



Today's Contractor

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Business Ownership: What Structure Is Best?

As a contractor, you have unique financial, tax, and liability concerns, which should be addressed by the form of business ownership you choose. In particular, how you structure your business will determine your tax treatment and your liability risk. As your construction company grows, ownership changes, reassessing your initial choices is wise. This article explores the characteristics of five basic business structures: sole proprietorships, partnerships,

C corporations, S corporations, and limited liability companies (LLCs).

Sole Proprietorships

The vast majority of small businesses start out as sole proprietorships, but contractors should beware of the personal liability risk. One person owns a sole proprietorship and typically runs the business. Sole proprietors own all assets and profits, and income is subject to individual income tax, as well as self-employment tax. The sole proprietor assumes personal liability for all aspects of the business, including debt and legal action taken against the business.

Partnerships

Two or more people own a partnership, and there are several types, including: general partnerships, limited partnerships, family limited partnerships, and limited liability partnerships. A legal agreement generally specifies how profits will be shared, delineates management responsibilities, and provides guidance for resolving disputes and



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Important Guidelines for Employment Recordkeeping

Given the day-to-day production demands of running a construction business, paperwork and filing can quickly become last on a list of priorities. But good recordkeeping can help minimize your risk in the highly regulated arena of employment. With an organized approach, you can minimize the time spent on paperwork and more easily ensure you are complying with standard employment practices.

EEOC Guidelines

Many federal employment laws were enacted to protect employees from discrimination in the workplace. Small construction companies with fewer than 15 or 20 employees may be exempt from certain rules. Even contractors not subject to Equal Employment Opportunity (EEO) regulations because of their size should consider following these federal guidelines. In the event an employee or former employee takes legal action, failure to keep proper records could hurt your defense during litigation. At some point, the onus may be on you to prove that your employment practices are lawful and comply with federal regulations. Without substantive documentation, this may be difficult, if not impossible.

In short, the EEO regulations stipulate that employers should preserve all employment records for one year. Records for employees who are involuntarily terminated should be preserved for at least one year following the date of termination. If action is taken against you, keep all relevant records until the charges are resolved.

ADEA, FMLA, FLSA, and EPA Regulations

In order to comply with the Age Discrimination in Employment Act (ADEA), the following records should be kept for three years: payroll

documentation that includes an employee's name, address, age, occupation, pay rate, and weekly compensation. The employer should also preserve records of an employee's benefit plan with information regarding seniority and merit systems while the plan is in effect and for one year following its termination.

Information regarding employees and the Family and Medical Leave Act (FMLA) should also be kept for three years, including: payroll records, dates and hours of FMLA leave, employer policies and procedures, and any pertinent medical information.

For recordkeeping purposes regarding the Fair Labor Standards Act (FLSA) and the Equal Pay Act (EPA), it is also important to keep payroll records for three years, as well as information regarding wages, rates, contracts, job descriptions, merit and seniority systems, and collective bargaining agreements for two years.

What Else and for How Long?

Time and information such as records and any relevant procedures should be kept for two years and employee applications for one year. If you use independent contractors, keep the contracts and their insurance information, plus all employment-related tax information, for four years from the tax due date.

Workers compensation regulations vary by state, so check with the appropriate state agency for more information on full compliance. In today's litigious world anything can be alleged. Complying with state and federal regulations can help protect your company's interests.

Recordkeeping Guidelines for Contractors

1 Year

Employment records, employee applications, résumés, physical exam results, information regarding promotions, demotions, and transfers, layoff and termination documentation, and requests for accommodation.

3 Years

Employee information such as date of birth, gender, and occupation, Form I-9 (employment eligibility verification form), payroll records, FMLA-related information, employer policies, wage rates, contracts, job descriptions, collective bargaining agreements, merit and seniority system documentation.

5 Years or More

OSHA safety forms, employment-at-will policies, equal employment policies, employee benefit plan summaries and related information, and affirmative action plan documentation.

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dissolving the partnership. General partners face unlimited personal liability, whereas limited partners assume liability no greater than the capital they contributed.

Tax treatment is similar to that of sole proprietorships. The partnership entity is not taxed; however, partners are subject to income tax on their compensation, plus self-employment tax, if applicable. Losses also pass through to partners, and restrictions on deductibility apply. Because of this “pass-through” taxation, partnerships avoid the double taxation that corporations may face.

C Corporations

Shareholders own a corporation, which is considered by law to be a unique entity separate from those who own and run it. The corporation pays corporate tax, and the shareholders pay tax on the income they receive as dividends. This double taxation can be a disadvantage, particularly for contractors who are not in a position to reinvest a significant portion of profits back into their business.

One advantage to this structure for construction businesses is the protection it offers from personal liability. Owners are personally shielded from debt liability and lawsuits against the company; only the amount of their investment is at risk.

S Corporations

S corporations, which limit ownership to 75 shareholders, share characteristics of C corporations and partnerships. This form of pass-through

entity generally does not pay corporate income tax and permits the shareholder to treat company earnings and profits as distributions. This income depends on the shareholder’s percentage of ownership and passes through directly to his or her personal tax return, thereby avoiding double taxation and self-employment tax. Shareholders

may also deduct losses, limited to their basis in the business. State tax treatment may vary.

As with C corporations, shareholders are protected from personal liability. Only their investment in the company is at risk.

Limited Liability Companies

A limited liability company (LLC) provides the limited liability benefits of a corporation and the tax efficiencies and operational flexibility of a partnership. Members of an LLC are protected from personal liability, risking only their investment in the company. Most states require LLCs to have at least two

members, but there is no maximum limit.

An LLC’s profits and losses pass through to members, who then pay income tax on these distributions. Self-employment tax may apply. Because LLCs are pass-through entities, they are not subject to federal tax at a corporate level, provided they have more partnership than corporate characteristics. The IRS classifies an entity as a partnership if it lacks at least two of the following four corporate characteristics: limited liability, centralized management, continuity of life, and free transferability of interests. State tax treatment may vary.

As you can see, each business structure has its advantages and disadvantages. Your choice will affect the taxes you pay and your personal liability risk. For help evaluating which entity is best for your construction business, call us.



TEA-21 Reauthorization Update

Just before a five-month Transportation Equity Act for the 21st Century (TEA-21) extension expired, Congress and President Bush again extended federal highway and highway safety programs, this time through April 2004. On February 12, 2004, the Senate passed a reauthorization bill (S. 1072) worth an estimated \$318 billion, which would fund highway, transit, and safety programs for six years with \$296 billion in funding guaranteed. Meanwhile, the House passed a less expensive bill worth an estimated \$275 billion, which is still more costly than Bush's \$256 billion proposal. At the printing of *Today's Contractor*, the House and Senate were fast at work on a compromise.

Steel Prices Surge

Soaring steel prices and shortages are delaying jobs, increasing the overall cost of contracts, and ultimately may boost the cost of heavy equipment and work trucks by as much as 3% to 5%. In response, some states are incorporating steel escalation clauses in new contracts. In a speech to the Associated General Contractors of America (AGC), Mary Peters of the Federal Highway Administration (FHWA) affirmed the actions that states have taken to alleviate the market challenges. However, the FHWA does not support retroactive adjustments on pre-existing contracts. On a federal level, the AGC also seeks fair adjustments on new and pre-existing federal contracts, as well as state and local projects that receive federal funds.

construction trend update

According to McGraw-Hill Construction, new construction rates increased by 4% in February 2004 to a seasonally adjusted rate of \$535.6 billion. Nonresidential building increased 7% to \$148.3 billion. Office construction, the largest dollar segment in this category, surged 39%. Nonbuilding construction was reported at \$78.3 billion, with the public works segment increasing 4% from January. Residential building increased 4% in February to \$308.9 billion. While single family housing rose 2%, multifamily housing increased by 21%.

Robert A. Murray, vice president of economic affairs for McGraw-Hill Construction states, "Housing remains very healthy, and the upturn

for nonresidential building in February was a welcome development after a sluggish January."

January and February 2004 had an unadjusted gain of 2%. The regional breakdown of these two months is: the South Atlantic, up 11%; the West and the Midwest, unchanged; the South Central, up 1%; and the Northeast, down 8%.

Dodge: Year-to-Date Construction Contract Value Unadjusted Totals, In Millions

	2 Mos. 2004	2 Mos. 2003	% Change
Nonresidential Building	\$19,866	\$21,402	-7
Residential Building	42,180	37,438	+13
Nonbuilding Construction	<u>11,811</u>	<u>13,524</u>	-13
Total Construction	\$73,857	\$72,364	+2