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Start-Up Contractor Growing Pains

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Agenda

- ▶ **Business Processes**
 - ▶ Construction Accounting
 - ▶ Work in Progress
 - ▶ Budgeting
 - ▶ Cash Flow
 - ▶ Internal Controls
 - ▶ Accounting Systems
 - ▶ Key Metrics
 - ▶ Buy vs. Lease
 - ▶ Financing operations
 - ▶ Bonding
 - ▶ Business structure and entity selection

- ▶ **The CEO's Role**
 - ▶ Strategy
 - ▶ Metrics
 - ▶ People
 - ▶ Strategy
 - ▶ Customers & Markets

Successful Executives Know the Numbers

- ▶ They think in quantitative terms and everything relates back to costs
- ▶ They close the books within 7 to 10 days and roll out their backlog
- ▶ They have a strong understanding of finance and accounting
 - ▶ GP by day/week
 - ▶ Costs to complete

What Does it Mean?

- ▶ Do your financial documents answer these questions:
 - ▶ Are we making money?
 - ▶ Why ? or Why Not?
- ▶ Does the Contracts Schedule answer these questions for each job?

What is Unique About Construction Accounting?

- ▶ Billings are not revenues
- ▶ Long-term projects that often overlap two or more accounting periods.
- ▶ EARNED REVENUE must be calculated as “percentage of completion,” a ratio of cost to date divided by the estimated total cost.
- ▶ Overbillings are a liability (similar to deferred revenue)
- ▶ Underbillings are an asset (similar to a receivable)
- ▶ Total losses on projects must be booked for the entire project as soon as they are identified

WIP- Work in Process

- ▶ The WIP report is for you – not just for your bonding company
- ▶ The WIP reports tells you how much you have made on each job
- ▶ The WIP report tells you were you have made your money
- ▶ The WIP report can help you forecast future profits

Accounting

- ▶ **Financial Statement/Work in progress**
 - ▶ Tie the Job Status Reports to the Work in Process Report
 - ▶ Tie the Work in Process Report to the Income Statement and Balance Sheet

- ▶ **WIP Schedule**
 - ▶ By customer
 - ▶ By job type
 - ▶ By Owner
 - ▶ By job size
 - ▶ By GC

An Operating Budget Provides Focus

- ▶ Origin is the Backlog Rollout - “Your jobs”
 - ▶ Set Goals by Customer
- ▶ Includes:
 - ▶ Direct Expenses
 - ▶ Indirect Expenses
 - ▶ General & Administrative Expenses
- ▶ All department heads should be involved in the budgeting process
- ▶ Use your accounting software and track budget vs. actual
- ▶ Starting point is your existing P&L

Internal Controls

▶ Cash

- ▶ Segregation of Duties
- ▶ Who opens mail
- ▶ Who signs checks
- ▶ Who reconciles cash
- ▶ Who enters data into accounting software
- ▶ Who authorizes new vendors
- ▶ Who deposits the check
- ▶ Who posts cash receipts
- ▶ Who creates and enters bills
- ▶ Who opens bank statements (operations and payroll)
- ▶ Who can authorize a new employee

▶ Purchasing

▶ Estimating

- ▶ Budget vs. actual

Accounting Systems - Financial

- ▶ Quickbooks Pro, Peachtree - smaller contractor
 - ▶ 100,000 – 5,000,000
- ▶ Starbuilder, CF Data, Masterbuilder, Computerease – medium size, union reporting, certified payrolls
 - ▶ 5,000,000 – 50,000,000
- ▶ Timberline, Dexter Chaney – larger, more sophisticated packages

Managing Your Cash Flow

- ▶ Best of class billing practices
- ▶ Best of class change order process
- ▶ Contract negotiations
- ▶ Manage vendor relations
- ▶ Use email for collections
- ▶ Benchmark results against
 - ▶ “Best of Class”
- ▶ Prepare Cash Flow projections

Key Metrics: Know the Industry Benchmarks You Should Attain

	GC/CM	SUB
Gross profit (Coming out of the field)	10-12% 2-3%	20%
Operating profit	7-8% 1-2%	4-5%
Accounts receivable days (Includes retainage)	50	72
Accounts payable days (Includes retainage)	66	28
Debt/equity	3:1	2:1
Revenue/working capital	20:1	10:1

Buy vs. Lease Equipment

“How long do you want to hold the Asset”

Lease

- ▶ Avoid the cost of obsolescence
- ▶ Retain your capital
- ▶ Preserve bank credit
- ▶ Can charge directly to a job
- ▶ More cost effective for cars, computers and other equipment that decrease in value over time that you'll use for less than 5 years

Buy

- ▶ Less expensive in the long run
- ▶ Accelerated depreciation related tax deductions
- ▶ Equity in the equipment
- ▶ Interest payments deductible on your federal tax return
- ▶ For property you'll use for more than 5 years, buying is usually less expensive

Bonding: the Surety Bond Agent

- ▶ Primary surety contact – They represent you in the surety market and need to know everything
- ▶ Should be the first person to know about a problem
- ▶ Communicates concerns to underwriter & helps negotiate resolution
- ▶ Provides sound business advice
- ▶ Provide them with timely financial reports to maintain confidence
- ▶ SBA program

Business Structure

- ▶ C Corporation
- ▶ S Corporation
- ▶ Limited liability Partnership/Company (LLP/LLC)

Choice of Entity - Summary

- ▶ **Pass-through entity generally better (S Corp, LLC, LLP)**
 - ▶ One level of tax
 - ▶ Unreasonable compensation issue does not apply, reasonable compensation does apply

- ▶ **Partnership form generally better than corporate form**
 - ▶ More flexible in terms of compensation allocations
 - ▶ No entity level taxes

- ▶ **LLC provides best of both**
 - ▶ Limited liability
 - ▶ Flow through entity
 - ▶ Special allocation of profit and losses

- ▶ **Liquidation of corporation**
 - ▶ S Corp - one level of tax
 - ▶ C Corp - double tax on distribution of appreciated assets and accumulated earnings – Distributions and income is taxed

The CEO's Role

Strategy

- ▶ **Define your business**
 - ▶ What types of work do you do?
 - ▶ How do you do it? (your distinctive competencies)
 - ▶ For whom do you do it?
 - ▶ Where do you do it?
 - ▶ Elevator speech

Strategy

- ▶ Select the “Right Projects”: The key to making money in this business is learning which “opportunities” to avoid and having the discipline to say “no!”

- ▶ Michael Porter

Strategy

- ▶ **The Type of Work You Pursue**
 - ▶ Public building or private work?
 - ▶ Lump sum hard bid, guaranteed maximum price, design-build, etc.?
 - ▶ Residential, retail, office space, manufacturing, medical/health care, food service, or a strategic combination?

Strategy

- ▶ **Define Your Market Niche**
 - ▶ Provider of value-added services or low-cost provider?
 - ▶ Technical competencies?
 - ▶ Consistency/dependability
 - ▶ Industry leader

Strategy

- ▶ Define your “ideal” customer
- ▶ Define the criteria for your “ideal” type of project
- ▶ Define your “ideal” geographic area

Customer/Markets: Disciplined Thought

- ▶ Develop “Competitive Advantage”
- ▶ Delivers “WOW’s” to at least 30% of customers – 9/10’s measure
- ▶ Niche based – not just a good builder
- ▶ Reinforce why you are different and not a “company”
- ▶ Disciplined use of “Best of Class” behaviors in customer service delivery

Customers & Markets

Do they have:

- ▶ A positive track record in this type of construction?
- ▶ A management philosophy consistent with your company's?
- ▶ Resolve extras fairly and quickly?
- ▶ Pay requisitions fairly and on time?
- ▶ The proper financing?

Researching the Customer

- ▶ Understand the customer's legal entity
- ▶ Check for claims and judgments
- ▶ Obtain a credit report (D&B, Paydex – higher the better)
- ▶ Look at reputation within the industry
- ▶ Ask for a copy of last years financial statement, bonding letter, customer/vendor testimonials, professional references
- ▶ Google

People

- ▶ ***“It is better to hire people with the right work ethic and character and teach them how to make steel than to hire people who know how to make steel but lack the work ethic and character traits.”***

–Daniel DiMiccio, CEO

- ▶ **New England Patriots**

- ▶ Use data and metrics to select players-grades
- ▶ Does not have the “scouting services” other teams use-on field performance is a part of the decision
- ▶ Rates draft picks on nontraditional metrics-intelligence and willingness to sacrifice ego for the team
- ▶ Belichick – Intangibles

People

- ▶ Hire smart people
- ▶ The right people don't have jobs, they have responsibilities
- ▶ Right people are passionate about the Company
- ▶ Right people when hired share the core values

People

- ▶ Set goals – with employees and hold them accountable
- ▶ Groom the next leaders
 - ▶ Behaviors
 - ▶ Passion
 - ▶ Identify the winners early and retain them
 - ▶ Interact with the 25-35 year old employees
- ▶ Tracking/measurement for:
 - ▶ Mentoring

CEO's Role

- ▶ Asset vs. Revenue (long-term vs. current) – Don't "Milk the Asset"
- ▶ Look in the mirror
- ▶ Personal Strategic Planning – "Set the Goals"
- ▶ Stay current
- ▶ Focus – "Depth first, then breadth"
- ▶ Build rolodex
- ▶ Interpersonal skills – Read personality / react

CEO's Role

▶ Goal Setting

- ▶ Why are you more valuable this year than last year?
- ▶ What are you going to do to make yourself more valuable this year than last year?
- ▶ What are the new skills that you will acquire next year?
- ▶ What is your personal strategic plan over the next 3 years?
- ▶ What will you do to differentiate yourself in the marketplace?
- ▶ Communicate these goals and have someone hold you accountable

Break Out Session

- ▶ What roll do you play in your organization now....and what role do you want to have in 5 years?
- ▶ Discuss solutions to the 2-3 biggest time wasters you encounter.
- ▶ Discuss the ways that you try to use down time
- ▶ How do you leverage technology to get more work done In less time