Construction Industry Seminar

October 28, 2010

Camp Hill • Lancaster • Lehigh Valley
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Agenda

- 1:00 pm — Taking the Mystery Out of Surety Bond Credit Analysis: An Inside Look at Universal Underwriting Guidelines
  - *Greg Marco, McConkey Insurance & Benefits*
- 1:50 pm — Break
- 2:00 pm — Facilitated Discussion on a Recent Survey of the Construction Community and the Issues They All See Impacting Their Businesses
  - *Scott Heintzelman, Michael Hoffner & David Blain, McKonly & Asbury, LLP*
- 2:50 pm — Break
- 3:00 pm — Getting Paid Through the Assertion of Mechanics Liens and Payment Bond Claims
  - *Thomas Williams, Reager & Adler, PC*
- 3:50 pm — Evaluations & Adjournment
- 4:00 pm — Networking Mixer at the Hotel's Elephant & Castle Pub and Restaurant

Taking the Mystery Out of Surety Underwriting

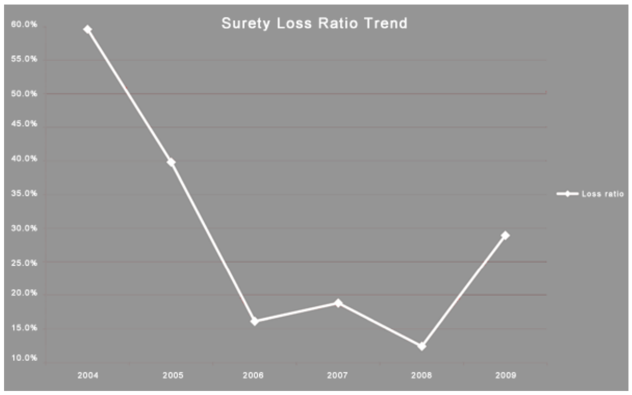
Presented by:

Greg Marco
Surety Account Executive
gmarco@ekmcconkey.com

Preview

- Surety Trends
- Bond Underwriters Perspective
- Balance Sheet Hot Buttons
- Backlog/Experience
- Off Balance Sheet Support
- Communication with your professional team
- Questions

Industry Trends



- 2000-2004 loser years
- Kmart
- Enron
- World Comm
- Private Job Bonds
- Sub Bonding


Dubai Construction Update
mre Solt - 2007 ©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GILLESPIES

Underwriters Perspective

- Unsecured Credit
- “Zero Loss”
- Bank in first position
- Uniform Underwriting as a base

Why Projects Fail

80% of Failed Projects Derive From:

- Cash Flow Deficiency/Insufficient WC
- Mismanagement of Project Funds
- Diversion of Funds to “non-project” purposes
- Working out of territory
- Taking on a job larger than 2 times your biggest job to date
- Underbidding/Poor Estimating

Balance Sheet Support

- WIP
- Working Capital
- 10% Case

Equity

- Quality of Equity
- Current A/R
- Retained Earnings

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WORK IN PROGRESS REPORT

ABC Construction 4/23/2010

Job Description and Location	Contract Price (Include Approved Change Orders)	Contractors Total Estimated Cost	Total Amount Billed to Date (Including Retainage)	Cost to Date	Revised Estimated Cost to Complete	Current Estimated Gross Profit	Estimated Date of Completion
Core Holdings	$ 693,150.00	$ 640,343.00	$ 486,365.30	$ 343,160.60	$ 287,183.00	$ 68,239.00	7/10/2010
Bridgetown	$ 799,405.99	$ 625,000.00	$ 741,079.00	$ 453,504.00	$ 125,000.00	$ 174,405.00	10/10/2010
York Y	$ 61,830.00	$ 52,544.00	$ -	$ 890.00	$ 52,544.00	$ 8,396.00	8/10/2010
VA Hospital	$ 325,000.00	$ 274,345.00	$ 30,979.00	$ 2,884.00	$ 271,461.00	$ 50,655.00	7/10/2010
A&M University	$ 145,400.00	$ 119,300.00	$ 8,465.00	$ 1,200.00	$ 118,100.00	$ 26,100.00	8/10/2010
Private Building	$ 78,680.00	$ 63,030.00	$ 71,863.00	$ 33,232.00	$ 28,500.00	$ 15,600.00	6/10/2010
Allentown High	$ 116,808.00	$ 86,524.00	$ -	$ 2,000.00	$ 84,524.00	$ 30,284.00	9/10/2010
Hillsdale	$ 540,799.00	$ 458,304.00	$ 458,182.00	$ 225,525.00	$ 220,000.00	$ 81,119.00	7/10/2010
Egg Harbor	$ 10,880.00	$ 7,800.00	$ -	$ -	$ 7,800.00	$ 3,080.00	5/10/2010
Totals	$ 2,771,952.99	$ 2,327,190.00	$ 1,796,933.30	$ 1,062,395.60	$ 1,195,112.00	$ 457,878.00	

CONTRACTS COMPLETED SINCE LAST FISCAL CLOSING STATEMENT OR LAST STATUS REPORT

Job Description & Location	Final Contract Price	Total Cost	Gross Profit / Loss
Harrisburg Depot	$ 90,421.00	$ 69,659.00	$ 20,762.00
York Surgical	$ 648,047.00	$ 621,883.00	$ 26,164.00
Millersville University	$ 362,697.00	$ 304,793.00	$ 57,904.00

Submitted By: John Doe
Title: President
Date: 4/27/2010
Email Address: jdoe@abcconstruction.com

Financial Statement Trend Analysis

Contractor Name ABC Construction Company (Review)

DATES	12/31/2009	12/31/2008			
ASSETS					
CURRENT ASSETS					
Cash…………………………………………	$ 296,283.00	$ 104,359.00			
Marketable Securities……………………..	$ 5,500.00	$ 7,650.00			
Accounts Receivable……………………….	$ 344,251.00	$ 848,723.00			
CD………………………………..		$ 339,181.00			
Inventory………………………………..	$ 102,423.00	$ 82,846.00	Divide by 2- argument for more/Inventory Obsolete?		
Cost & Estimated Earnings / Billings………..	$ 14,952.00	$ 9,244.00	un approved Change orders? Will this materialize into billings? Poor cash management? 25% of working capital is a red flag		
Cash Value Life Insurance………………….	$ 163,207.00		*Argument Made on being a current asset		
Note Recievable	$ 36,622.00		* Argument made on current asset see notes		
Total Current Assets……………………….	$ 963,238.00	$ 1,392,003.00			
SECONDARY ASSETS					
Notes Receivable/CP………………………….			* Can this go above the line-see notes		
Accounts Receivable > 90 Days………………			* What's the Story? Gov't pays but late etc.		
Notes Receivable Net of CP…………………	$ 343,239.00				
Inventory - Non-Current………………………	$ 102,423.00	$ 82,845.00			
Non-Compete (net)…………………….	$ 65,267.00	$ 80,942.00			
Other Securities/Captive……………………	$ 36,000.00	$ 36,000.00			
Prepaid Expenses / Deposit………………		$ 11,100.00			
Deposit………………………………………	$ 8,200.00	$ 8,194.00			
Total Secondary Assets…………………….	$ 555,129.00	$ 219,081.00			
FIXED ASSETS					
Propety & Equipment……………………..					
MINUS Accumulated Depreciation………..					
Real Estate…………………………………					
software					
Total Fixed Assets………………………….	$ 471,599.00	$ 476,008.00			
TOTAL ASSETS………………….	$ 1,989,966.00	$ 2,087,092.00			

LIABILITIES					
CURRENT LIABLITIES					
Accounts Payable……………………………..	$ 115,814.00	$ 296,661.00			
Accruals………………………………………..	$ 175,052.00	$ 106,389.00			
Notes Payable Bank……………………………		$ 158,919.00			
Other Notes Payable/Lease………………					
Current Portion of Long Term Debt……	$ 10,670.00	$ 60,201.00			
Federal Income Taxes…………………………	$ 94,080.00	$ 43,000.00			
Deferred Income Taxes………………………..	$ 133,696.00	$ 209,081.00			
Billings / Cost & Estimated Earnings………..	$ 95,065.00	$ 164,577.00	Could be GC using owners cash OR Job borrow using the cash to fund loser jobs		
Total Current Liabilities…………………..	$ 624,377.00	$ 1,038,828.00			
LONG TERM LIABILITIES					
Other Notes Payable………………………….					
Due on Real Estate……………………………					
Long Term Debt - Net of Current Portion…		$ 11,358.00			
Capital Lease……………………….					
Deferred Tax Liability…………………………	$ 75,766.00	$ 72,190.00			
Total Long Term Debt………………………	$ 75,766.00	$ 83,548.00			
Total Liabilities……………………………..	$ 700,143.00	$ 1,122,376.00			

EQUITY

Proprietorship / Partnership Equity………..					
Members' Capital - LLC…………………….					
Capital Stock……………………………….	$ 28,488.00	$ 28,488.00			
Retained Earnings……………………	$ 3,017,965.00	$ 2,690,708.00			
Accumulated Other Loss……………………	$ (3,630.00)	$ (1,480.00)			
Treasury Stock……………………………	$ (1,753,000.00)	$ (1,753,000.00)			
Total Equity……………………………….	$ 1,289,823.00	$ 964,716.00			
TOTAL LIABILITIES & EQUITY	$ 1,989,966.00	$ 2,087,092.00			

INCOME STATEMENT

Sales………………………………………….	$ 6,906,387.00	$ 7,750,857.00			
Gross Profit……………………………………	$ 2,074,758.00	$ 2,053,472.00			
% of Gross Profit to Sales……………….	$ 0.30	$ 0.26			
General & Administrative Expenses……….	$ 1,801,095.00	$ 1,864,006.00			
% of G & A to Sales………………………..	$ 0.26	$ 0.24			
Net Profit After Taxes…………………………	$ 327,257.00	$ 71,801.00	Onetime $169,585 income recognition in 08		

WORKING CAPITAL……………………..	$ 338,861.00	$ 353,175.00			
TOTAL NET WORTH……………………..	$ 1,289,823.00	$ 964,716.00			

DEBT TO EQUITY…………………………	0.54	1.16			

Experience

- History of Past Profitability
- Profit Fade
- Accurate Estimating
- Management team/capacity
- Subcontractor team
- Same Scope of work
- Geography

Backlog – Spread your Risk

- No one Job should be more than 50% of your backlog
- A Problem on 1 large job wipes out all equity

Communicate

- Schedule Regular meetings with Advisors
- Suretys hate surprises
- Changes in Company?
- Listen to Surety Advice

Off Balance Sheet Support

- S Corp with Strong owners
- No debt
- High Liquidity
- Personal Guarantee worth something

- Strong Bank/CPA Support
- Meeting all Covenants
- Bank Reference Letter
- Regular communication with professional team

Break

Contractors Issues & Best Practices to Not Only Survive, but to Thrive in a Period of Uncertainty

Scott Heintzelman, Partner – sheintzelman@macpas.com
Michael Hoffner, Partner – mhoffner@macpas.com
David Blain, Principal – dblain@macpas.com

Objectives

1. What Just Happened?
   A. Where are we?
   B. How did we get here?
   C. Why we will be here awhile.
2. Industry Trends – Contractors in General and Mechanical Specifically.
3. Action Steps – Ideas & Best Practices to Not Only Survive, but Thrive.

Three Components of This Recession

1. Normal Cyclical Recession.
   A. U.S. Personal Savings Rate

Three Components of This Recession

B. Consumer spending represents about 70% of our economy.

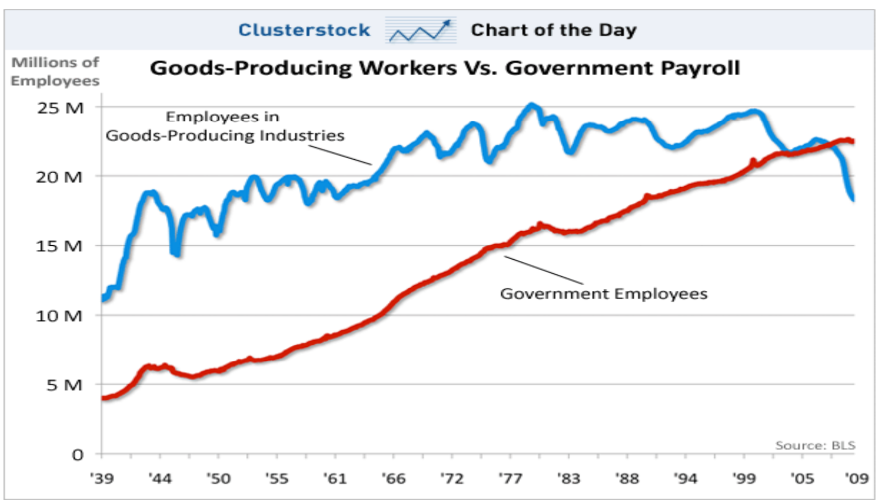
C. For every 1% move in the U.S. Savings Rate, it pulls about $100 Billion out of economy.

D. We went from 1% in 2005 to 8% in 2009 which put ¾ of a TRILLION Dollars on the Sidelines.

Three Components of This Recession

2. Decline of the Industrial Age.
   - A. During the past 20 years we have outsourced production.
   - B. Every year we become less of a producing nation and more of a consuming nation.

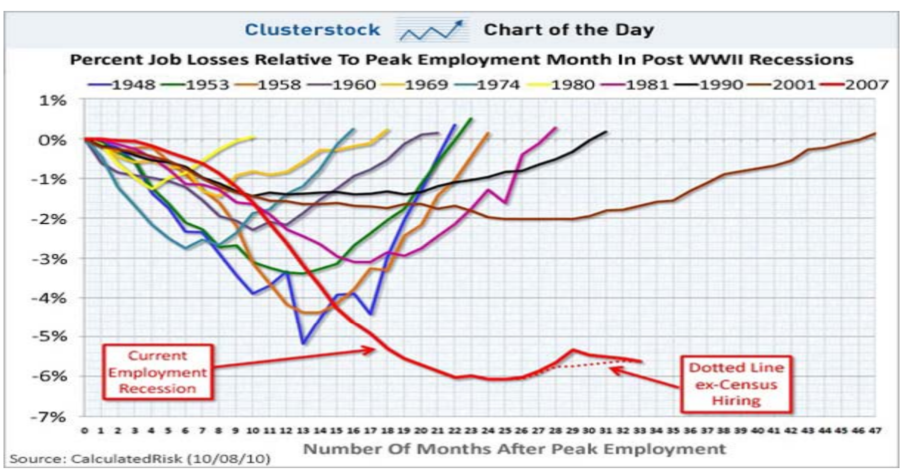
Three Components of This Recession



Three Components of This Recession

3. Standard of Living Continues to Rise with Cheaper Goods Being Imported.
   A. As real estate fell the house of cards started to collapse.
   B. Unemployment shot up – U-3 at 9.6% & U-6 at 17.1%.
   C. Many construction/manufacturing jobs not coming back any time soon.
   D. Need college degree or a skilled trade.

Three Components of This Recession



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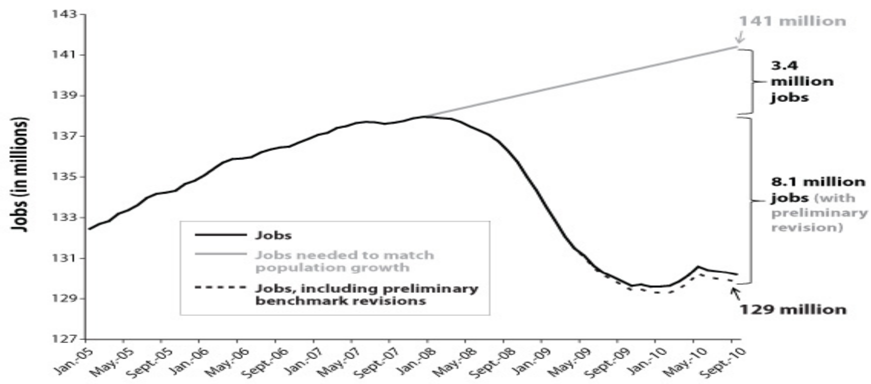
BEST ACCOUNTING FIRMS TO WORK FOR 08 09

Three Components of This Recession

Gap in labor market now 11.5 million jobs



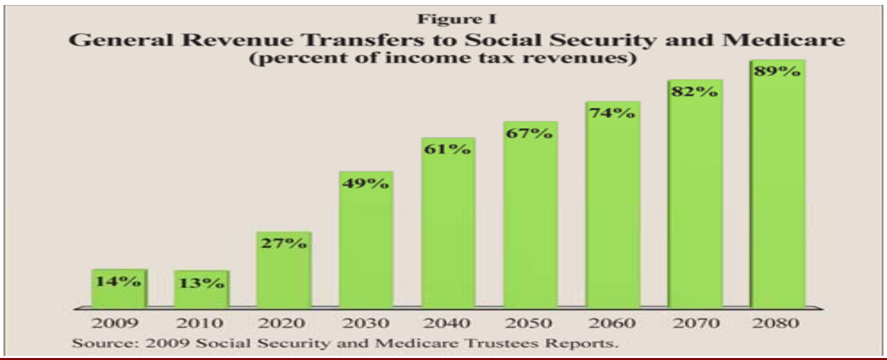
Source: EPI analysis of BLS and Census data.

How Long Will It Be Here?

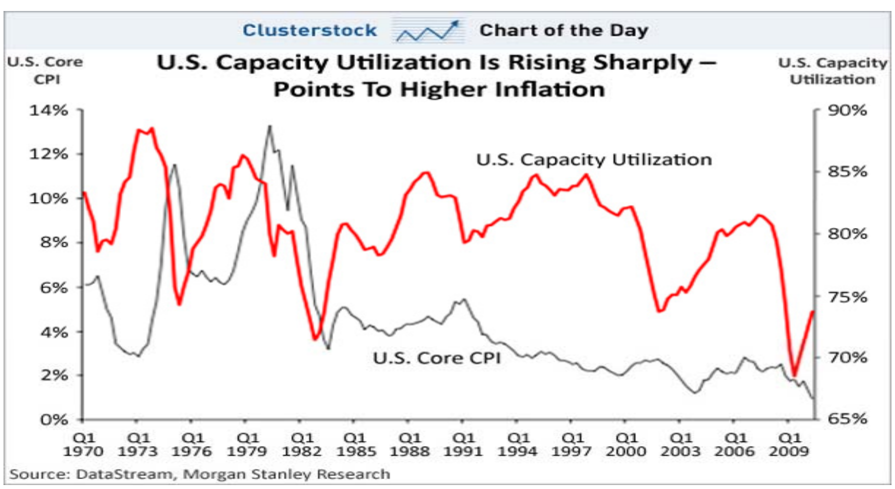
- Current National Debt: **$13.5 TRILLION**!
- Last two fiscal years produced $2.7 Trillion in debt.
- White House projects $10 Trillion additional debt in next 10 years.
- SS & Medicare Trustees Reports shows Unfunded Liability is $107 Trillion (without Obama Care).

How Long Will It Be Here?

- By 2020 it will take 27% of all tax receipts to pay these two programs.



How Long Will It Be Here?



Top Issues Facing the Construction Industry

- **Lack of Work & Low Margin Work:**
  - -- True cost of low cost yet to be known.
  - -- Winning bids below costs.
  - -- Many general contractors bidding on same project.

Top Issues Facing the Construction Industry

- **Subcontractors:**
  - -- Financial condition of subcontractors.
  - -- Prequalifying of subcontractors.

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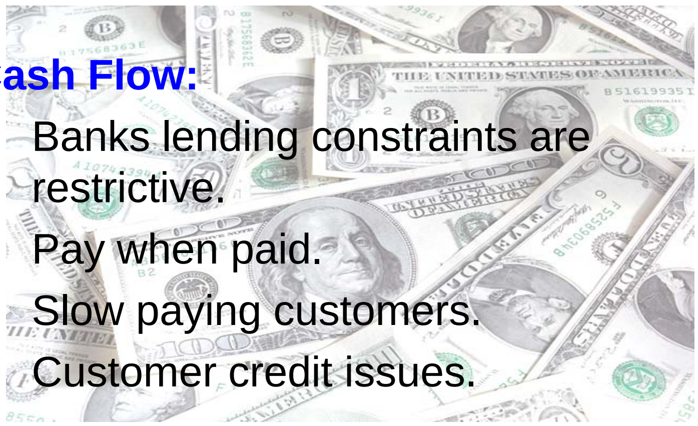
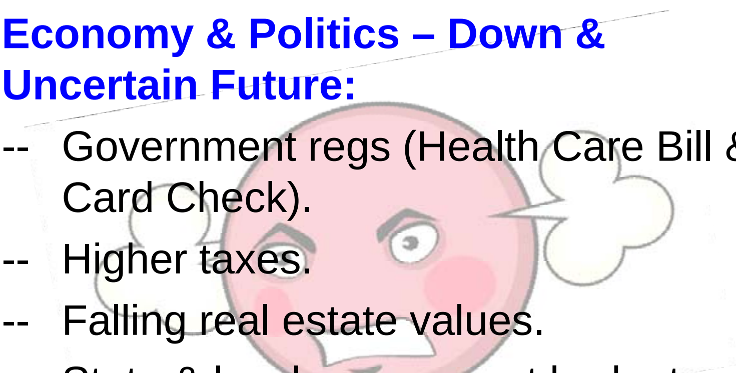
Top Issues Facing the Construction Industry



- **Cash Flow:**
  - -- Banks lending constraints are restrictive.
  - -- Pay when paid.
  - -- Slow paying customers.
  - -- Customer credit issues.

Top Issues Facing the Construction Industry



- **Economy & Politics – Down & Uncertain Future:**
  - -- Government regs (Health Care Bill & Card Check).
  - -- Higher taxes.
  - -- Falling real estate values.
  - -- State & local government budgets.
  - -- 25C Tax Credits expired.

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BEST ACCOUNTING FIRMS TO WORK FOR 08 09

Top Issues Facing the Construction Industry

- **Cost of Doing Business:**
  - -- Bonding difficulties.
  - -- Cost of healthcare & benefits.
  - -- Shortage of skilled craftsmen.
  - -- Misplaced loyalties.

Top Issues Facing the Construction Industry

- **Evolution of Accounting Standards:**
  - -- Revenue Recognition.
  - -- Lease Accounting.
  - -- Consolidation.
  - -- Convergence with International Standards.

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Ideas & Best Practices to Survive & Thrive

- Stop comparing current situation with past.
- Protect your margins.
- Reduce costs and focus on LEAN & efficient.
- Go Green.
- Focus on niches.

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Ideas & Best Practices to Survive & Thrive

- Public sector money is the fat wallet.
- Educate buyers on value added.
- Have risk transfer agreements in place.
- Aggressively pursue talent.
- Marketing is everything now.

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Ideas & Best Practices to Survive & Thrive

- Social media.
- Solidify future business through mergers & acquisitions.

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www.contractorscenterpoint.com

Contractors Center Point is led by Principal, David Blain and Partner, Michael Hoffner and communicates timely and relevant information that impacts the construction community. From information on LEED certification, federal and state stimulus information, insurance, tax, accounting, and other construction related matters, this blog is a great way to keep up to speed on the very changing construction environment.

www.exuberantaccountant.com

The Exuberant Accountant is written by Partner, Scott Heintzelman for business leaders as a way to communicate ideas, how new legislation will impact them, family business issues, leadership development, business strategies, and various best practices.

Break

Mechanics' Lien Law / AN OVERVIEW

Tom Williams

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Reager & Adler, PC

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What is a MECHANICS' LIEN?

- Claim securing priority of payment
- For value of labor and materials
- Lien against land and building

The mechanics' lien law is "intended to protect the prepayment of labor and materials that a contractor invests in another's property, by allowing the contractor to obtain a lien interest in the property involved."

Matternas v. Stehman, 642 A.2d 1120 (Pa. Super. 1994)

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A MECHANICS' LIEN is NOT an exclusive remedy

A mechanic's lien claim is only one of many potential remedies for non-payment

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§ 1301 Provides THE RIGHT TO FILE A LIEN

"Every *improvement* and the estate or title of the owner in the property shall be subject to a lien, to be perfected as herein provided, for the payment of all debts due by the owner to the contractor or by the contractor to any of his subcontractors for labor or materials furnished."

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IMPROVEMENT as Defined by § 1201(1)

Includes any building, structure or other improvement erected or constructed on land, together with the fixtures and other personal property used in equipping it for the purpose for which it was intended.

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What items can be INCLUDED IN THE CLAIM?

- Labor
- Materials
- Profit

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Who can be a CLAIMANT?

- Contractor
- Subcontractor
- Sub-Subcontractor
- Suppliers

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MATERIALS AS DEFINED BY § 1201 (7)

Building materials and supplies of all kinds, including fixtures, machinery and equipment reasonably necessary to and incorporated into the improvement.

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WHAT CANNOT BE INCLUDED IN THE CLAIM:

- Attorney's fees
- Interest
- Non-permanent fixtures
- Costs not related to the improvement

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THE REQUIREMENT to Complete the Work

Can you file a lien if you don’t complete the work under your contract?

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GENERAL RULE:

The claimant must complete its work to file a mechanic’s lien.

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§ 1201 DEFINES completion of the work as:

"Performance of the last of the labor or delivery of the last of the materials required by terms of the claimant's contract or agreement, whichever last occurs."

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§ 1305

"Except in case of destruction by fire or other casualty, where, through no fault of the claimant, the improvement is not completed, the right to lien shall nevertheless exist."

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§ 1305 ALLOWS A LIEN WHERE:

- Owner issues stop-work order.
- Owner takes some action that prevents contractor from completing its work.
- Claimant is “excused, hindered or prevented” from completing its work.

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FILING AND PERFECTING a Mechanics’ Lien

§1501 - 1503

* Unforgiving Statute *

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§ 1501(b) Subcontractor's

NOTICE REQUIREMENTS

Subcontractors must provide formal notice to the owner of their intention to file a mechanics' lien at least 30 days prior to filing the lien.

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§ 1501(c): NOTICE MUST INCLUDE:

- the name of the claimant;
- the name of the person with whom he contracted;
- the amount claimed to be due;
- the nature and character of the labor or materials furnished;
- the date of completion of the work
- a description of the property claimed to be subject to the lien.

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§ 1502 (a): FILING THE CLAIM

Claimant must file a mechanics' lien within six months after the completion of the work.

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§ 1503: THE CLAIM MUST STATE:

1) Name of claimant, and whether he files as a contractor or subcontractor
2) Name and address of the owner;
3) Date the work was completed;
4) If filed by a subcontractor, the name of the person with whom he contracted, and the dates on which notice of intention to file a claim was given;

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§ 1503 continued . . .

5) If filed by a contractor under a contract for a specific sum, an identification of the contract and a general statement of the labor or materials furnished;
6) In all other cases than that set forth in clause (5), a statement of the kind and character of the labor or materials furnished, and the prices charged for each;
7) The amount claimed to be due; and
8) A description of the improvement and the property claimed to be subject to the lien.

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CONTESTING a Mechanics' Lien

- rule to file a Lien under § 1506;
- preliminary objections;
- defend the action;
- set-offs; and
- discharge the lien.

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Preliminary OBJECTIONS

- Exemption or immunity;
- Claimant is not in the class of persons permitted to file a mechanics' lien;
- There was a waiver of liens;
- Claimant failed to comply with statute.

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Defend the Action

- Defective work or materials;
- Failed to follow contract's requirements for:
  - change order work
  - applications for payment
- Pay-if-paid clause (where claimant is a sub);
- Set-offs.

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DISCHARGE THE LIEN under §1510

Any party can request discharge of the lien where a sum equal to the lien or double in the form of a bond is deposited with the court for application against the amount found to be due to the claimant.

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ESSENTIAL ADVANTAGES

ENTERING OUR FOURTH DECADE

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Payment Bond Claims

Presented by:

Thomas Williams, Esq.
TWilliams@ReagerAdlerpc.com

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What is a SURETY?

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What law(s) govern PAYMENT BONDS and CLAIMS?

Governing law:
Federal = Miller Act
PA = Commonwealth Procurement Code and Pennsylvania Public Works Contractor Bond Law (little Miller Act)

Is there a SURETY PAYMENT BOND on my project?

If there is, how do I get a copy?

Is my company a proper CLAIMANT?

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How do I FILE A CLAIM on the payment bond?

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Bond claim REQUIREMENTS:

1) Covered items
2) Notice requirements and deadlines

** See statutory provisions and payment bond itself **

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Will the SURETY pay my claim quickly?

- Surety responses and reality

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The surety has denied my claim.

WHAT NEXT?

- Deadline to file lawsuit
- Where do I file my lawsuit?

Surety Defenses

- Surety steps in the shoes of its principal

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ESSENTIAL ADVANTAGES

ENTERING OUR FOURTH DECADE

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Thank You!

For those of you joining us for the networking mixer, please proceed to the Cathedral Room at the hotel's Elephant & Castle Pub and Restaurant.