Construction trends

Integrated project delivery puts teamwork to the test

Satisfying your surety in today's economic environment

Are you forgetting something?
For many contractors, sales and use taxes are too easily ignored

ON-SITE

PLUS

The Contractor's Corner
Construction company owner tires of failing fleet

Fall 2010

Construction trends

Integrated project delivery puts teamwork to the test

Under the traditional construction paradigm, the three major parties — owner, architect and contractor — are theoretically working toward the same goal: getting a structure built.

But, in reality, it's rarely that simple. The owner is trying to get its project completed as quickly as possible within — or under — budget. The designer wants its plans followed to the letter. And the construction company is trying to do the best possible work without losing control of its costs. All of these objectives don't always gel with one another and, when they don't, conflicts can arise.

To prevent such discord, many jobs are operating under a relatively new paradigm: integrated project delivery (IPD). Although this approach certainly puts the concept of teamwork to the test, it's proven successful on a wide variety of projects.

Defining the term

Figuratively speaking, IPD eschews the traditional "silo" approach to construction and replaces it with a more collaborative boardroom-table approach. That is, instead of the owner passing its concept down to the architect who, in turn, passes its plans down to the contractor, all come together as equals and teammates bound by a single contract.

Thus, bidding for the job in question has much less to do with price and more to do with who will be best able to communicate and collaborate effectively. Although any subcontractors involved probably won't be considered primary team members, they'll need to sign off on the contract and be aware of its perhaps unusual nature.

IPD agreements are generally set up with a guaranteed maximum price (GMP) clause that sets a maximum at-risk amount for the job. The same clause, however, also creates a pool of incentives for the team to shoot for. The American Institute of Architects offers sample agreements as well as a complete look at IPD projects in its *Integrated Project Delivery: A Guide*, which is available via its Web site (aia.org).

Revolving around BIM

Lately, IPD projects have been widely associated with a specific construction technology that's also gained popularity in the industry. That technology is Building Information Modeling (BIM). This computerized modeling system covers every facet of a building project, from CAD drawings to work schedules to manufacturer recommendations for building components.

Along with generating specifications and drawings, BIM allows everyone on an IPD project to access the same updates, changes and other information in the same place. BIM also operates continuously, so it shows not only how physical components look (such as 3-D), but also when each facet of a structure will be built (4-D) and how much each component will cost (5-D).

Plus, BIM can detect conflicts in building design and alert team members with detailed computer visualizations of each part in relation to the total project. This function, in particular, makes it perfectly suited for IPD jobs, wherein designers and builders are working in close collaboration.

Assuming the risks

Among the basic objectives of IPD is the elimination of change orders. When the owner, architect and contractor work together, nothing should change unexpectedly and cause the need to negotiate additional payments or extended deadlines.

Of course, that doesn't mean IPD eliminates the risk of conflict. A core team that doesn't get along may never get a job off the ground, so it's important to choose co-collaborators carefully. As a show of goodwill, some contracts include a waiver preventing litigation and calling for arbitration or some other form of alternative dispute resolution.

Another potential risk is a hesitant surety. Some bonding firms are leery of anything outside the norm and may make you jump through a few extra hoops before undersigning an IPD job. Their primary fear is usually an unclear delineation of duties among the parties.

Thinking lean

Ultimately, IPD is an incarnation of the "lean construction" movement that began several years ago. As the economy and many local construction markets keep contractors on the financial defensive, IPD can serve as a means to reduce conflicts and speed efficiency. But the team chemistry must be right.

Satisfying your surety in today's economic environment

The construction industry has many inherent ups and downs. But, with the continuingly rocky economy, the ups and downs have been a little (or a lot) more severe in many areas. Because of this, many bonding firms have tightened their requirements considerably. Here are some ways to satisfy your surety in today's tricky economic environment.

Good communication paramount

For starters, keep the lines of communication with your surety wide open at all times. Consider your surety agent part of your overall advisory team, just as you do your accountant and attorney.

To make sure your agent is always aware of what your company's doing, send him or her regular financial reports as well as updates on your current project workload. And even if nothing particularly earthshaking is going on, give him or her a call occasionally just to say hello. Sometimes a little goodwill can go a long way.

Well-ordered financials a must

Every construction company needs to make sure it's providing the right information to its sureties. Bonding firms tend to focus on equity and working capital. If you can demonstrate that you're managing your cash flow, and that you have enough working capital to see you through any unforeseen problems, you'll generally stay on a surety's good side.

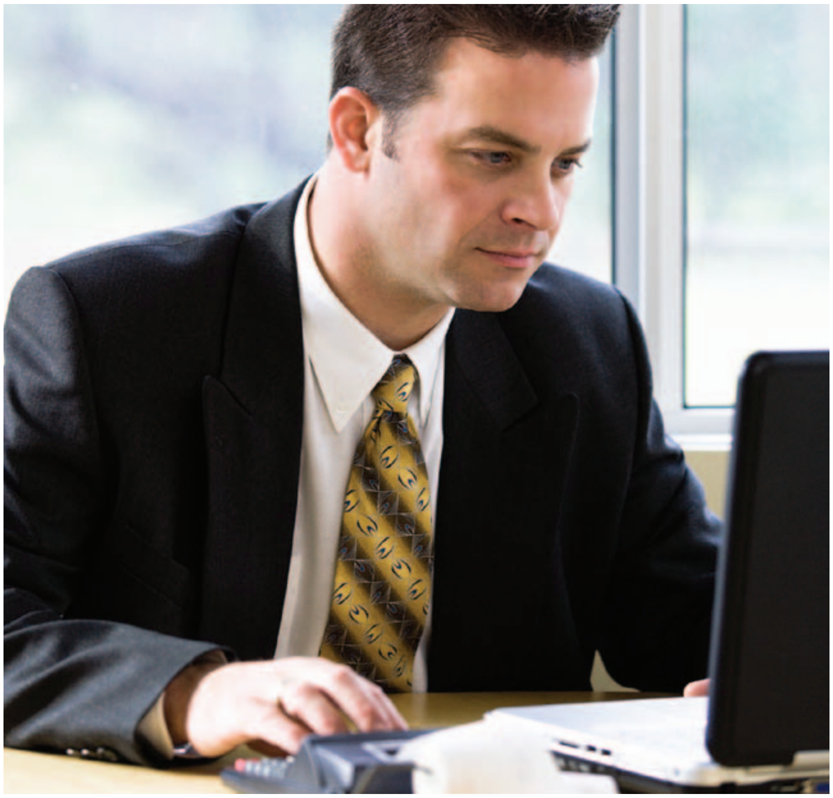
Sureties also look for evidence that you've managed to stay profitable over the long term. By nature, the construction business has highs and lows. So if you can consistently demonstrate a steady history of profitability, you'll show your surety that you clearly know how to get through the lean times.

Bear in mind that, to ensure a construction company isn't taking on an unacceptable amount of risk, a surety will sometimes also want to review recently completed contracts as well as those in progress.

Sureties look for evidence that you've managed to stay profitable over the long term.

Don't ignore your business plan

A sound business plan that clearly indicates not only where you're going, but how and why, can put (and keep) your surety at ease. When a construction company has a written, up-to-date plan, sureties think it's less likely to go off on a risky tangent.



Similarly, a contingency plan that shows how you'll deal with financial emergencies demonstrates your ability to remain cool under fire. Creating a disaster recovery plan that delineates your planned response for natural and manmade catastrophes is also a good move.

Still cautious

In many cases, bonding firms have been able to weather the last few years' economic storms rather well. But they're generally still subject to the cautiousness of the financial sector as a whole. Work with your CPA to ensure your financials and business documentation are in the best shape possible.

Are you forgetting something?

For many contractors, sales and use taxes are too easily ignored

With year end fast approaching, you may instinctively be thinking about income tax planning. But there's another tax issue that also warrants your attention, and it's one that's all too easy for contractors to ignore: sales and use taxes.

With many states desperately trying to keep their budgets balanced, some are raising money by increasing those taxes — or by more actively pursuing their collection. If your contracts aren't taking this into account, you could be short-changing your profitability.

Sales vs. use

If you've ever taken an out-of-state job, you know that every state brings its own sales and use tax regulations to the table. Property type and contract structure can affect whether you or the owner is on the hook for these taxes.

Generally, you must pay sales taxes on any materials you buy for a project unless those materials are deemed "for resale." This may be the case if you buy materials, agree to sell them at a fixed price and perform a service in connection with the sale — either for an additional fixed price or on the basis of hours worked. It may also occur if you sell materials or supplies as a retail transaction.

Use taxes, on the other hand, come into play when goods bought in one state are owned, kept or used in another. For example, if you buy out-of-state materials and don't pay sales tax, you'll almost always be liable for use tax to the state in which you use those items. Use taxes, which are sometimes referred to as "compensating use

taxes," prevent taxpayers from avoiding sales tax on out-of-state purchases.

If you haven't done so lately, check with your tax advisor regarding how your home state (and any other state in which you work) handles sales and use taxes and whether any changes have occurred.

Best case and worst

There can be both best and worst cases when it comes to sales and use taxes. Let's start with the worst: Some jobs may lead you to *double* taxation. This can occur when two taxes are imposed on the same purchased materials during the same period. Although you'd think such a possibility would be barred by law, it often is not.

Double taxation is common when a contractor buys materials in one state (triggering sales tax) and then transports those goods to another state for storage (triggering use tax). To prevent this detrimental occurrence, you can obtain an exemption certificate from sales tax — claiming an out-of-state purchase — and pay only the use tax in the state where you intend to store and use the materials.

As for the best case, many states offer exemptions from these taxes when the project in question involves a charitable, religious or educational organization. You may even be exempt from sales and use taxes when doing repair or maintenance work for a qualifying organization. The key is: You've got to obtain an exemption certificate *before* buying the materials and performing the work.

Projects involving the federal government, as well as state and local governments, are also generally immune from sales and use taxes. But the key word there is "generally." There may be some items related to a federal job that don't qualify for this immunity.

The challenge is to accurately estimate just how much of your bid should account for materials and equipment *not* subject to the exemption. Guessing wrong and then winning the job could turn out to be a disaster if the project's bottom line is crushed by unanticipated sales and use taxes.

Contractual approaches

Contract structure plays a big role in how sales and use taxes affect your construction company. For instance, under a lump-sum contract, you incur tax on your purchases and then don't collect any sales tax from your customers. On the other hand, under a time-and-materials contract, you buy materials tax-free using resale certificates and then charge your customers sales tax.

If you've grown accustomed to using either contract type exclusively, it doesn't hurt to review the other and determine whether it might put you in a better position on certain jobs. Typically, going with a lump-sum contract allows you to lower your bids in states that require time-and-materials contractors to buy for resale and tax their customers. But, for smaller jobs, sometimes a time-and-materials contract is easier to negotiate and carry out.

A time for review

The uncertain economy has given many contractors financial fits. One relative upside to this situation is that you may not need to do quite as much income tax planning this year — though you certainly shouldn't ignore it either. If this is the case with your construction company, a great way to leverage that extra time is to review and perhaps improve how you're handling sales and use taxes.

You still have time to reap the full benefit of the retention credit

The Hiring Incentives to Restore Employment (HIRE) Act offers two valuable tax breaks for hiring certain unemployed workers: payroll tax forgiveness and a retention credit. Although payroll tax forgiveness is available only through Dec. 31 and thus will provide limited tax savings for hires you make between now and year end, you still have time to reap the full benefit of the retention credit.

The credit applies to workers who are qualified for the purpose of the payroll tax forgiveness and whom you retain for 52 consecutive weeks. The tax savings per qualified retained worker are equal to the lesser of 6.2% of the wages paid to the worker during the 52-week retention period or $1,000.

Because the retention period won't end until 2011, you'll claim the credit on your 2011 tax return. But you must make the hires by Dec. 31, 2010. Additional limitations apply, so check with your tax advisor for details.

The Contractor's Corner

Construction company owner tires of failing fleet

As I stood on a job site recently, staring at a huge piece of expensive equipment with smoke pouring from its engine, a simple question occurred to me: Is there a better way? Up until now, we've tried to maintain our vehicles and equipment as best we could to maximize their lives. But a spate of recent breakdowns has really hurt us. So I ask again: Is there a better way?

Fortunately, there is — and it's called "fleet management." As its name indicates, this is a formalized, comprehensive approach to buying, using, maintaining and disposing of your vehicles — including those used to transport personnel, supplies or construction equipment.

What's it all about?

A critical aspect of fleet management is gathering data to track which company's vehicles are in peak operating condition. Any that aren't in prime condition are likely increasing your operating expenses — sometimes in amounts small enough that you may not even realize it.

Tracking information related to each vehicle's age, condition and usage will help you make the critical decision of whether to lease or buy a given asset and, if you purchase new, when it's time to sell. Leasing is often the go-to choice because of the flexibility of these arrangements, which often last as long as two to three years.

New vehicles feature lower initial maintenance costs, increased dependability and better technology. But a vehicle purchase will likely gobble up cash quickly and may even require a loan. Plus, the inevitable wear-and-tear put on job site assets accelerates their devaluation, which has become an even greater problem in many areas of the country as the used equipment/vehicle market continues to struggle.

Is there an app for that?

Like just about every other aspect of the construction business, software is available to help you manage a fleet management program at your company. Many include interactive parts catalogs to help you target each asset's potential needs.

Another great function of many fleet management systems is their capacity to be integrated in multiple platforms — including your accounting and billing systems. This can help you better manage your finances as well as collaborate with subcontractors and joint venture partners.

Of course, no mention of fleet management would be complete without a nod to GPS technology. Installing GPS capabilities on vehicles can help you keep employees from using your assets for personal or recreational purposes. It may also help improve dispatching and lessen fuel consumption.

Need to tighten up?

Contractors nationwide are having to tighten their financial belts in various ways. Getting more from — and paying less for — your company's vehicles is a good way to do so.