Gorfine Schiller Gardyn
Certified Public Accountants and Consultants

Dimensions

SUMMER 2019

Focus on Safety

OSHA Compliance Is Just the Beginning

Is there a visit from the Occupational Safety and Health Administration (OSHA) in your future?

According to the U.S. Department of Labor, the odds of an OSHA inspector showing up at your jobsite may increase in coming years.

In April, Labor Secretary Alexander Acosta told a House Appropriations subcommittee that OSHA hired 76 new inspectors in the 2018 fiscal year, and he expects the number of jobsite inspections to go up as these new inspectors finish training and start conducting field inspections. (See "Getting Ready for an OSHA Visit" on page 4 of this issue.)

This increase in inspections is one of several recent safety developments that contractors should be aware of.

New Rules, Changing Risks

In January, OSHA released the final version of its new electronic recordkeeping rule, "Recording and Reporting Occupational Injuries and Illnesses" (29 CFR 1904).

The final regulation was published after a nearly two-year delay to address concerns that industry groups and others raised when the first version was unveiled in 2017.

Under the new rule, businesses with 20 or more employees in certain industries—including construction—must electronically submit information from their OSHA Form 300A (Summary of Work-Related Injuries and Illnesses) to a designated OSHA website. The deadline for submission is in early March of each year.

The original version of the rule also would have required businesses with 250 or more employees to submit their OSHA Form 300 (Log of Work-Related Injuries and Illnesses) and individual injury and illness incident report forms (Form 301) online as well.

But OSHA removed that requirement after industry groups and privacy advocates pointed out it could result in employees' personal information being revealed publicly.

The new rule also strengthens provisions that prohibit employers from retaliating against employees for reporting a workplace injury.

Such retaliation was already against the law, but under the new regulation, OSHA no longer needs to wait for an employee to file a complaint before it can cite an employer for alleged retaliation.

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Handling Change Orders

A Disciplined Approach Can Avert Problems

If you ask a group of contractors to list their biggest headaches, change orders will usually be near the top. Change orders are inevitable on most construction projects. How you manage them can mean the difference between a profitable project and a money-loser.

Know Your Contract

The first step in successfully handling change orders is to fully understand the change order process that is detailed in your contract. The language should be clear about who on the project owner's team has the authority to assign additional work. It should also indicate how and when your change order request should be submitted and processed. If anything is unclear, ask the project owner for written clarification.

Follow the Process

When out-of-scope work is assigned, make sure you follow the contract procedure to the letter—every time. If your request for a change order is denied and you decide to pursue a formal claim or litigation, the first thing you will need to do is show that you complied with the notification terms in the contract.

This discipline is especially important when dealing with a new customer or one with whom you have limited experience. Often, a project manager is under considerable pressure to "just get it done" and save the paperwork for later. But until the project owner has a well-established history of authorizing change orders reasonably and promptly, it is prudent to insist on a signed change order before any substantial work commences.

Get Everyone Involved

The principles that apply to general contractors submitting change order requests to project owners also apply when subcontractors submit their change order requests to the GC. In fact, you could argue that change orders are an even greater concern for subcontractors because they are usually the ones who will perform the requested work.

What's more, even if a subcontractor follows the contract procedures for change order submissions to the letter, there's still a risk the subcontractor will not get paid for the work if the general contractor drops the ball. Most contracts between GCs and subs contain a "paid-when-paid" clause, so subcontractors should verify that their GC complies with contract terms to ensure successful handling of the change order. If there is any doubt, subs should ask for copies of all relevant change order requests the GC submits to the project owner.

Understand the Accounting

There is also a less obvious reason for strict adherence to contract terms: it can affect how the costs associated with change order-related work are reported and accounted for, which can directly affect your company's bottom line. According to Generally Accepted Accounting Principles (GAAP), you can recognize revenue from work that is billed to a change order only after the change order is approved. But it is common to begin incurring some costs for out-of-scope work even before a change order is approved. How well you adhere to contract terms will affect how these costs are accounted for while you are awaiting approval. When contracts extend beyond a single reporting period, this can make a significant difference on your financial statements.

When you start to incur costs related to work that you think should be covered by a change order, GAAP rules allow you to record those costs as a prepaid expense—that is, as an asset on the balance sheet—only if you are adhering to your contract's change order process and your company has a good record of getting approvals. You also need a strong cost identification system to segregate these costs into a separate account rather than just charging them to general job costs.

Above all, do not let change orders accumulate until the end of the project when you have less leverage. Getting change orders processed promptly takes discipline, but the alterative—not getting paid for legitimate work—is not acceptable.

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Reassigning Responsibility

Another recent safety-related development emanated from a source outside of OSHA—the U.S. Court of Appeals for the 5th Circuit in New Orleans. In 1981 this court had ruled that OSHA regulations protect only an employer's own employees.

This was interpreted to mean that if a subcontractor's OSHA violations endangered only its own employees, a general contractor could not be held liable—the liability was the subcontractor's alone.

But late last year the court decided that, due to a subsequent U.S. Supreme Court ruling in an unrelated case, its previous position was no longer valid. In that case, the Supreme Court ruled that courts generally should defer to an agency's interpretations of its own regulations.

The Fifth Circuit found that OSHA could indeed choose to hold a general contractor liable for a subcontractor's violations because the GC was the "controlling employer" and had the "general supervisory authority" over the worksite. Industry observers are watching closely to see how this new precedent is applied in other cases.

Beyond Regulatory Compliance

Avoiding OSHA fines and penalties is worthwhile, of course, but contractors have even more important reasons to run a safe jobsite.

Foremost among these is a company's fundamental responsibility to provide a safe work environment, coupled with owners' and executives' basic humanitarian concern for their employees' welfare.

In addition, safety is just good business. Accidents can trigger significant avoidable costs, including medical expenses, legal fees, and higher insurance premiums.

A safety-conscious worksite is more productive, too, and a strong commitment to safety also can attract and retain skilled workers—a critical concern these days.

Accidents can diminish your ability to compete for new jobs as well. Project owners often inquire about bidders' safety records, including lost-time accidents, experience modifiers, and workers' compensation claims.

Eliminating workplace injuries and deaths is an ongoing priority for the industry. Every year, the construction industry accounts for more workplace fatalities than any other sector of the economy.

According to the U.S. Bureau of Labor Statistics, a total of 4,674 fatal workplace injuries were reported in private industry in 2017 (the latest year for which totals are available). One out of every five of those—971 fatalities—occurred in the construction industry.

OSHA, trade associations, equipment manufacturers, and private vendors produce numerous programs and training materials. All have the same goal: to make construction sites safer places to work.

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Getting Ready for an OSHA Visit

If an Occupational Safety and Health Administration (OSHA) inspector showed up today, would you be ready? Here are some practical steps that can help you prepare:

- **Get organized.** One individual—ideally your safety director, site foreman, or other manager—should act as your company's spokesperson during an OSHA inspection.

  Assign another employee to take notes and photos of anything the inspector records.

- **Be proactive.** Bring along several workers with tool belts. If the inspector finds simple problems, fix them immediately.

- **Get your papers ready.** Be sure your records are complete, current, and close at hand.

  This includes OSHA forms (especially Form 300A) for current and previous years; Material Safety Data Sheets for every chemical on site; a copy of your safety program or injury prevention plan; and records of safety training, internal inspections, and safety committee meetings.

- **Know how to respond.** An OSHA inspector could decide to interview workers, so make sure all employees know what to do.

  They should answer all questions directly and honestly—but remind them to just stick to the facts and avoid offering opinions.

Of course, the most important preparation is to maintain a safe jobsite. One important component of that is effective safety training on a range of topics, including:

- **Recognizing hazards.** All employees should understand the inherent dangers involved in working at heights, trenching, entering confined spaces, and using machinery or hazardous materials.
- **Best practices.** Train workers in the safe ways to perform virtually every task, from the simplest to the most complex.
- **Accident response.** Make sure site workers know the appropriate actions to take in an accident or emergency.
- **Safety equipment and protective gear.** Teach the proper use of personal protective gear, lockout/tagout systems, and other equipment.
- **Hazardous materials and labeling.** Enforce the rules about labeling chemicals and other materials.

Begin safety training before any new employee sets foot on the job, and then continually update and document every component, including daily "tailgate" or "toolbox" sessions.

Subchapter S Corporations

"Reasonable" Compensation Is a Must

The 20 percent deduction on pass-through income, introduced as part of the 2017 Tax Cuts and Jobs Act, could make subchapter S ownership even more appealing to many contractors.

But take care—the question of "reasonable compensation" for S corporation officers is consistently an area of concern to the IRS.

To reduce payroll tax liability, S corporation officers might try to pay themselves a nominal salary and instead take most of their earnings in shareholder distributions.

But the Internal Revenue Code establishes that any corporation officer is an employee who should be paid reasonable compensation.

The question, of course, is how to define the word "reasonable." There are no hard-and-fast rules, but the IRS does offer a list of specific factors that tax courts have considered when deciding the issue.

These include the shareholder's duties, responsibilities, training, and experience, as well as the time and effort devoted to the business.

Written compensation agreements and formulas are also considered, along with comparisons with what similar businesses pay.

The more of these factors you can demonstrate in your favor, the better your chances of convincing the IRS or a tax court that your officers' salaries are reasonable and that you are not using S corporation distributions to illegally avoid paying Social Security, Medicare, and unemployment taxes.

The consequences of failing an audit for reasonable officer compensation can be quite costly, so contractors who use this corporate structure should ensure that the salaries they pay themselves and other active shareholders will stand up to scrutiny.