



MANAGING CONTRACTOR DEFAULT RISK

PREQUALIFYING CONTRACTORS AND SUBCONTRACTORS

Presented by

Steve Warnick
Vice President
Austin Commercial, Inc.

Default

One of the most disruptive events in a construction project is a contractor's failure to perform its contractual obligations, especially completion of the agreed-upon work. Performance bonds are frequently utilized to protect the hiring party (owner or contractor) from the financial impact of a contractor or subcontractor default, including the cost of finding a replacement contractor, higher contracting costs, and delays caused by the default. However, many contractors choose to self-insure this risk, and minimize the risk of default using a rigorous prequalification process to select qualified and financially secure subcontractors. Recently, several insurers have developed an insurance policy that provides a form of stop loss coverage for contractor default. In this session, learn strategies for helping your clients make an informed decision on whether to self-insure, bond, or insure this risk. Also learn how to assist your client in minimizing the financial impact of a default no matter which method of financing is selected.

Monday, November 13, 9:00 a.m.–5:00 p.m.

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the elements of a solid future

Steve Warnick
Vice President
Austin Commercial, Inc.

Mr. Warnick is one of the presenters for Monday's all-day seminar, "Managing Contractor Default Risk." He is risk manager and vice president of Austin Commercial. His current responsibilities include contract review and negotiations, insurance (including OCIP/CCIP administration), and bonding. Mr. Warnick received his bachelor's degree in architectural construction at Texas A&M in 1968 and has spent his entire career in the construction industry. He is a director of the Texas Associated General Contractors (AGC) Workers Compensation Purchasing Group, is on the Board of Directors of the Dallas Chapter of AGC, and serves on the national AGC Contract Documents Committee, Risk Management Committee, and Surety Committee. Also, Mr. Warnick serves on the Board of Directors of the Construction Education Foundation.

Austin Commercial is a subsidiary of the 82-year-old, Dallas-based Austin Industries. Austin Industries is an employee-owned, merit shop construction company. Today, Austin is one of the largest and most diversified construction organizations in the United States. It is ranked number 38 on *ENR Magazine's* Top 400 Contractors listing.

Notes

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PREQUALIFYING CONTRACTORS AND SUBCONTRACTORS

***Steve Warnick
Austin Commercial, Inc.***

I. Prequalification Form

- A. General information
- B. Financial information
- C. Safety and health information

II. Prebid Procedure

- A. Verify subcontractors are pre-qualified
- B. Explain subcontractor default risk program

III. Bid Procedures

- A. Scope card review
- B. Select contractor providing best value for the project

IV. Daily/Monthly Procedures

- A. Pay application review
- B. Field inspection

V. Default Procedures

- A. Warning signs
- B. Remedial actions
- C. Dispute resolution
- D. Loss scenario

VI. Management Reports

- A. Enrollment report—tracks contractors enrolled in program
- B. Risk report—tracks contract amount/total amount to complete
- C. Warning report—tracks contractors that have shown warning signs of default and lists remedial actions implemented
- D. Claims report—tracks numbers of claims/dollar value of claims
- E. Completion report—recap of information at completion from reports A–D

VII. Exhibits

- A. Pre-qualification Process
- B. Pre-qualification Questionnaire
- C. Pre-qualification Worksheet
- D. Enrollment Form
- E. Completion Form
- F. Z Score Profitability Analysis
- G. Additional Financial Ratio Calculations

VIII. Glossary of Terms

Default

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PREQUALIFYING CONTRACTORS AND SUBCONTRACTORS

Subcontractor Default Risk Program Operations Manual

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PRE-QUALIFICATION FORM REVIEW PROCEDURE

The Subcontractor Pre-Qualification Questionnaire is designed to provide the information required to begin the underwriting process. After the subcontractor completes the documents, the information is analyzed to determine if the subcontractor qualifies to be enrolled in the program. The information provided by the subcontractor becomes the framework of the underwriting process.

The following criteria are used in determining subcontractor qualification for enrollment in the Subcontractor Default Risk Program (SDRP):

GENERAL INFORMATION

- Five or more years of successful operation with stable management and ownership.
- Qualified key personnel for the type and size of work to be undertaken.
- In business five (5) or more years.
- Does work experience meet the requirement for current project?

FINANCIAL INFORMATION

- Has current bank letter of credit been exhausted or is it about to expire?
- Does letter of reference from bank officer reflect satisfactory performance?
 - Line of credit.
 - Basis extended.
 - Amount of unsecured credit.
 - Security required.
 - Overall banking relationship.
 - Years of relationship.

Additional information may be desirable.

- Request cash and investment balances.
- Are there any loans?
- Are the Year-End Financial Statements for the past three (3) years CPA Reviewed (as per AICPA standards)? Interim Statement if Year-End Statement is more than nine (9) months old.
- The following criteria are used in determining subcontractor financial health:
 - Z-Score (Profitability Analysis) of 2.675 or greater.
 - Debt to Equity of 3 to 1 or less.

- Current Ratio of 1 to 1.5 or greater.
- Ratio of Working Capital to Uncompleted Work-in-Progress of 8% or greater.
- Ratio of Net Worth to Uncompleted Work-in-Progress of 10% or greater.
- Consistent Gross and Net Profits over the past three (3) years.
- Net Over-billed Position.

- Part of consolidated group?

Additional information required if yes.

- Consolidated group financial statements for the past three (3) years.
- Audited preferred.

- Bankruptcy or failed business, closed business, defaulted or failed to complete on a contract?
- Check references from two (2) major suppliers, two (2) owners, two (2) contractors, and two (2) subcontractors to see if they reflect "good" or "satisfactory" payment and performance records.
- Surety must be Treasury Listed and have a minimum A-VII Rating listed in A. M. Best's Key Rating Guide.
- Has letter of good standing been provided by Surety?
 - Years at relationship.
 - Largest bond.
 - Total bonding capacity.
- Is current backlog acceptable?
- Has annual revenue volume increased/decreased over the past three (3) years?
- How much of prior work has been bonded?
- Current projects and program underway are of the same type work and size (within two times) of those previously completed successfully.
- Current project and applicant's other projects are within their normal geographical area of operation.
- Check with three (3) owners/general contractors to see if they describe satisfactory performances on three (3) of the applicant's larger jobs.

SAFETY AND HEALTH INFORMATION

- Work related fatalities?
- OSHA citation within past three (3) years?
- Environmental citation within past three (3) years?

PRE-BID PROCESS PROCEDURE

- Verify subcontractors invited to bid have been pre-qualified.
- Explain Subcontractor Default Risk Program during pre-bid conferences
 - Provide SDRP Enrollment Form.
- Explain process of bidding project net of bond cost with “add alternate” to provide payment/performance bonds.

BID PROCESS PROCEDURE

- Match pre-qualification worksheet with subcontractor.

- Evaluate bond cost that would have been charged to project as determined by the "add alternate".

- Assist in review of scope cards during subcontractor selection process.
 - Review price.
 - Review schedule.
 - Review personnel assigned to project.
 - Review schedule of values.
 - Review quantities.
 - Determine percentages of self-performed work.
 - Determine percentages of subcontracted work.
 - Confirm major suppliers and lower tier subcontractors have been named.
 - Examine bid to verify it is in line with other bidders, or determine the reason for any major differences.

DAILY/MONTHLY PROGRAM MANAGEMENT PROCEDURE

- ❑ Assist in review of monthly pay applications
 - Consult with project manager to certify billings are in line with percentage complete and consistent with field inspections so that over-billings do not occur.
 - Consult with project manager that stored materials are being verified.
 - Confirm that suppliers and lower tier subcontractors are being paid timely.

- ❑ Inspect quality of subcontractor's work.
 - Confirm submittal of shop drawings is timely.
 - Attend job site progress meetings.
 - Review QA administrator inspections & reports.
 - Review testing agency inspection reports.
 - Review Architect/Engineer field reports.
 - Review contractors daily construction reports.
 - Request information from field personnel, superintendents, and engineers, regarding any problems observed with performance, quality of work, man-power, or delivery of supplies.
 - Confirm work is consistent with plans and specifications.
 - Confirm submittal of Change Order Request pricing is timely.
 - Verify that schedules are being met.
 - Determine extent of punch list items, and that they are being addressed timely.

SUBCONTRACTOR DEFAULT PROCEDURE

WARNING SIGNS (DEFAULT INDICATORS)

Any negative change in the underwriting items listed in the Pre-Qualification Form Review Procedure is a warning sign and an indicator of potential default. Obviously, the degree of change and the importance of the element determines the significance of the sign. Generally, we are looking for a large swing, a negative trend, or a negative change in multiple areas. It is necessary to keep in mind that a negative or change in one area can be offset with a strengthening in other areas.

Specific warning signs to be aware of:

Pre-qualification Phase

- Exhausting bank line of credit.
- Bank taking greater security for loans or line of credit.
- Deterioration in working capital and/or cash flow.
- Slow turnover of receivables.
- Deteriorating profit margins or the existence of losses.
- Deterioration in pay record as reflected in references and credit reports.
- A change from a standard to a non-standard bonding company.
- Fast growth and rapid expansion in terms of program size and annual volume (expansion greater than 50% is considered rapid).
- Undertaking individual projects of a greater size (more than two times) and complexity than those previously completed.
- Undertaking a different type of work than what the contractor has previously experienced.
- Geographic expansion whether it is one large job or multiple smaller jobs.
- Becoming involved in unrelated ventures such as real estate development or manufacturing.
- Significant amount of work with questionable owners/general contractors.
- Continuous litigation with owners/general contractors.

Bid Phase

- Large spread between contractor's price and the next several bidders.
- Scheduling of work is significantly different from other bidders.

- Schedule of values and quantities are not in line with next several bidders.
 - Quality of named major suppliers and lower tier subcontractors is less than acceptable.
- ❑ Construction Phase
- The appearance of liens and other such legal actions.
 - Overall decline in performance in both field operations and project management.
 - Contractor experiences difficulties in manning jobs and/or slips in schedules occur.
 - Quality of work is unacceptable, has to be removed and replaced.
 - A change in management or ownership, especially the incapacitation of key owners/officers.
 - There are over-billings on pay requests.
 - Submittals, requests for change, request for information not timely.

REMEDIAL ACTIONS

- ❑ Pre-qualification Phase
- Enroll subcontractor into mentoring program.
- ❑ Bid Phase
- Determine reasons for difference from other bidders.
 - Reduce scope, where applicable, to focus on core scope.
 - Do not award.
- ❑ Construction Phase
- Suggest strategies to subcontractor to work more efficiently.
 - Set up daily strategy/performance tracking meetings.
 - Prepare schedules and manning requirements for subcontractor.
 - Direct purchase of materials.
 - Direct furnish of construction equipment.
 - Provide project manager/superintendent to supplement field management.
 - Supplement subcontractor with personnel, i.e., laborers, tradesmen, field engineers, foremen, etc.
 - Finance subcontractor.
 - Supplement subcontractor with additional subcontractor(s).

- Issue joint checks.
- Reduce scope, where applicable, to focus on core scope.
- Replace subcontractor.
- In case of lien notice/filing
 - Prepare joint checks, as applicable.
 - Assist subcontractor with workout schedule of payments.

DISPUTE RESOLUTION

- Discussions between the parties
 - Project Level.
 - Corporate Level.
- Dispute Review Board
 - Panel of three individuals with different expertise, (engineering, construction, and ownership.)
 - Issue non-binding written decision.
- Mediation (non-binding).
- Arbitration (binding).
- Litigation.

IN CASE OF LOSS

- Written notification of default/termination to subcontractor.
- Written notification of default/termination to internal management, agent, surety and/or insurer.
- Mitigate loss.
- Collect expense data to substantiate loss incurred to report to internal management, agent, surety and/or insurer.
- Conduct "Root Cause Analysis".
 - Was pre-qualification process faulty?
 - Were early warning signs missed?
 - Were remedial actions ineffective?
 - Were remedial actions instituted too late?

MANAGEMENT REPORTS

Reporting of results of the Subcontractor Default Risk Program consists of project-level and management-level reports. Reports should include detailed information on the status of individual contractors in the program.

At the project level, the early warning signs of potential default must be organized and tracked to allow the manager to act as soon as a warning sign flashes. The manager can then begin to implement remedial actions.

- ❑ SDRP-1. Enrollment Report
 - Track subcontractors enrolled in SDRP.

- ❑ SDRP-2. Risk Report
 - Tracks total contract amount and total amount to complete by subcontractor.

- ❑ SDRP-3. Warning Report
 - Track subcontractors that have shown warning signs of default and lists remedial actions implemented.

- ❑ SDRP-4. Claims Report
 - Tracks number of claims and dollar value of claims incurred by subcontractor.

- ❑ SDRP-5. Completion Report
 - Calculates adjusted contract value at close out by subcontractor.
 - Recaps information contained in SDRP 1-4.

MANAGEMENT REPORTS

SDRP-1 Enrollment Report

SDRP-2 Risk Report

SDRP-3 Warning Report

SDRP-4 Claims Report

SDRP-5 Completion Report

SDRP-1
ENROLLMENT REPORT

Subcontractor Name

Project

Start Date

Estimated Completion Date

Initial Contract Amount

SDRP-2
RISK REPORT

Subcontractor Name

Project

Start Date

Initial Contract Amount

Change Order Amount

Payment to Date

Percent Complete

Balance of Contract

Estimated Completion Date

Default

SDRP-3
WARNING REPORT

Subcontractor Name
Project
Warning Sign
Remedial Action Taken

SDRP-4
CLAIMS REPORT

Subcontractor Name
Project
Claim Number
Claim Amount

SDRP-5
COMPLETION REPORT

Subcontractor Name
Project
Contract Completion Date
Initial Contract Amount
Change Order Amounts
Final Contract Amount
Combined information from SDRP 1-4

EXHIBITS

- EXHIBIT 1: PRE-QUALIFICATION PROCESS
- EXHIBIT 2: PRE-QUALIFICATION QUESTIONNAIRE
- EXHIBIT 3: PRE-QUALIFICATION WORKSHEET
- EXHIBIT 4: ENROLLMENT FORM
- EXHIBIT 5: COMPLETION FORM
- EXHIBIT 6: Z SCORE PROFITABILITY ANALYSIS
- EXHIBIT 7: ADDITIONAL FINANCIAL RATIO CALCULATIONS

EXHIBIT 1

PRE-QUALIFICATION PROCESS

Thank you for your interest in bidding work connected with the Subcontractor Default Risk Program. Enclosed is the Pre-Qualification Questionnaire. All subcontractors must complete this document **before** they will be allowed to participate in the bid process.

The questionnaire consists of three sections: general information, financial information, and safety and health information. Please direct any questions you may have concerning this form, and return the completed document to:

Contractor

Address

City/state/zip

Contact person:

Phone # of contact person

Fax # of contact person

Email of contact person

EXHIBIT 2

PRE-QUALIFICATION QUESTIONNAIRE

GENERAL INFORMATION

Company Name: _____

Street Address: _____

City: _____ State: _____ Zip Code: _____

Contact Name: _____ E-Mail: _____

Telephone: _____ Fax: _____

Federal Taxpayer ID No. _____ Texas Sales and Use Tax Permit No. _____

List Owners, Officers, and Key Personnel (Include Resumes):

<u>Name</u>	<u>Years in Position</u>	<u>Position</u>
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

How Many Years Has Your Firm Been In Business? _____

Organized As A (Check One):

Corporation in the State of _____ Partnership Joint Venture Proprietorship Other _____

MBE: Yes No M/WBE Certification Agency: _____ M/WBE Certification Number: _____

Work Experience (Check all that apply):

Hotel Hospital Airport Semi-Conductor Corporate Build to Suit Interiors
Retail Multi-Family Industrial Heavy /Highway Commercial Other

Does Your Firm Operate Under Any Other Name?
Yes No (if yes, explain)

Name: _____

Address: _____

Comments: _____

Is Your Firm Affiliated With Any Other Firm?
Yes No (if yes, explain)

Name: _____

Address: _____

Comments: _____

EXHIBIT 2

FINANCIAL INFORMATION

Contact Name (*financial*): _____ Telephone: _____

Bank References:

<u>Name of Bank</u>	<u>Bank Officer</u>	<u>Phone Number</u>
_____	_____	_____
_____	_____	_____

Line of Credit: _____ Unused Line of Credit: _____ Expiration Date: _____

Provide letter of reference from bank officer (line of credit, basis extended, how much unsecured and secured, what security required, overall banking relationship, and years of relationship).

Financial Statement:

Must provide copies of the past three (3) year-end financial statements (*audited if available*), and if statement is more than nine (9) months old, provide a current interim financial statement.

Are you part of a Consolidated Group? Yes No

(If yes, provide Consolidated Group Financial Statements for the past three (3) years. ~ audited if available)

Company Name: _____ Year In Business: _____

Street Address: _____

City: _____ State: _____ Zip Code: _____

Contact Name: _____

Telephone: _____ Fax: _____

Has your firm or any affiliated firm or any of its principals ever petitioned for bankruptcy, failed in business, closed a business, defaulted or failed to complete on a contract? Yes No (*if yes, explain*)

Comments: _____

Owner, General Contractor, Subcontractor and Supplier References: (*minimum two (2) each*)

<u>Name of Company</u>	<u>Contact</u>	<u>Phone Number</u>
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

EXHIBIT 2

Bonding Agent:

Company Name: _____

Contact: _____ Phone: _____

Surety:

Company Name: _____

Contact: _____ Telephone: _____

Provide letter of good standing from surety (years of relationship, largest bond, total bonding capacity).

Current Backlog:

(If needed, please provide an additional sheet continuing your current backlog)

<u>Project/Location</u>	<u>Contract Amount</u>	<u>Percent Completed</u>	<u>Cost to Complete</u>	<u>Completion Date</u>	<u>Bonded (yes/no)</u>
_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____

Provide your annual revenue volume over the past three years and estimate the percent of volume bonded:

Year _____	Year _____	Year _____
\$ _____	\$ _____	\$ _____
_____ % bonded	_____ % bonded	_____ % bonded

List your three (3) largest jobs completed:

	<u>Project/Location</u>	<u>Contract Amount</u>	<u>Year Completed</u>	<u>Bonded (yes/no)</u>	<u>Owner/General Contractor</u>
1.	_____	_____	_____	_____	_____
2.	_____	_____	_____	_____	_____
	_____	_____	_____	_____	_____

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Default

EXHIBIT 2

SAFETY AND HEALTH INFORMATION

Contact Name (*safety*) _____ Telephone _____

If work-related fatalities have occurred among your workforce within the last three (3) years, provide the following information for each fatality: (Use extra sheets if necessary):

Date: _____ Location: _____

Citation Issued: Yes No Agency issuing citation: _____

Status of citation, e.g., contested, withdrawn, etc. _____

Are any lawsuits filed relating to the same event? Yes No

If so, please give status. _____

Has your company received an OSHA citation within the past three (3) years for items other than those listed above? Yes No Number of citations: _____

Type and severity of citations:

Pending citation(s): Yes No Number of citations: _____

Location(s): _____

Type and severity of citations:

Has your company received an environmental citation or notice of violation within the last three (3) years? If yes, provide the following information:

Issuing Agency (s): _____

Describe: _____

Status: _____ Contested: _____

I understand the questions above and have answered truthfully and to the best of my knowledge.

Name _____ Title _____
Type or Print

Signature _____ Date _____

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EXHIBIT 3

PRE-QUALIFICATION WORKSHEET

Subcontractor Name: _____

Address: _____

	Required	Actual	Meets Criteria	Comments
<input type="checkbox"/> GENERAL INFORMATION:				
1. Years with stable management/ ownership?	5			
2. Key personnel qualified for the project?	Yes			
3. Years in business?	5			
4. Work experience compatible with current project?	Yes			
<input type="checkbox"/> FINANCIAL INFORMATION:				
5. Letter of Credit exhausted or expired?	No			
6. Reference from Bank Officer?	Satisfactory			
7. Financial Statement Review	CPA Review			
– Z-Score (profitabililty analysis)	2.675 or >			
– Debit to Equity	3 to 1 or <			
– Current Ratio	1 to 1.5 or >			
– Ratio Working Capital/Uncompleted Work in Progress	8% or >			
– Ratio Net Worth/ Uncompleted Work in Progress	10% or >			
– Consistent gross and net profits	Yes			
– Net overbilled position	Yes			
8. Are you part of a Consolidated Group?	No			
9. Filed for bankruptcy or defaulted on contract?	No			
10. References - payment & performance record	Satisfactory			
11. Surety rating?	A-VII Rating or >			
12. Letter of Good Standing from Surety	Satisfactory			
13. Current projects are of same type and size as previous experience	Within two (2) times			
14. Current projects are within normal geographical area of operation.	Yes			
15. Reference from owners and/or general contractors on three (3) largest jobs.	Satisfactory			

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EXHIBIT 3

SAFETY AND HEALTH INFORMATION:

1. Worked related fatalities?
2. OSHA citation within past three (3) years?
3. Environmental citation within past three (3) years?

No			
No			
No			

EXHIBIT 4
ENROLLMENT FORM

Default

To:

Project Name/Description: _____ Project #: _____

THE SUBCONTRACTOR NAMED BELOW HAS BEEN AWARDED A CONTRACT ON THE REFERENCED PROJECT:

Company Name: _____

Street Address: _____

City: _____ State: _____ Zip: _____

Contact Name: _____

Phone: _____ Fax: _____

E-Mail: _____

Federal Taxpayer ID Number: _____

Type of Work: _____

Start Date: _____

Estimated Completion Date: _____

Type of Contract: Lump Sum Unit Price Cost-Plus GMP Other

Initial Contract Amount: _____

Awarding Contractor: _____

Awarding Contractor Contact: _____ Phone: _____

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EXHIBIT 5
COMPLETION FORM

To:

Project Name/Description: _____ Project #: _____

Company Name: _____

Street Address: _____

City: _____ State: _____ Zip: _____

Contact Name: _____

Phone: _____ Fax: _____

E-Mail: _____

Federal Taxpayer ID Number: _____

Type of Work: _____

Type of Contract: Lump Sum Unit Price Cost-Plus GMP Other

Completion Date: _____
Final Contract Amount: _____
Through Subcontractor Change Order Number: _____

Authorized Representative of Prime Contractor

Title

Date

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EXHIBIT 6

Z SCORE PROFITABILITY ANALYSIS

Subcontractor _____

Project _____

Z Score Profitability Analysis:

Ratio		Formula	Enter Data		Weight Factor		Weighted Ratio
Return on Total Assets	=	$\frac{\text{Earnings Before Interest and Taxes}}{\text{Total Assets}}$	_____	x	3.3	=	
Sales to Total Assets	=	$\frac{\text{Net Sales}}{\text{Total Assets}}$	_____	x	0.999	=	
Equity to Debt	=	$\frac{\text{Market Value of Equity}}{\text{Total Liabilities}}$	_____	x	0.6	=	
Working Capital to Total Assets	=	$\frac{\text{Working Capital}}{\text{Total Assets}}$	_____	x	1.2	=	
Retained Earnings to Total Assets	=	$\frac{\text{Retained Earnings}}{\text{Total Assets}}$	_____	x	1.4	=	
					Z Score	=	
					Criteria		Classified as "failed" if < 2.675

Default

**EXHIBIT 7
ADDITIONAL FINANCIAL RATIO CALCULATIONS**

Subcontractor _____

Project _____

Additional Financial Ratio Calculations:

Ratio		Formula	Enter Data		Ratio	Criteria
Debt To Equity	=	$\frac{\text{Total Liabilities}}{\text{Market Value of Equity}}$		=		3 to 1 or less
Current Ratio	=	$\frac{\text{Current Assets}}{\text{Current Liabilities}}$		=		1 to 1.5 or greater
Working Capital to Uncompleted Work-in-Progress	=	$\frac{\text{Working Capital}}{\text{Uncompleted Work-in-Progress}}$		=		8% or greater
Net Worth to Uncompleted Work-in-Progress	=	$\frac{\text{Net Worth}}{\text{Uncompleted Work-in-Progress}}$		=		10 % or greater

Additional Financial Statement Analysis:

	Enter Data	Year	Criteria
Gross Profit			Consistent Gross and Net Profits the past three (3) years
Net Profit			
Net Over-billed Position (current financial report)		Overbillings minus Underbillings	Overbillings should be higher than underbillings

GLOSSARY OF TERMS

amortization - The process of cost allocation that assigns the original cost of an intangible asset to the periods benefited.

asset - A physical or intangible item of value to an organization or individual.

balance sheet - (*statement of financial position*) - The financial statement that shows the assets, liabilities, and owner's equity of an entity at a particular date.

cash - Coins, currency, money orders, checks, and funds on deposit with financial institutions; the most liquid of assets.

cash flow - earnings + depreciation + amortization = cash flow. The positive (inflow) or negative (outflow) movements of cash caused by an activity over a specific period of time.

cash flow statement - The financial statement listing the cash impact of the activities of a business over a specified period of time separating the cash flows into areas of operations, investments, and financing.

common stock - The most frequently issued class of stock; usually it provides a voting right but is secondary to preferred stock in dividend and liquidation rights.

current assets - cash + marketable securities + accounts receivable + inventories = current assets. Any asset on the balance sheet with a short-term expectation of being turned into cash, such as receivables and inventories; usually considered as having less than a year before being converted into cash.

current liabilities - accounts payable + short-term notes payable + current maturities of long term debt + accrued income taxes + other accrued expenses (principally wages) = current liability. Any liability on the balance sheet with a short-term maturity, usually payable within one year, such as accounts payable.

current ratio - (*liquidity ratio*) - current assets / current liabilities. This ratio is the most commonly used measure of short-term solvency, since it indicates the extent to which the claims of short-term creditors are covered by assets that are expected to be converted to cash in a period roughly corresponding to the maturity of the claims.

debt ratio - (*leverage ratio*) - total debt / total assets. Measures the percentage of total funds provided by creditors. (*creditors equity*).

debt to equity ratio - total liabilities / shareholders equity. Measures the percentage of total funds provided by creditors.

depreciation - The allocation of the cost of an asset over a period of time for accounting and tax purposes. Also, a decline in the value of a property due to general wear and tear or obsolescence; opposite of appreciation.

earnings before interest and taxes - Same as operating income.

equity - The value of the funds contributed by the owners (the stockholders) plus the retained earnings (or losses). On the balance sheet it is usually referred to as "shareholder's equity".

equity ratio - (*leverage ratio*) - owners equity / total assets. Measures the percentage of total funds provided by owner. (*owners equity*).

financial statements - Reports such as the balance sheet, income statement, and cash flow statement, which summarize the financial status and results of operations of a business entity.

fixed asset - Any asset on the balance sheet considered to have a life or usefulness for a business in excess of one year, such as land, buildings, and machinery.

goodwill - An intangible asset that exists when a business is valued at more than fair market value of its net assets, usually due to strategic location, reputation, good customer relations, or similar factors; equal to the excess of the purchase price over the fair market value of the net assets purchased.

income statement - (*statement of earnings*) - The financial statement that summarizes the revenues generated and the expenses incurred by an entity during a period of a time.

intangible asset - Long-lived assets without physical substance that are used in business, such as licenses, patents, franchises, and goodwill.

liabilities - Obligations measurable in monetary terms that represent amounts owed to creditors, governments, employees, and other parties.

liquidity - A company's ability to meet current obligations with cash or other assets that can be quickly converted to cash.

long term assets - (*operating assets*) The value of a company's property, equipment, and other capital assets, expected to be useable for more than one year, minus depreciation.

long term liabilities - A company's liabilities for leases, bond repayments, and other items due in more than one year.

market value - A security's last reported sale price (if on an exchange) or its current bid and ask prices (if over-the-counter); i.e. the price as determined dynamically by buyers and sellers in an open market.

net assets - total assets - total liabilities = net assets. The ownership interest in the assets of an entity. (*owners' equity*).

net income - A measure of the overall performance of a business entity; equal to revenues minus expenses for the period.

net sales - Gross sales minus returns, discounts, and allowances.

net worth - Total assets minus total liabilities. Also called owner's equity, or shareholders equity or net assets.

operating income - A measure of a company's earning power from ongoing operations, equal to earnings before deduction of interest payments and income taxes, also called operating profit or EBIT (earnings before interest and taxes).

owner's equity - Total assets minus total liabilities. Also called net worth, or shareholder's equity, or net assets.

preferred stock - A class of stock that usually provides dividend and liquidation preferences over common stock.

quick assets - Current assets, inventory.

quick ratio - (*liquidity ratio*) - quick assets / current liabilities. Inventories are typically the least liquid of a firm's current assets and the assets on which losses are most likely to occur in the event of liquidation. Therefore, this measure of the firm's ability to pay off short-term obligations without relying on the sale of inventories is important.

receivables - Claims for money, goods, or services.

retained earnings - Earnings not paid out in dividends but retained by the company to be reinvested in its core business or to pay debt. The portion of a corporation's owners' equity that has been earned from profitable operations and not distributed to stockholders.

shareholders - Individuals or organizations that own a portion (shares of stock) of a corporation. (*Stockholders*).

total assets - Current assets plus long term assets.

total debt - Current liabilities and all bonds.

total liabilities - Current liabilities plus long term liabilities.

working capital - Current assets minus current liabilities.