UHY LLP
Certified Public Accountants

CONSTRUCTION INSIDER

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CORONAVIRUS (COVID-19) – GUIDANCE FOR CONTRACTORS

The Coronavirus pandemic has been covered extensively since the start of 2020. The potential impact of the Coronavirus is wide-reaching. This involves onsite and offsite impacts including labor shortages, production delays, transportation embargos or even governmental actions. So how can you be prepared to combat these risks and prepare for the road ahead?

1. **Review contract terms** - Review each contract carefully for clauses that address rights in the event of unforeseen conditions or excusable conditions or delays. Terms may vary, however there is typically a clause in most contracts that outline unforeseen circumstances. For example, your contract may or may not use the phrase "force majeure" which is a French term commonly used in US contracts that refer to overwhelming forces that would otherwise prevent the fulfillment of a contract. If there appears to be no clause, keep looking as some contracts contain relief in circumstance, which can allow for extra time and compensation for unforeseen events.

2. **Provide clear and compliant notice** - Identify your contract's notice provisions for claiming delays and additional costs, including time limits for giving proper notice, who must be copied on the notice, as well as the method of delivery. Each project should have a written notice sent to the project's owner that complies with contract requirements, explains the cause, and reserves rights for time and money. Some contracts may include provisions that may expose the contractor to forfeiting rights to adjustments if notice is not made

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in a timely manner. Notices can be sent in a few ways, depending on your contract, such as email and hand delivery (certified mail). Verbal communication should be avoided as a written record trail should be established. The objective of these notices is to provide the project owner with advanced warning of the likely impacts of delays. Taking these steps may enable the owner and yourself to make appropriate, informed business decisions. It is good practice to develop a notice form that meets the requirements of each individual contract.

3. **Suspension and termination clauses** - Most contracts include a clause that allows the owner to suspend the project. These clauses allow for time extensions and even additional compensation if a project is restarted. These clauses also tend to give the contractor the right to terminate an agreement and receive defined compensation if the suspension lasts longer than a stated time frame.

4. **Document cost and schedule impacts** - Properly document and segregate any impact from the Coronavirus on construction projects that were impacted. Jobs should be evaluated for two components 1) establishing the right to added time and a price adjustment and 2) establishing the amount or extent of the delay/added costs. Be as specific as possible with your reports to accurately capture the impact of the Coronavirus delay.

5. **Contracts that do not address the issue** - What if your contract does not support relief efforts for extraordinary events like a pandemic or matters beyond your control? Under common law, circumstances that sufficiently delay or interrupt performance may excuse a contractor's non-performance. However, the concept of foreseeability can affect the support of common law. The argument that performance is excused may be undermined on the grounds that the party should have foreseen the problematic circumstances. We recommend seeking counsel as assessing these issues tends to involve fact-intensive inquiry.

6. **Consider insurance products** - Evaluate existing insurance policies to see if coverage is offered for Coronavirus-related losses. Inspect existing insurance policies of the project owner including Builder's Risk, business interruptions and any other relevant documents. Many policies require demonstration of actual losses, therefore having the proper documentation for support is key.

7. **Prime and subcontracts** - Analysis of prime and subcontracts should be conducted considering all of the differing relevant matters in each. Some subcontracts may have identical terms and conditions that exist in the prime contract while others may have different terms and conditions. Carefully phrase communications to ensure when an issue is addressed in the prime/owner context that it is consistent with how the issue should be addressed in the prime/subcontractor context.

8. **Identify challenges early** - Contractors may have the responsibility to mitigate consequences that arise from a delay or disruption. Reach out to subcontractors and vendors to address any potential delays due to the Coronavirus. Discuss and develop a contingency plan with subcontractors and vendors. Consider exploring alternative sourcing options and substitution options if shortages are likely and notify the project owner on a timely basis of the change. Keep up to date with market conditions and the potential impact it may have on jobs.

9. **Consider unique safety issues** - Revisit safety protocols of office and job sites and implement healthy procedures to properly address the spread of the disease. Providing guidance to employees regarding hygiene, travel, etc. may become a factor in continued performance or the shutting down of a project. It is suggested that contractors/employers seek guidance from professionals and follow the standards and recommendations offered by organizations like the Occupational Safety and Health Administration (OSHA), Centers for Disease Control (CDC), and the World Health Organization (WHO).

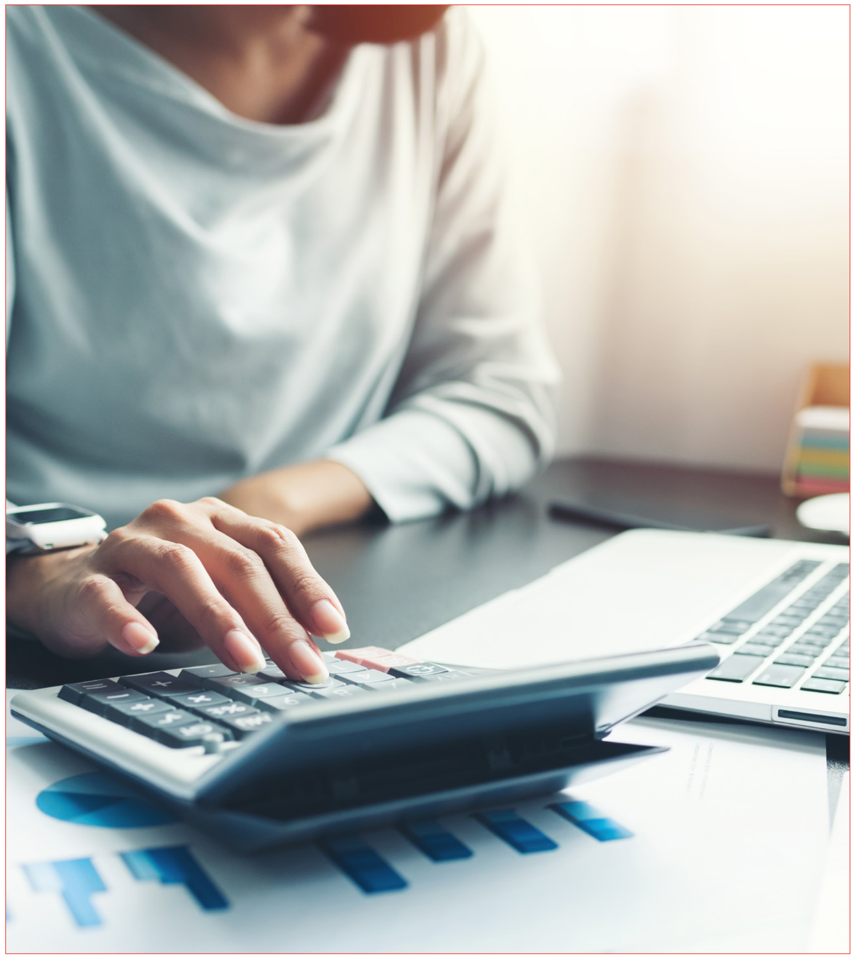
10. **Carefully consider language in contracts about to be executed** - Contracts that were signed during the pandemic may present unique challenges as these conditions were not "unforeseen" at the time of signing. Carefully review contracts entered into this time to ensure that the appropriate language is included to still account for any delays that may take place.

Conclusion

Contractors should be reviewing and monitoring all of the above items to help mitigate any losses that may arise due to the pandemic. The best way to mitigate losses is to be proactive with existing and new contracts that are in process during this time.

> "Keeping in contact with your legal counsel and CPAs during this time is crucial."

FIVE TAX UPKEEPING DUTIES TO COMPLETE THIS YEAR



With the new year past and tax season being extended, it provides an opportunity to take a look at some tax activities that are typically ignored throughout the year. Keeping up on these will safely prepare you for any upcoming changes.

1. **Tax withholding check-ins** - A quick check-in on tax withholdings early in the year can be beneficial. If a significant life event has occurred, then it is always a good idea to check current withholding information to ensure withholdings are still accurate.

2. **Beneficiary designations** - Coupled with tax withholdings, do not forget about beneficiary designations. These are tremendously important when starting a new job or working on wealth planning. Knowing how the law works and who your appointed beneficiaries are could play a role in contributions and benefits received from retirement plans.

3. **Estate Planning review** - Well-designed estate planning should be considered in conjunction with beneficiary designation reviews. Even if one was not affected by the Tax Cuts and Jobs Act, it is still beneficial to review to ensure marital and family trusts are still applicable. Additionally, those who made modifications during the year, especially those as a result of income tax planning, should consider if their existing estate plan is still in line with their overall estate and tax planning goals.

4. **Security habits** - Building better security habits is pivotal for successfully keeping private information private. This should not be limited to once a year, but security should be checked regularly. Along with building your own security habits, client data protection is important and should be combined with protecting your own data. Federal law requires tax professionals to create and follow a written information security plan to protect client data. Some recommendations are strong passwords or passphrases, using secure internet connections, and be mindful about personal and client information.

5. **Cryptocurrency** - Much like foreign accounts, the IRS has focused their interests on virtual currency reporting. As a result, a new checkbox on schedule 1 of Form 1040 has been added for virtual currency. Just because it is intangible does not mean it should be forgotten about, remember to check in if you own any virtual currencies and report them. Answering honestly can help save you time and money by avoiding civil and criminal penalties.

Conclusion
Even though tax filing only happens once a year, tax planning and compliance should be a year-round objective. Tackling these items early in the year and throughout could help prevent surprises down the road. Reach out and check in with your trusted adviser and look to do a mid-year review of your business and tax planning.

LONG-TERM CONTRACTS: SMALL CONTRACTOR THRESHOLD

The adoption of an appropriate accounting method for long-term contract is key to ensure that your company is in the most tax advantageous position possible. Thanks to the Tax Cuts and Jobs Act, other reporting methods are now permissible for construction contractors who meet certain thresholds.

Contractors generally utilize the percentage-of-completion method (PCM) when accounting for long-term contracts for tax purposes. However, this does not apply to construction contracts entered into, that are estimated to be completed within the two-year period beginning on the contract commencement date and also meets the gross receipts test for the taxable year in which the contract is entered. Contractors that previously met these requirements were able to elect the small contractor exemption. Effective January 1, 2018, the gross receipts threshold increased from $10 million to $25 million during the three prior years as part of the Tax Cuts and Jobs Act (TCJA). This has allowed contractors within these thresholds to elect a better suited tax method like completed contracts or even cash method. The small contractor exemption only applies to contractors who meet the two-year requirement and receipts threshold.

For those considering the adoption of the cash method under the Tax Cuts and Jobs Act, there is a key distinction based on a contractor's corporate structure. C corporations or partnerships can only use the cash method if their average annual gross receipts does not exceed $25 million for the three-taxable-year period. In most cases, S corporations can use the cash method as an overall tax method regardless of gross volume.

When calculating the total amount of gross receipts for the small contractor exemption, an entity must also factor in receipts from commonly controlled entities and joint ventures. If a contractor has 50% or greater ownership in a commonly controlled entity or joint venture, this will need to be included as income for the gross receipt calculation. If a contractor's ownership interest is only 5% - 49%, then the contractor must aggregate a proportionate share of any construction-related gross receipts.

In the instance that a contractor wants to change their contract accounting method they must file Form 3115. For contractors who were previously forced to PCM due to the $10 million threshold and are now under the $25 million threshold, filing of a 3115 is not required if you would like to return to the prior method used, as long as it is still an acceptable method. If in future years a contractor ends up exceeding the average gross receipts threshold, they are not required to notify the IRS, however they will need to implement the PCM for all new contracts for the following tax year.

Upon switching accounting methods for long-term contracts, a contractor is to only use the new method of accounting in the taxable year of adoption. For any contracts started in a prior year, the contractor must account for those contracts under the prior long-term contract method. It should be noted that if switching from the cash method to the PCM or accrual method, for cut-off purposes, contractors should compute the status of each contract on the cash basis as the contract enters the tax year. A 481(a) adjustment may be needed as a "catch-up" when switching from one method to another.

Contractors structured as S corporations should be cognizant of the fact that if they are utilizing the small contractor exemption, there is a possibility that they may be subject to Alternative Minimum Tax rules (AMT). For tax purposes, if you use a method other than PCM, you will need to report an AMT adjustment for the difference between the two methods on the company's tax return.

Conclusion

Implementing the most tax advantageous accounting method related to long-term contracts could make a significant financial difference for a contractor. It is important to meet with your tax advisor to discuss what methods are most beneficial for your company.

CONSTRUCTION INDUSTRY INSIGHT

UHY LLP's National Construction Practice is comprised of the country's foremost experts in regards to audit and assurance, tax planning and compliance, and business advisory services for the construction industry. We work with a wide range of key industry segments including general contractors, underground contractors, underwater construction, tunnel, and bridge and heavy highway contractors.

As active members of various national, state and local construction associations, state housing councils and specialty trade groups, our team keeps alert to industry trends and opportunities. Our professionals are leaders in the industry and take the steps necessary to ensure our client's future success by identifying and addressing new accounting requirements and regulations. You can depend on us to anticipate major industry issues that might impact your company and help you structure workable solutions.

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