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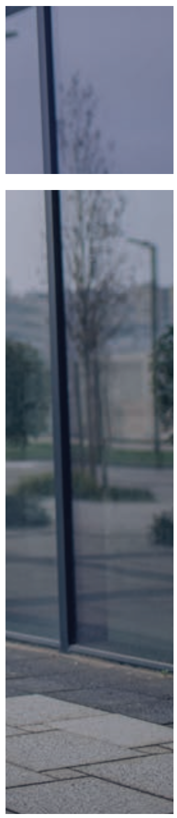

Entity choice

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Bits, bytes and building: The latest on BIM

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LIMITED PARTNERSHIPS AND LIMITED LIABILITY COMPANIES

When two or more like-minded individuals decide to launch a construction company, a partnership is often the most attractive entity choice. However, working in the building trade also involves a high degree of inherent risk that makes guarding against liability important. For this reason, many contractors look to either a limited partnership or limited liability company (LLC) as a business structure.

Limited partnership benefits

Indeed, a limited partnership is often an excellent entity choice for launching a new venture because it allows the business owners to raise capital from private investors while providing those investors with limited liability protection.

A limited partnership allows the general partners to manage and operate the construction business with little intervention from the other partners. In addition, general partners can raise equity capital from the investors, who receive limited partnership interests in exchange for their contributions. As limited partners, they'll share the entity's earnings without having to manage the company or risk personal liability for its activities.

General partners must exercise care to ensure that limited partners don't inadvertently lose the liability protection by participating in the management of the business. Merely consulting generally doesn't trigger personal liability so long as the general partners remain the decision-makers.

A limited partner may become personally liable by taking certain actions, such as guaranteeing a partnership debt. Of course, general partners must bear in mind that they're personally liable for the company's debt. (See "Two ways to minimize general partners' liability" on page 3.)

… and the tax impact

Because a limited partnership is a pass-through entity for tax purposes, each partner must include his or her share of income, deduction, credit and loss from the construction business on his or her individual federal tax return.

Had the partners decided to form a C corporation instead of a limited partnership, their earnings would have been taxed at a higher effective tax rate. This is because they would have been taxed once on the corporation's earnings and again when those earnings were distributed to shareholders.

Moreover, subject to various limitations, partners may qualify for the Section 199A "pass-through" tax deduction to the extent the income passed through to them is "qualified business income" under the tax code.

With proper planning, a limited partnership can be structured to provide special allocations of various tax benefits that make the venture more attractive to prospective investors. For this reason, a limited partnership may be a better choice for some new ventures than an S corporation. To pass muster with the IRS, however, special allocations must have what's known as "substantial economic effect." (Your tax advisor can explain further.)

The LLC difference

Similarly named but slightly different is an LLC. Think of an LLC as a hybrid entity that can be structured to resemble a partnership for federal tax purposes and a corporation for owner liability purposes.

Like the shareholders of a corporation, LLC owners (called "members" rather than shareholders or partners) generally aren't liable for the debts of the business except to the extent of their investment. Thus, the owners can operate the business with the security of knowing that their personal assets are protected from the entity's creditors.

This protection is greater than that afforded by limited partnerships. As mentioned, general partners are personally liable for the company's debts, and even limited partners can become liable if the IRS deems that they've been actively participating in business management.

LLC taxation

LLC members may elect to have the entity treated as a partnership for federal tax purposes. Doing so can provide several important benefits to the owners.

For example, partnership earnings aren't subject to an entity-level tax; instead, they "flow-through" to the owners in proportion to the owners' respective interests in profits. Earnings are reported on the owners' individual returns and taxed only once.

To the extent the income passed through to a member is qualified business income, he or she may be eligible for the Sec. 199A pass-through deduction, subject to various limitations. In addition, because members are actively managing the business, they can deduct their ratable shares of any losses generated by the company on their individual tax returns. This, in effect, allows a member to shelter other income that he or she (and a spouse) may have.

An LLC that's taxed as a partnership can provide special allocations of tax benefits to specific partners. For this reason, many business owners (construction and otherwise) opt for an LLC over an S corporation, an entity choice that provides tax treatment similar to a partnership's.

Another reason for using an LLC over an S corporation is that LLCs aren't subject to the tax code's restrictions on S corporations, which include limits on the number of owners and the types of ownership interests that may be issued.

Many choices

To be clear, limited partnerships and LLCs are but two of many entity choices. Whether launching a new construction company or reconsidering the business structure of an existing one, it's important to consider all the tax, legal and administrative implications. Your professional advisors can help you choose wisely. ■

TWO WAYS TO MINIMIZE GENERAL PARTNERS' LIABILITY

One drawback to a limited partnership is that general partners are personally liable for the entity's debts. This is the "price" a general partner must pay in exchange for the right to operate and manage the enterprise.

The risk of liability can be minimized somewhat by:

1. Creating a corporation to manage the partnership and serve as general partner, and
2. Procuring adequate insurance to cover potential liabilities arising from operating the business.

ASSESS THE RISKS BEFORE JUMPING INTO AN M&A DEAL

Construction companies are no strangers to mergers and acquisitions (M&A). In fact, M&A transactions in the construction and real estate industry totaled $10.4 billion in the United States during June 2021 alone, according to international analytics firm GlobalData.

If you think your business might engage in an M&A deal in the near future, assess the risks carefully before jumping in.

Core competencies

When buying a competitor, perhaps the biggest mistake construction owners make is acquiring targets that lack synergies with their own companies. For example, a commercial roofing contractor and a residential roofing contractor would seem to have much in common. Yet the two require different skills, equipment and employee training. The two types of businesses also tend to vary dramatically in terms of financial structure.

The best way to avoid "swerving into the other lane" — and, possibly, disaster — is to specifically define your core competencies. In other words, what do you do best? Then identify an opportunity for growth that's not going to stretch you too thin or take you too far afield from your areas of strength.

Cultural factors

Every company has its own culture. Some organizations are "top-down" (the boss gives the orders), strict and methodical. Others have a more free-wheeling, collaborative feel. Often, a business is a blend of both — reflecting the will of leadership and the ideas of its workforce.

There's no single "right way" to establish a company's culture. But two businesses with vastly different

organizational structures, accountability measures, schedules and employee expectations can crash into each other when trying to form a new, combined entity.

For example, commercial plumbing contractor A acquires commercial plumbing contractor B. Company A has, for years, required all its project managers to submit daily logs detailing exactly what was completed at each job site. Company B has never had such a requirement. As one might imagine, it may take some persuading on the part of management to get project managers from the former Company B to comply with the more rigorous reporting rules.

So, what can be done? One strategy is to reinforce that all employees are being judged by the same measures. Merging companies must have one set of expectations for everyone from managers to laborers, and these rules must be clearly defined and communicated to everyone. A post-transaction consultant can help with this process.

Rebranding is another strategy for bringing together a combined workforce after a merger. Establishing a new company name, logo, branding guidelines and mission statement can go a long way toward unifying a newly formed team.

Financial details

Owners who focus only on getting "a great deal" often underestimate the full financial implications of an M&A transaction beyond the initial purchase price.

One way to understand what a merger's full costs may be is to hire a private investigation firm to vet the company you're interested in buying. Although businesses have a legal obligation to disclose financial information and outstanding liabilities, intangibles such as bad management and a disgruntled workforce may not be captured in the sales proposal.

In addition, you'll need to work with your financial advisors to come up with reasonable projections regarding, among various factors, debt load, cash flow and tax liability. Getting bigger may not immediately translate to profitability.

Customer concerns

During and after an M&A transaction, it's easy to focus on assimilating the two companies. But don't forget about the important people who are along for the ride: your customers.

For contracts already signed and jobs in progress, clear communication is vital. Notify them of company name changes and new personnel as soon as possible. For future work, maximize the marketing opportunity. You're not just a bigger construction company, you're a better one. Tell people about the change in a timely manner and explain how it may or may not affect them.

Complex arrangements

An M&A deal may seem like a simple way to grow your construction company. However, these arrangements are typically anything but simple. Work closely with your professional advisors to evaluate the opportunity. ■

8 WAYS TO RUN A LEANER CONSTRUCTION COMPANY

For years, contractors have been urged to explore and adapt "lean" practices originally pioneered in the manufacturing sector. The challenge and benefits of doing so remain. Today's construction companies need to maximize resources and streamline processes to stay competitive. Here are eight ways to run leaner:

1. Transport for maximum efficiency. The unnecessary transport of equipment, materials and workers before they're needed results in a misuse of time and effort. You can reduce inefficient transportation by using fleet management software and identifying other ways to better coordinate on-site workers and complete job tasks.

2. Improve your inventory system. Although having some inventory on hand may help keep jobs moving, lean practices favor just-in-time delivery as opposed to just-in-case inventory. For example, instead of allocating cash and storage space for a stockpile of extra tools and materials, consider investing in reusable items such as guard rail systems or concrete formwork instead of two-by-fours that get tossed at the end of a project.

3. Prevent overproduction. In construction, overproduction occurs when a task is completed faster than scheduled or before the next sequential task is ready to start. It may seem like a good thing, but these scenarios can result in downtime or wasted materials. Plus, the jobsite can become needlessly congested, which may raise safety risks.

4. Monitor motion. Under a lean approach, "motion waste" refers to unnecessary movement or unproductive activities. Examples include making multiple trips across the jobsite to obtain materials or using unnecessarily labor-intensive processes when a better option is available. Extra movement and exertion increase the likelihood of accidents and may put workers at risk of fatigue or injury — especially in extreme or inclement weather conditions.

5. Track and avert defects. Costly rework arises from anything done incorrectly the first time. For instance, elements may be installed against specifications or building codes. Although you probably can't eliminate all errors, you can capture and monitor data related to defective work and engage in a continuous effort to reduce them.

6. Reduce excess processing. Also known as "overprocessing," excess processing refers to redundant steps that don't add value, such as altering or double-handing supplies or materials. It also refers to inefficient administrative workflows, such as double data entry, multiple signatures on forms, redundant daily reports, and the unnecessary forwarding or copying of emails.

7. Shorten or eliminate long waits. When workers must wait for materials or equipment to be delivered, or for preceding work to be completed, workflow is disrupted. Productivity also drops when project team members must wait for plans, information requests, job progress updates or approvals. Digital solutions, such as construction management software and mobile apps, enable project teams to share information in real time from anywhere.

8. Maximize talent and skills. This may be the most difficult lean measure to take given the ongoing skilled labor shortage in construction. Nonetheless, make sure you're fully aware of the skill sets and potential of everyone on staff.

Conduct regular performance evaluations and provide training and upskilling as budget and time constraints allow. Employees are your greatest asset — use their talents, creativity and knowledge to make your construction business as lean and profitable as possible. ■

BITS, BYTES AND BUILDING: THE LATEST ON BIM

The roots of building information modeling (BIM) lie in manufacturing and computer-aided drafting. Over the years, this high-tech tool has transitioned from a desktop design tool for architects to a valued collaboration tool among all stakeholders in a construction project — including contractors.

Mobile devices and cloud-based technology have made data-packed BIM models easier to work with, providing a central, multidimensional representation of every aspect of a project throughout its lifecycle. Let's look at three ways that BIM is being used on today's jobs.

Remote collaboration

More contractors are adopting digital tools to comply with COVID-19 safety regulations and reduce the risk of transmission among team members. A cloud-based repository and BIM workspace enables users to work on shared models simultaneously. That way, you can access real-time models and project data via laptop or mobile device from anywhere at any time.

> Newer BIM solutions now offer virtual reality and augmented reality tools.

In most cases, BIM updates are instantly communicated to all project members. So, you can better predict job costs, identify design clashes and resolve construction issues before work begins. Then, you can run simulations of the construction schedule to create a visual representation of the job to optimize each phase.

Virtual walkthroughs

Newer BIM solutions now offer virtual reality (VR) and augmented reality (AR) tools. With these, contractors can present stakeholders with immersive "virtual walkthroughs" of the design or project. With VR, a user can use a headset to become immersed in the BIM model.

AR superimposes digital objects over the real world. So, for instance, users can use AR glasses or a mobile app to examine BIM models in full scale, superimposed over the physical site in front of them. AR applications also can use markers — such as QR codes, architectural drawings, images and GPS — to overlay BIM models.

Digital twinning

BIM models can create "digital twins" — virtual models of structures that include data gathered by lasers, sensors, drones and the Internet of Things. Data is processed using artificial intelligence and advanced analytics. Once a project is finished, contractors can turn over the as-built virtual model complete with all important data of the project's elements, including parts and history.

From there, owners integrate the model with services, such as computerized maintenance management system tools, to track and schedule maintenance and ensure the structure is running efficiently. Building managers can monitor and automate electrical and HVAC loads and maintenance tickets.

A continuing need

With COVID-19 still hovering, the need for advanced remote collaboration continues. Keep tabs on the latest features of BIM, as this tech tool or one like it may soon affect one of your jobs if it hasn't already. ■

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- We develop **relationships with lenders and bonding agents** and understand how to present your financial picture in their preferred format.
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