



CFMA news

Construction Financial Management Association
Honolulu Chapter

Volume 13 • Issue 2
July 2006

The Fundamentals of ESOPS for the Construction Industry

Our first CFMA seminar for the year was very informative and well attended.

46 members and guests enjoyed the May 16, 2006 seminar which started with breakfast at the Pacific Club. Greg Hansen, Esq., an attorney from the firm of Case Lombardi & Pettit specializing in Employee Stock Ownership Plans

(ESOPs) explained how ESOPs work, why companies choose employee ownership (tax & non tax reasons), and special considerations for construction companies considering ESOPs.



CFMA members in attendance at the recent ESOP seminar.

The concept of ESOPs began long ago when economists studied how to spread equity benefits to employees who only worked for wages. Owners got rich from the success of their companies but the workers weren't sharing in that prosperity. In 1974 Employee Retirement Income Security Act of 1974 (ERISA) was passed to address this issue.

Continued on page 2

President's Message

As my first President's Message of the 2006 – 2007 fiscal year, I'm lucky enough to be able to introduce the new and improved CFMA Honolulu Chapter Newsletter. Thanks to the efforts of the communications committee and board members spanning two years, the vision of upgrading our newsletter has become a reality. Mahalo, for everyone's hard work and to our sponsors!

In addition to the newsletter, CFMA has been busy the last few months.

- Gregg Hansen and a panel of experts educated members about Employee Stock Ownership Plans.

- Thanks to Hawaiian Dredging, members were able to get a sneak peek at the twin 48-story towers on Kapiolani Boulevard. If you haven't ridden a man-lift to the 48th-story, you just haven't lived.

- Mitsunaga Construction donated its time to show members the recently completed Piikoi Vista – an affordable elderly rental project.

- A standing-room-only crowd was taught the finer points of additional insured status by professionals from King & Neel.

Several more events are planned for this year and I hope to see you there!

INSIDE

Page 1
The Fundamentals of
ESOPS for the
Construction Industry

President's Message

Page 3
Preparing Your 2007
Compensation Budget—Now!

Page 4
IRS & Treasury Issue
Regulations on IRC §199

Upcoming Events



Mahalo to our sponsors



AMERICAN
Savings Bank

Detor&Williams

Certified Public Accountants | A Professional Corporation



Turn to the Experts.™

B F TILE, INC.

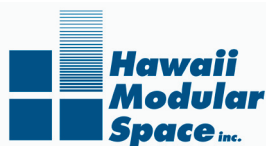
LICENSE # C 20385

P.O. Box 17909, Honolulu, Hawaii 96817-0909
(808) 847-3050 FACSIMILE: (808) 847-3057



First Hawaiian Bank

MARSH
The world's #1 risk specialist®



The Fundamentals of ESOPS continued from page 1

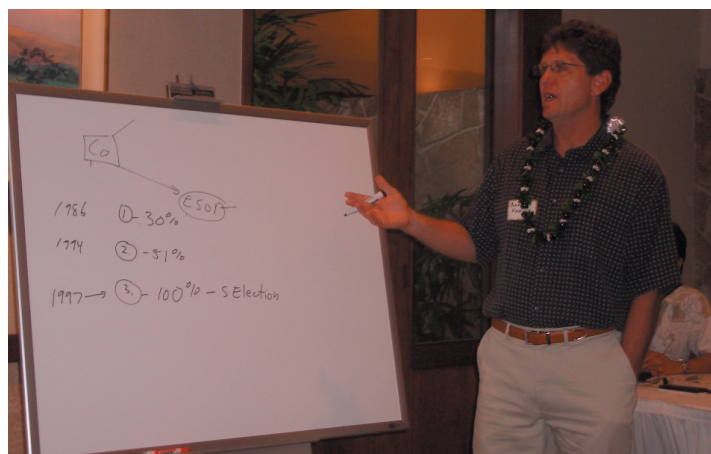
ESOP is a unique type of profit sharing plan where an employer contributes cash to the ESOP which is used to acquire Company stock on behalf of employee-owners. Often, a loan is obtained to facilitate the purchase (leveraged ESOP). It is important to note that Company contributions, not employee deferrals, fund the plan. After retirement, death, disability or other termination of service, employee accounts are distributed in cash equal to the fair market value of stock allocated to the accounts.

Richard Maxey, contract underwriter for Liberty Mutual Surety, provided a bonding company's perspective on ESOP transactions. In owner-financed ESOPs, the seller would ordinarily have to provide personal indemnities to the surety. When bank financing is involved, personal guarantees are usually not available. This generally results in a decrease in the bonding credit.

The panel consisted of CEOs of three contractors: Russell Young of AC Kobayashi, Inc., a 20-year ESOP; Mel Izumi of Allied Builders System, which became an ESOP in December 2005; and Ken Kobatake of Delta Construction who also just implemented ESOP in December 2005. Russell commented that in the beginning, an ESOP is primarily a means for the owner to get his money out of the business and it



Panelist, Mel Izumi and Russell Young share their personal experiences.



Greg Hansen educating CFMA members on ESOP plans.

takes a while for employees to really buy into the ESOP culture; however, once a long time employee retires and gets a sizeable check it becomes clearer to participants that the certificate is more than a piece of paper and that employees can really benefit from a successful ESOP. Critical to making the ESOP work is the continued profitability of the company. This is why panel members agreed now is a good time for construction companies to consider ESOPs. Ken Kobatake explained that heavy taxes were avoided by forming an ESOP.

All panel members talked about spending many years exploring all the issues before setting up an ESOP. The overriding message was that ESOPs can provide major benefits in the right circumstances, but should not be implemented lightly. Companies considering ESOPs should consult early with their attorney, accountant, surety, & banker.

Thank you to all participants for the seminar and to Wesley Mikuni for facilitating. Special thanks to Case Lombardi & Pettit and to Liberty Mutual for their sponsorships of the seminar.

Preparing Your 2007 Compensation Budget – Now!

Contractors consider seven key factors in determining employee compensation. Three of these factors, employee performance, company performance and pay policy are under management control. The remaining four factors, inflation, employment costs, the economy, and market rates are outside the company's direct control. They are nonetheless equally important in determining fair and competitive compensation.

The four uncontrolled factors indicate the following. First, inflation at an annual rate of 4.2% (as of May 2006) is definitely a player in pay increases. Secondly, the Employment Cost Index (ECI) while down from 2004 levels, still rose by 3.1% in 2005. Third, the economy, except for a few localized mainland areas, is predicted to maintain sustained growth. And, fourth, the value of employees on the open market is rapidly increasing. The third and fourth uncontrollable factors will be key in 2007.

For construction in particular, a strong economy, large expenditures for infrastructure and mainland reconstruction efforts mean that the demand for experienced personnel will be higher than the supply. Contractors will continue to find that they simply cannot hire skilled and experienced employees at current pay rates. The obvious result - an increase in market value for critical positions.

In planning next year's compensation budget consider all seven key factors in determining employee compensation, however, keep in mind the "demand" for skilled professionals will be the driving force on market values. Begin now to consider the impact the "competition for manpower" will have on your pay program. Research market values and start your analysis of your pay structure, making the necessary adjustments to bring your base pay program into line with the going rate.

*By: Jeff Robinson, President of Personnel Administration Service.
PAS specializes in wage, salary and benefit information primarily
for the construction and engineering industry.*

CFMA needs your help! Our newsletter has gone through a cosmetic overhaul and to compliment the transformation, the Board has decided to rename the newsletter. We need your help and we're willing to pay. Email your suggestions to Frank Wirt (f) and if your name is selected, the board will pay you \$50.00 (gift certificate). There's no limit to the number of names you may submit, but please make your submission by August 18th.

**Mahalo!
Frank Wirt, President
CFMA Honolulu Chapter**



The Construction Financial Management Association, Honolulu Chapter

Frank Wirt, Marsh USA, Inc.	President
Carleton Williams, Detor & Williams, CPA's	First Vice President
Thalia Choy, Thurston Pacific, Inc.	Secretary
Ralph Kanetoku, KPMG, LLP	Treasurer

Directors

Neill Char, First Hawaiian Bank
Michele Kaneshiro, Carrier Hawaii
Darlean Kiyokane, B F Tile, Inc.
Danford Oshima, American Savings Bank
Wes Mikuni, Ralph S. Inouye Co., Ltd.
Lianne Uyehara, Jade Painting & Decorating
Glenn Yee, Hawaiian Dredging Construction Co., Inc.

Upcoming Events

Sign-up Now CFMA's ANNUAL GOLF TOURNAMENT

Wed., August 30, 2006
12:00 Check-in
12:30 Tee-off
Kapolei Golf Club
\$60.00, includes golf and heavy pupus

Save The Date

**The Construction Financial Management Association Presents:
A Seminar on Hawaii's Act 221/215 – An insightful presentation on Hawaii's Act 221/215, with a review of the Tax Benefits for Investors.**

Thurs., Sept. 14, 2006
7:15 a.m. – 10:30 a.m.
The Pacific Club
Includes a Buffet Breakfast
Members are Free!

IRS & Treasury Issue Regulations on IRC §199

The IRS and Treasury released final regulations regarding the IRC §199 Domestic Production Activities Deduction (DPAD). The new guidance specifies rules for the deduction for income attributable to domestic production activities.

The regulations contain a reverse de minimis rule for taxpayers who have a small amount of domestic production gross receipts (DPGR). The guidance classifies grading, demolition, clearing, and excavating as construction activities for DPAD purposes when the services are performed in connection with building or substantial

renovation activities. The regulations also clarify the methods of determining W-2 wages for IRC §199.

In addition, the new rules replace previous guidance that excluded the sale of materials incorporated into real property from the §199 deduction. CFMA, among other organizations, objected to this rule and other aspects of the temporary regulations in a comment letter issued in December 2005. The new rules clarify that materials consumed during construction or that become structural components of a building will qualify.

The new guidance will

simplify calculation of the deduction for contractors nationwide. Eric P. Wallace, who drafted CFMA's comments said, "The final regulations allow more contractors to take advantage of the new deduction with fewer prohibitive administration costs or concerns about qualification." According to William M. Schwab, CFMA's Chief Executive Officer, "It is the role of CFMA to ensure that policymakers understand issues specific to contractors. This is a classic example of CFMA fulfilling its mission as 'The Source & Resource for Construction Financial Professionals.'"

*Contributed by CFMA,
Princeton New Jersey*



CFMA Honolulu Chapter
c/o KPMG
P.O. Box 4150
Honolulu, HI 96812-4150