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Put some PEP in your step

A new retirement plan option to consider

For construction companies struggling to find skilled labor, a generous benefits package that includes a robust retirement plan can be a powerful recruiting tool. But providing cost-effective, high-quality retirement benefits for employees can be a challenge — especially for small businesses.

One new option to consider is a pooled employer plan (PEP). This variation on a multiple employer plan (MEP) was created by the SECURE Act of 2019 and became available just this year. PEPs allow participating employers to take advantage of group purchasing power and other benefits without the drawbacks that made traditional MEPs unworkable for many companies.

Pros to MEPs

A MEP is a defined contribution retirement plan, typically a 401(k) plan, maintained by two or more employers. The plan sponsor may be one of the participating employers or a third party, such as a trade association or professional employer organization. MEPs offer several significant advantages, including:

Cost savings. Group purchasing power and other economies of scale tend to lower the overall cost of providing a retirement plan.

Time savings. Participating employers avoid time-consuming and often disruptive administrative tasks. This allows them to focus on running their businesses.

Professional oversight. The MEP sponsor is responsible for plan design and day-to-day management. It coordinates with various third-party service providers, handles compliance issues, and oversees annual audit and reporting requirements. The sponsor may also provide participating employers with access to expertise and advanced technology that the participants might not otherwise be able to afford.

Reduced liability. Participating employers can shift some — though not all — of their fiduciary duties and liability exposure to the MEP sponsor.

And some drawbacks

However, traditional MEPs have drawbacks as well. For one thing, to be treated as a single employer plan for reporting, audit and administrative purposes, a MEP must be "closed." That is, its members must share some "commonality of interest," such as being in the same industry or geographical location.

Employers that join "open" MEPs, which don't require a commonality of interest, are treated as if they maintained separate plans with their own reporting, audit and other compliance responsibilities. (Note: Certain smaller plans — generally, those with fewer than 100 participants — aren't subject to audit requirements.)

Another big drawback of traditional MEPs is the "one bad apple" rule. Under that rule, a compliance failure by one participating employer can expose the entire MEP to the risk of disqualification.

Some employer fiduciary duties remain

A primary advantage of pooled employer plans (PEPs) is they allow employers to hand off many of their fiduciary responsibilities — as well as the associated liability risks — to the pooled plan provider (PPP).

However, that doesn't mean that employers are off the hook completely. Although the PPP assumes responsibility for most reporting and day-to-day administrative functions, employers retain fiduciary duties for selecting and monitoring the PPP. Employers may also remain responsible for investment selection, unless the PPP engages a discretionary investment manager.

Perhaps most important, employers cannot avoid responsibility for providing the PPP with accurate information regarding employee hire dates, compensation, hours worked, elective deferrals, matching contributions and other such data points.

The PEP solution

Under the SECURE Act, a properly designed PEP avoids both the commonality-of-interest requirement and the one bad apple rule. PEPs are treated like single employer plans for reporting, audit and other compliance purposes — even if they allow unrelated employers to join. One participating employer's compliance failure won't jeopardize a PEP's qualified status so long as the plan contains certain procedures for dealing with a participant's noncompliance.

PEPs are available from "pooled plan providers" (PPPs), which include financial services companies, insurers, third-party administrators and other firms that meet certain requirements. For example, PPPs must register with the U.S. Departments of Labor and the Treasury. They must also sign a written acknowledgement that they're the PEP's named fiduciary and plan administrator, and they need to ensure proper bonding of those who serve as fiduciaries or handle plan assets.

Although PEPs eliminate some of the obstacles that make traditional MEPs impractical for many companies, they're not without disadvantages. For instance, PEPs have limited flexibility to customize plan designs or investment options to meet the needs of specific employers and their employees.

Also, while one of the advantages of PEPs is cost savings, they may *increase* costs for participating employers in one area. That's because small employers aren't subject to annual audit requirements, but PEPs are. So, small employers that join a PEP will have to bear annual audit costs they otherwise wouldn't, though these costs are spread out among the PEP's participants.

It's also important to keep in mind that, while employers can shift certain fiduciary obligations to the PPP, employers aren't completely shielded from liability. (See "Some employer fiduciary duties remain" above.)

Do your homework

A PEP can be an attractive option for providing employees with valuable retirement benefits. If your construction company decides to pursue one, work with your professional advisors to weigh the pros and cons and to select the right provider. Among other things, you should:

- Evaluate the PPP's level of experience and management team's expertise with PEPs, MEPs or other group plans, and
- Review the PEP's policies and written agreements to be sure you understand the level of fiduciary responsibility the PPP is assuming, and which responsibilities will be delegated to other providers.

Also, get a feel for the PPP's level of transparency about its operations and types of reports you can expect from it. Without good communication from the PPP, you'll face difficulties monitoring and evaluating its performance. ■

Is the research credit within your reach?

Many construction company owners might assume that a tax credit related to research and development is out of their reach. Au contraire — contractors can and have claimed the research credit for improving construction techniques or developing industry-related software. Here's a refresher on this potentially valuable tax break.

Making the grade

Essentially, the research credit allows a business to reduce its federal and state income taxes by a percentage of the eligible expenses incurred for qualified activities. Such activities are qualified by a four-part test.

The improvement by the new tool, process or technique must be evolutionary or advanced in nature.

First, you need to spend time and money developing a new tool, process or technique for your business and/or industry. A product might be a new tool, whereas a process or technique could be a methodology for improving the performance, efficacy or efficiency of your construction activities.

The improvement by this new tool, process or technique must be evolutionary or advanced in nature. In other words, you can't claim the credit for a personal taste item like the mixing of a new color of paint. The new tool, process or technique needs to be a novel design element or a new approach for construction. Fortunately, 2003 U.S. Treasury regulations lowered the standard

from "revolutionary development" in the industry to "evolutionary development," easing access to the credit while retaining some stringency.

The second test stipulates there must be uncertainty before the research is performed. Innovation, by definition, can't be a slam dunk. The new tool, process or technique must spring from questions such as, "How could we redesign this tool to perform better and yield improved results?" or "Could our construction company actually perform this technique on our projects and see appreciable benefits?"

The third test dictates that an activity must evaluate different alternatives by experimentation of some sort. The experimentation should try to eliminate the uncertainty of whether a tool, process or technique will work by either building models of a product, simulating a process or technique on a computer, or conducting trial-and-error tests of a process or technique to find the best way.

The fourth test states that the activity must be technological or scientific in nature. In other words, it must use the physical, biological or computer sciences.

For example, you might synthesize chemicals to develop a new construction product or implement physical science or engineering principles to come up with a new building process or technique. (To be clear, you don't need to have invented or discovered the chemistry, physical science or engineering principles applied.)

Identifying your costs

If your research activities meet the four tests in the eyes of the IRS, you can include many of the associated costs as qualified expenses when claiming the credit. Specifically, expenses eligible for the credit must be direct costs incurred while performing, supervising or supporting your research.

Examples include costs associated with laboratory-style experiments (performing), and expenses incurred so project managers or others can supervise research (supervising). A third example is the cost of fabricating tools or components while doing research (supporting).

Direct costs of materials and supplies will typically qualify as long as they're clearly associated with the research. Administrative costs are usually ineligible because they're considered overhead. Travel, telephone costs and rent expense are also ineligible for the same reason.

A contractor's eligible expenses can also include 100% of wages paid to employees working on the qualified activities and supplies or materials costs incurred directly for those qualified activities. These must be payroll wages (including bonuses) but not pretax benefits such as a retirement plan or health care insurance.

Qualified research expenses may also include hiring subcontractors to work on the research project. However, eligible subcontractor expenses include a lesser 65% of the amount paid to them for qualified activities.

Getting credit for your work

Here's another possible surprise: You may have already done the work to qualify for this tax break. If so, now it's time to get credit — literally! Ask your CPA for more information. ■

7 coping strategies for volatile steel prices

The COVID-19 pandemic has disrupted steel supply and demand throughout the world. The problem was especially bad in the early months of the crisis. As the global economy and steel industry have reacted, steel prices have generally risen.

Although prices are expected to stabilize at some point, contractors may still see occasional spikes. Here are seven strategies to keep in mind:

1. Adjust your bids. Consider building some cushion into your bids to reflect the risk of price increases, being careful not to price yourself out of competition for jobs. Also, look into whether you should bid on more low-risk jobs, which are typically less vulnerable to changing material prices.

2. Put an expiration date on your bids. Keeping bids open for a relatively short time (30 days, for example) can help protect against sudden fluctuations in the price of steel or other materials. You can always extend the time, if appropriate, provided you confirm the price of materials beforehand.

3. Buy in advance. Purchasing steel or other materials in advance can help you lock in current prices and avoid shortages, provided you have a good handle on your needs and can weather the storage costs and impact on cash flow. Try to negotiate contracts that provide for release of funds early enough to buy in advance when needed.

4. Include escalation clauses in your contracts. These clauses shift some of the risk of fluctuating steel prices to owners by providing for periodic price adjustments that reflect the changing costs. Despite the name, owners will be more likely to accept these clauses if they also provide for *downward* price adjustments in the event steel prices drop.

Design escalation or price adjustment clauses carefully to clarify when prices will be adjusted, under what circumstances and by how much. For instance, these clauses usually provide for an adjustment if changes in a material's price exceed a certain threshold (such as 2% or 3%), as evidenced by a published price index or, in some cases, by the contractor's actual supplier invoices. It's also common for prices to be adjusted at fixed intervals (for example, quarterly) during a job or at the end of the contract.

5. Review existing contracts. Find out whether existing contracts contain escalation or price adjustment clauses. If not, determine whether other contractual provisions, such as force majeure or change-in-law clauses, are written to protect you against sudden materials shortages or price increases. Consider specifying in future contracts that unavailability of certain materials is an excusable delay under a force majeure clause.

6. Establish agreements with fabricators. If you use prefabricated building products, consider the impact of rising steel prices on fabricators. If possible, secure written agreements with them that lock in prices for a specified period.

7. Excel at communication. Whichever strategies you use to mitigate the impact of volatile steel prices, put the effort into developing and maintaining strong supplier relationships. Good communication will help you keep abreast of developments that may affect prices. You'll be more likely to learn about opportunities to lock in prices for specified periods, as well as to gain access to the materials you need when there are shortages. ■

Adding value with life-cycle cost analysis

In today's challenging economic environment, many construction companies are looking for a competitive edge that distinguishes them from other contractors in their markets. One way to differentiate yourself is to offer customers value-added services beyond your usual functions on a job site.

Life-cycle cost analysis (LCCA), for example, can create a new source of revenue for your construction company while providing long-term added value for property owners.

A sustainable approach

Typically, preconstruction analysis looks at upfront costs — such as land acquisition, design, construction and mechanical equipment. LCCA goes beyond identifying these initial costs to estimate a construction project's overall cost of ownership over its "useful life cycle." It then strives to identify design or construction alternatives that will minimize costs over that life cycle.

In many cases, investing in these alternatives, though they may cost more up front, can pay off over the long term in lower operating costs. Examples include:

- Energy and water conservation measures (such as energy-efficient building envelopes, lighting or HVAC systems),
- Design alternatives that enhance a building's residual value (such as incorporating techniques that make it easier for a buyer to adapt the building to other uses), and
- Alternative building approaches that streamline the construction schedule.

An LCCA examines various factors affecting the cost of operating a building — from utility and labor costs to available tax credits, grants and rebates for energy-efficient properties.

The contractor's role

Ideally, an LCCA should be conducted as early as possible in a project. This way, its findings can be incorporated into critical choices regarding design, materials and scheduling.

To help identify the highest value design and construction solutions, you'll want to form a multidisciplinary team to share expertise and reach a consensus. Such teams typically include architects, engineers, estimators, construction professionals and other experts.

Ideally, an LCCA should be conducted as early as possible in a project.

One critical topic of conversation should be the project delivery method. LCCA is generally best suited to design-build projects, which usually involve all the aforementioned disciplines from the beginning.

In addition to recommending upfront investments that can streamline the construction process, an LCCA-friendly contractor can help identify design, construction, equipment or materials choices that will likely reduce long-term energy or other operating costs. Knowledgeable contractors can also enhance the building's residual value or otherwise improve the owner's return on investment.

Getting started

To start exploring the feasibility of adding LCCA services to your construction company's repertoire, research continuing education and training courses both online and at local trade schools. Although the potential benefits are considerable, you'll want to be fully committed to the concept before investing time and money into it. ■