff in life. Stop and smell the roses. See the big picture. Focus on what *really* matters.

But, in the construction business, there's a lot of seemingly little stuff that you shouldn't ignore. And, during a recession, it becomes even more important. Here are three examples of things you might overlook while you're fighting to keep your company competitive in today's tough economy and some ideas on how to improve them.

### 1. Indirect costs

Expenses not directly related to your projects, commonly referred to as "overhead" or "indirect costs," are easy to ignore. After all, they often occur in the office while you're out on the job site trying to manage a project to completion.

*The management of construction receivables and payables is easily taken for granted.*

When looking for ways to reduce indirect costs, consider your construction company's history. For instance, an analysis of your indirect costs and their relationship to your operating results can help you determine which costs are fixed, which are variable and which are a little of both. You probably can't do much to change fixed costs beyond, perhaps, negotiating with your lenders, landlords, utility providers, etc. But you may be able to trim variable costs by cutting out (or down on) unnecessary expenses.



Once you're armed with that knowledge, you can construct a budget (usually annually) for indirect costs to plan for the coming year. Then you can regularly compare your budgeted amounts for indirect costs with your actual spending. If you're going overbudget, look for ways to cut back.

### 2. Receivables and payables

You do the work, you generate an invoice and you send it out. Bills come in and you pay them the best you can. The management of construction receivables and payables, however, is easily taken for granted.

One receivables strategy that plays well with many contractors is front loading contract billings. This involves shifting some profits into earlier phases

rather than applying a flat rate to all phases as usual. Be careful not to be too aggressive, as overbilling can alienate your owner or general contractor, which can cause problems down the line. But, when done properly, this strategy can help you collect some of your profits before the retainer is paid on completion.

When it comes to payables, make sure pride isn't getting in your way. If you've always paid vendors within 30 days and are experiencing a cash flow shortage, consider extending your payment cycles. Just as you are sometimes flexible with parties that owe you money, ask for a break from your creditors to help you handle the cash crunch and deal with cost overruns.

*Taking the time needed to address change orders can do much to protect and even bolster your bottom line in tough times.*

### **3. Change orders**

With your eye firmly fixed on project completion, change orders can often arise like ants at a picnic. You just want to deal with them quickly and get to your lunch. But taking the time needed to address changes properly can do much to protect and even bolster your bottom line in tough times.

For starters, know your contracts. It's next to impossible to quickly identify a change unless you



know how it differs from the original agreement. Also, be sure you have a well-managed change order system. In order to ultimately receive the written, signed and authorized change order that will get you paid, maintain daily reports, project correspondence, meeting minutes, schedules, cost records, photos and other documentation to help indicate an operational change.

Last, be sure to provide written notice and an explanation of how your revised work will affect the schedule and delivery date, including a date on the document to prove you gave owners plenty of time to react to the associated costs. Lack of notice can be a strong defense for owners, so following these steps will help increase the likelihood you'll get paid for the extra work.

### **Survive to fight another day**

Many construction companies are struggling to maintain their profitability — if not stay in business altogether. You'll stand a better chance of surviving to fight another day by doing all the little things right while everyone waits for better times to arrive. ☒

# The Contractor's Corner

## Should we hire a CFO?

*Fortunately enough, I've been able to keep my construction company relatively busy over the past year. The problem is my financials: I have an accounting clerk who helps maintain the books and, of course, I work with my CPA come tax time, but I can't help feeling as if I'm missing something. A friend of mine who works in a different sector suggested I look into hiring a chief financial officer (CFO). Is this a good idea for contractors?*

A CFO may be a great addition to many construction companies for a variety of reasons. But taking on an employee of this stature is a big decision that warrants some careful consideration.

### Review your staff

Because of the risks involved, undertake the decision of whether to hire a CFO within the context of a total staffing review. In today's economy, you need to maximize your return on investment of every employee on your payroll. Who is absolutely necessary to staying in business? Who isn't?



A construction company that's struggling to stay afloat probably shouldn't take on a full-time CFO's salary and benefits, no matter how much long-term good he or she might do. Then again, many contractors could use a higher-level person to help them stay profitable. The tipping point is whether your company can fit a CFO into its staff and is prepared to follow through on the initiatives he or she will be responsible for developing.


### Conduct your search

So let's say you think you do have the room on your roster to hire a CFO. What exactly would he or she do for you? Well, a job description might read:

This individual will oversee and take responsibility for the company's financial plans and policies, including its accounting practices and its relationships with lending institutions and the financial community. Will hold primary responsibility for project analysis and cost controls, cost accounting systems, budgeting and cash flow projections, and asset maximization.

Don't expect to find the right CFO by just putting an ad in the paper or on an Internet job board. For a high-level position like this, you may need to retain a recruiting firm to handle the search. Or you might look at hiring someone away from one of your competitors. Outsourcing the function on a contractual basis may even make sense.

### Think about it

This may not be the ideal economic climate to add a major position to your payroll. But having a CFO can allow you to let someone else worry about — and improve — your financials, while you focus on winning and completing projects. 



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