

Construction

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Subcontractors and surety bonds: 5 tips for getting paid

Eliminate the creep!
How to manage indirect costs

Public construction projects
Reinventing yourself to compete

CONTRACTOR'S TOOLBOX

Is subcontractor safety
any of your business?

Subcontractors and surety bonds: 5 tips for getting paid

When it comes to getting paid, especially in the current environment, subcontractors shouldn't take any chances. If you're a subcontractor that works on bonded projects, there are steps you can take to help ensure you get paid for your work and materials. Here are five tips to consider:

1. Don't assume

Payment and performance bonds are generally required on public projects, under the federal Miller Act or one of the many state-level "Little Miller" acts. Some private construction contracts require bonds, but in most cases they're unnecessary because state mechanics' lien laws provide the most effective remedy for subcontractors who haven't been paid. Mechanics' liens can't be filed on public property, however, so payment bonds generally serve as a substitute on public projects.

Even if a bond is legally required — and you're within the class of subcontractors entitled to make a claim — there's no guarantee that the general contractor has actually furnished one.

If you're contemplating work on a public project, however, don't assume that you'll be protected by a payment bond. For one thing, some apparently



public projects are, in fact, privately financed, and the Miller Act doesn't apply. And even if the Miller Act or a Little Miller act applies, that doesn't necessarily mean you're covered.

The Miller Act, for example, requires bond protection only for first-tier subcontractors and suppliers (those that contract directly with the prime contractor) and for second-tier subcontractors and suppliers who contract with a first-tier subcontractor. Most Little Miller acts have similar requirements.

Even if a bond is legally required — and you're within the class of subcontractors entitled to make a claim — there's no guarantee that the general contractor has actually furnished one. Rather than assuming that the bond requirement has been fulfilled, you should ask for a copy of the executed bond to verify that the general contractor has complied and that the bond is valid and sufficient.

2. Make alternative security arrangements

If there's no bond, consider requesting an alternative form of security. For example, you might ask the general contractor to place a certain

amount of cash in escrow, provide a letter of credit, or furnish personal guarantees. If the general contractor refuses to provide such security, and you're uncomfortable with its ability to pay you in a timely fashion, you should seriously consider walking away from the job.

3. Check the surety's financial condition

Like many businesses in today's economy, some sureties are struggling financially. Even if you're covered by a valid, sufficient payment bond, if the surety becomes insolvent you may be left without protection.

Before you sign a contract, it's a good idea to investigate whether the surety is financially stable. Also, find out whether the state in which the project is located has an insurance guaranty association or similar program that provides you with insurance in the event the surety becomes insolvent.

4. Know the rules

To preserve your right to recover payments from the surety, be sure that you understand any contractual terms that govern your right to payment, as well as all applicable notice and statute of limitation requirements related to the bond.

Under the Miller Act, for example, you must provide written notice of your claim to the principal (the general contractor or other party responsible for furnishing the bond) within 90 days after the last day on which you furnished labor or materials for the project. The federal act also imposes a one-year statute of limitations on bond claims. The bond agreement itself may impose additional procedural requirements.

5. Document your claim

Having the documentation to back up your claim is essential. First, to comply with statutory notice requirements, you'll need to state the amount of your claim with a high degree of accuracy. Second, you'll need solid documentation to prove that you're entitled to payment under the bond.

Don't take chances

It's a big mistake to assume that you're protected by payment or performance bonds. Before you sign a contract, work with your financial and legal advisors to perform the due diligence needed to confirm that required bonds exist, that they're valid and sufficient, and that the surety is financially stable. This is the best way to protect yourself. ■

Eliminate the creep!

How to manage indirect costs

What your construction company spends on project management, repairs, small tools, office trailers and so forth can easily creep up on you. These *indirect* job costs — if not properly allocated to their projects — can cause your overhead to increase and your profitability to suffer.

Overlooking indirect costs when preparing job estimates can cause a project to run over budget. Moreover, if you bid on a project and consider only the *direct* costs, you may win the contract,

but you'll likely lose money in the long run. Let's take a closer look at how to track and recover indirect costs.

Gain insight on your spending

A good place to start is in your chart of accounts — it should break down indirect costs into enough categories to provide you with insight into these expenses. Then, with your CPA's help, analyze the information by performing a budget-to-actual analysis. This



involves setting a budget amount (usually annually) through a review of previous years' costs, planning for the coming year and comparing the budgeted amount to your actual costs regularly. Set up the budget using up-to-date accounting software so you can run the budget vs. actual comparison at any time.

You can also benchmark your company's indirect costs to a peer group. Trade organizations may perform annual financial surveys that provide such information. Or you can work with a construction consultant who has access to a large database of contractor data. By gaining an understanding of the levels of indirect costs your peers are incurring, you'll have a better idea of the significance of indirect costs for your company.

Determine how costs affect projects

When you know what you're spending and how those numbers compare to your budget and to numbers from similar construction companies, you can start cutting your indirect costs. Using the data you've gathered, determine how each indirect cost contributes to your projects. Then identify which costs are fixed, which are variable and which are a little of both.



In addition, analyze how changes in your job types or volume affect your indirect costs. There may be some indirect costs that are more directly affected by the type or volume of your projects than you previously thought.

Look at outside costs

After looking inside, take a look outside to see whether you're incurring unnecessary (or unnecessarily high) indirect costs. This means reviewing the amounts you're paying vendors for items such as uniforms, utilities and technology.

Also consider whether any personal relationships you've established with vendors are hurting your bottom line. Granted, the vendor relationships that contractors build over time often play a huge role in their companies' success. Still, you need to make sure you're spending your indirect dollars wisely.

Scrutinize direct costs too

You likely are already doing a pretty good job of tracking your direct costs, such as labor, subcontractors, materials costs and equipment. It doesn't hurt to review your cost-tracking process, however, to make sure you're not overlooking anything.

One of the best ways to track direct costs is to assign every job a number and record that number with every cost incurred. Good job-costing software is a must to help you crunch the numbers and generate detailed profitability reports. Profit and loss, job cost, aged accounts receivable and aged accounts payable are examples of key reports that you should review each month. Look for places where you're over- or underbudget and adjust as needed.

Strive for realistic bids

Set up correctly, an indirect-cost allocation system can help you to bid projects more realistically and build up your bottom line. Give us a call; we're here to help you. ■

Public construction projects

Reinventing yourself to compete

The struggling economy has been tough on the construction industry, particularly for contractors that do residential and commercial work. In the current climate, many contractors have found that the key to survival is to reinvent themselves to take advantage of new opportunities in public works construction.

If your firm has never done this type of work — or hasn't done any recently — it's critical that you get up to speed on the rules for bidding on public contracts. One misstep can be the difference between winning and losing a job, or worse yet, the difference between profit and loss.

Finding the work

To get involved with public construction projects, the first step is to find out where the jobs are. Most federal projects are advertised on the Federal Business Opportunities Web site (fbo.gov). Learning about state and local projects, however, can be more challenging.

Once you've identified a project you'd like to bid on, it's critical to become familiar with the government agency's public bidding rules.

Competitive bidding rules vary significantly from state to state and even among local governments. Although government agencies generally are required to publish bid solicitations in a manner designed to attract a significant number of bidders, they also have a great deal of discretion in the advertising vehicles they use. It's not unusual for a school district or other agency that has established relationships with local contractors



to place bid solicitations in newspapers that aren't widely circulated.

By learning about these strategies and finding out where various government agencies advertise projects, you can uncover new opportunities and get a leg up on the competition.

Understanding the rules

Once you've identified a project you'd like to bid on, it's critical to become familiar with the government agency's public bidding rules. These rules are often widely published or found in state statutes or local ordinances.

Smaller agencies may have their own rules that aren't as readily available. To avoid having your bid rejected on a technicality, it's a good idea to call the contracting agency to be sure you're aware of all applicable rules.

Don't get dismissed on a technicality

Bidding on public projects can be very different from bidding on projects in the private sector. Generally, if you don't follow the rules to the letter, your bid will be rejected. Here are some tips for staying in the game:

Comply with deadlines. Know the deadline and comply with it. Public agencies rarely accept late bids.

Don't impose conditions. If your bid is conditional on the occurrence of some event — such as certain terms being included in the contract — it will probably be rejected.

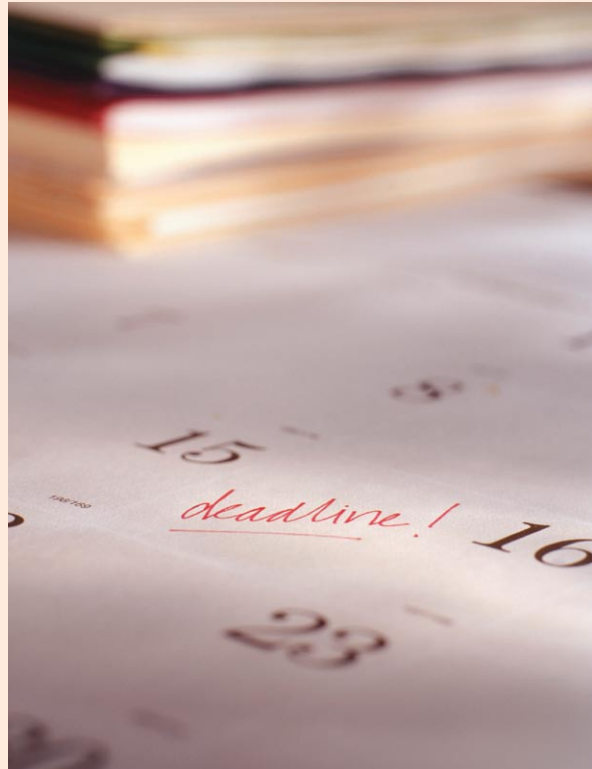
Submit a bond. Be sure to submit a bid bond or bid deposit, if required.

Avoid material errors. Make certain you bid on any materials specified in the solicitation documents.

Dot the i's and cross the t's. Prepare a checklist and go over your bid carefully to ensure you've signed it wherever required and furnished all requested information. If required, remember to submit a "Certificate of Eligibility" or similar document.

Ask questions. If the bid solicitation is vague about the work to be performed or any other terms or conditions, be sure to address this issue with the contracting agency up front. If you wait until the bidding process is over to raise the issue or file a formal protest, there's a good chance your challenge will be rejected.

Attend the prebid conference. Increasingly, attendance at these meetings is mandatory.



As noted, public bidding rules vary from agency to agency, so it's important to study the specific rules that apply to the project on which you're bidding. See "Don't get dismissed on a technicality" above for some tips on staying out of trouble.

Getting a competitive edge

Understanding public bidding rules provides you with another important advantage: It enables you to identify other bidders who have submitted incomplete or noncompliant bids and then bring them to the attention of the contracting agency, either informally or through a formal bid protest.

It's not unusual for a contractor with the second or third lowest bid to win a job when lower bids are bounced because of rule violations.

Do your homework

Public construction projects can be a lucrative source of new work right now. To successfully compete for this work, however, it's essential that you learn about — and comply with — each public agency's competitive bidding rules.

Moreover, keep in mind that some agencies are better than others and still others are more difficult to work with. ■



Is subcontractor safety any of your business?

In a nutshell, YES! In a recent decision, the U.S. Court of Appeals for the Eighth Circuit reversed a ruling by the Occupational Safety and Health Review Commission (OSHRC) and upheld OSHA's policy of citing general contractors for their subcontractors' safety violations. What does this mean to you? The policy effectively makes general contractors responsible for ensuring a violation-free worksite for *all* employees, not just their own.

Working without a net

Summit Contractors was the general contractor for construction of a college dormitory in Little Rock, Ark. The firm subcontracted the entire project, so its only employees on the job site were a project superintendent and three assistant superintendents.

On several occasions, Summit's project superintendent observed employees of All Phase Construction (the exterior brick masonry subcontractor) working on a scaffold without guardrails or personal fall protection. The superintendent advised All Phase to correct the problems, but when its employees moved the scaffold to another location, they continued to work without guardrails or fall protection.

Eventually, an OSHA officer observed the violations and issued a citation to Summit based on the "controlling employer" policy. In other words, even though none of Summit's employees were exposed to the hazard, as a controlling employer Summit was liable for the All Phase employees' violations of OSHA standards.

Summit contested the citation and the OSHRC ruled in its favor, finding that OSHA regulations require employers to protect only their own

employees. But, when it went to court, the Eighth Circuit disagreed, concluding that the controlling employer policy was consistent with the language of the regulations and deferring to OSHA's interpretation.

What you should do

Although the Summit case is binding only in the states that make up the Eighth Circuit (Arkansas, Iowa, Minnesota, Missouri, Nebraska, North Dakota and South Dakota), it's likely that OSHA will continue to enforce its controlling employer citation policy outside the Eighth Circuit. It remains to be seen, however, whether the OSHRC will acquiesce in the court's decision outside the Eighth Circuit and, if it doesn't, how other circuits will rule on the issue.

General contractors in all states, including states outside the Eighth Circuit, should carefully review their subcontractors' safety records and monitor their activities on construction sites. It may also be a good idea to consult an attorney about modifying construction contracts to require subcontractors to comply with OSHA safety requirements as well as the general contractor's safety plan, and to impose penalties if they don't comply. ■

