

Notebook...

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Tax Law Changes Help Contractors

by Len Pytlak, C.P.A.

"The Taxpayer Relief Act of 1997" is the formal name of the new tax laws passed this summer by Congress and President Clinton as part of their budget deal, but a better name might be "The Tax Preparer's Full-Employment Act." The law had 800 changes and 300 additions to the already confusing laws and regulations.

Fortunately, some of these were quite favorable to builders, as the building industry got much of what it lobbied for in the new tax packages. Here are a few highlights of those items affecting the industry.

Sale of Principal Residence

Effective May 7, 1997, up to \$500,000 of the gain from the sale of a personal residence is now per-

manently tax-exempt, a benefit that taxpayers can take advantage of every two years if certain rules are met. Under the old rules, you had to either buy another house within two years to avoid such taxes, or be over age 55, in which case you could take one lifetime exemption. This new, more liberal exemption should bring added fluidity to real estate markets.

Tax-Free IRA Withdrawals for First-Time Homes

Starting January 1, 1998, early withdrawals of up to \$10,000 from an IRA will be exempt from the usual 10% preretirement withdrawal penalties as long as the money is used to buy, build, or rebuild a "first-time home" — defined rather generously as any home bought by someone who hasn't owned a home in the prior two years. Close relatives of such home buyers can also withdraw funds from their IRAs without penalty to help out. This should make it easier for some prospective homeowners to come up with down payments they otherwise lack.

Health Insurance for the Self-Employed

Some of the changes directly benefit contractors by making some business expenses easier to deduct. For instance, self-employed individuals are finally — if slowly — getting the same deductions that corporations have long taken for the costs of health insurance. This new deduction will phase in slowly over the next decade, however, so you won't be able to deduct 100% of your premiums until 2007.

Home Office Deduction

Another big plus for builders is a change in definition of the deductible home office. A 1996 Supreme Court decision had effectively eliminated the home office as a deductible expense for most contractors by declaring that a home office could be deducted only if it was the place where the core work of the business was done — a role filled by the job site for most contractors. The new law, however, requires only that the office be the primary place where the business's managerial and administrative tasks are performed. It takes effect on January 1, 1999.

continued

The image shows two tax forms. On the left is Schedule B (Profit or Loss from Business), which is a continuation of Form 1040. It contains various sections for reporting business income and expenses, including a table for depreciation and amortization. On the right is Form 1040 (U.S. Individual Income Tax Return) for the year 1996. It includes sections for personal information, income, deductions, and credits. Both forms are filled out with handwritten and printed information.

Window Certification Programs

by Kathy Price-Robinson

While window technology often seems to move at light speed, installation techniques for these high-tech wonders sometimes seem stuck in the Ice Age. Too often, untrained workers forget backer rods, misapply caulk, leave gaps at joints in ganged windows, or incorrectly handle sealant joints. Naturally, problems follow: Infiltrating water can ruin exterior finishes, paneling, insulation, and framing, while infiltrating air can cancel much of the energy savings new windows are designed to deliver.

Seeking to prevent these problems, a symposium entitled "Window Installations: Standards and Certification" was held earlier this year at NAHB's Washington, D.C., headquarters. The event brought together various groups and speakers who support a certification program for window installers. Many of the attendees called for the development of training and certification programs for window installation. Such programs, they say, not only save energy and money, but give participating contractors a way to distinguish themselves.

A few programs are already offering these benefits. Pacific Gas & Electric, a major western utility, has already trained 1,000 contractors. (One PG&E consultant said the contractors were "hungry for training.") The utility then provides referrals to participants in its energy-efficient window replacement program, which gives homeowners \$15,000 low-interest loans to



High-tech windows can't deliver energy savings unless they're installed correctly.

replace old windows. Other groups elsewhere are developing similar programs.

To find out more about certification programs in your area, contact the National Glass Association (8200 Greensboro Dr., 3rd Floor, McLean, VA 22101; 703/442-4890, nga@glass.org), the Building Environment and Thermal Envelope Council, a council of the National Institute of Building Sciences (1090 Vermont Ave. N.W., Suite 700, Washington, DC 20005; 202/289-7800, bev@nibs.org), the American Society of Testing and Materials (100 Barr Harbor Dr., West Conshohocken, PA 19428; 610/832-9585), or the California Association of Window Manufacturers (2080-A N. Tustin Ave., Santa Ana, CA 92705; 714/835-2296).



Kathy Price-Robinson, of Arroyo Grande, Calif., is a freelance writer on building issues.

Offcuts ...

If those OSHA standards seem too intimidating in book form, you can try reading the *Construction Resource Manual* on the Internet instead. The electronic guide to all OSHA's standards, as well as relevant general industry standards and much other information, can be found at www.osha-slc.gov, under the "Construction" category. It features a search file as well as a list of the most frequently violated construction standards for the last six years.

More than three out of every 100 mortgage applications could be fraudulent, according to an analysis of some 280,000 loan submissions by the Mortgage Asset Research Institute, says a recent report on the Inman News Service Web site (www.inman.com). The study found that 3.3% of the loan applications made to ten major lenders during the six-month study period had one or more of the earmarks of fraud.

A Mixed Bag as Economy Wavers

Rockies cool, Calif. heats up,
Northeast pauses

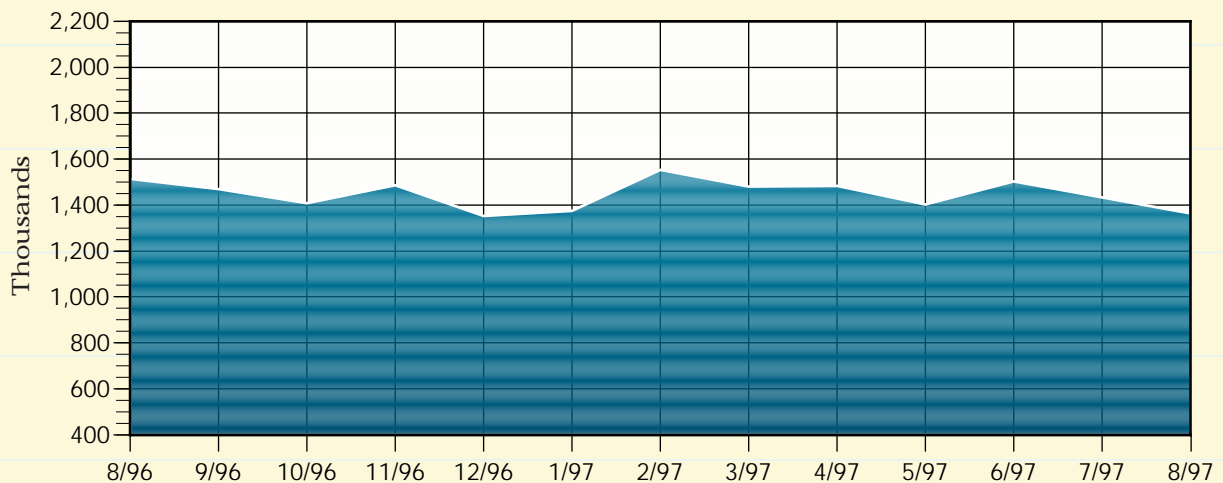
The mixed economy that has characterized the economic expansion of the 1990s continued its fickle ways as autumn took hold, with overall growth checking itself and the building economy surging in some areas of the country while stopping to collect itself in others.

Economists, including those at the National Association of Home Builders, have been saying for a while that the expansion of 1996 and the first half of 1997 would slow at some point to a more sustainable pace. That point seemed to come in late summer, when August housing indicators fell across the board. Starts fell 4.8% from July's pace to a rate of 1.36 mil-

significant variations within themselves. In the West, for instance, California continued its robust growth, with healthy starts and double-digit surges in home prices that indicated demand is presently outpacing supply. California also saw significant increases in speculative building, which it hadn't seen in almost a decade. Meanwhile the Rockies, which have been hot for several years now, finally cooled as starts slowed and predictions of job growth for 1988 were modest. Colorado's state economist predicted job growth of only 2.2% for 1998 — down from an estimated 3.7% in 1997 and from several years where job growth ran around 5%. Fortunately, both economists and building industry officials there said that builders have anticipated this downturn fairly well by not overbuilding, and that supply shouldn't outrun demand too badly.

For builders in the Northeast, meanwhile, the 19.2% drop in permits in August merely continued the yo-yo pattern of uneven growth that had marked that region's slow recovery from the 1990-91 recession. With housing inventories and unemployment both

National Housing Starts
August 1996 to August 1997



lion per year (see graph), down substantially not only from July, but from economists' predictions for a 1.4 - million-plus rate for August. Some saw this as a sign the market had plateaued, others that the market had resumed more sustainable rates. NAHB economists had earlier predicted that starts would end up at 1.42 million for 1997 (down from 1.48 million in 1996) and would cool to 1.34 million in 1998.

The end-of-summer drop was felt unevenly throughout the country. Starts fell 3.8% in the West, 3.5% in the Midwest, 2.7% in the South, and a whopping 19.2% in the Northeast. And those regions saw

low, no one expected the 19.2% drop would be repeated anytime soon.

Indeed, with the basic components of the recent expansion still in place over most of the nation — high consumer confidence and employment combined with low mortgage, inflation, and inventory rates — most observers felt the late-season drop in starts was primarily a market correction to the slightly overheated rate of early summer.

As one Colorado economist put it, "This is not a recession."



Sprinkler Co. Offers to Fix Problem Heads

by Leland Stone

One of the country's leading residential fire sprinkler manufacturers, Central Sprinklers Company, Inc., has launched a nationwide program to test and replace a faulty part in roughly two million of its popular Omega sprinkler heads. The suspect heads, designed for the residential market and manufactured between 1993 and 1996, included an EPDM O-ring that can swell if exposed to petroleum-based products, creating a small chance, according to the company, that the head might fail to open in the event of a fire. A company spokesperson who declined to be named said that no such failures have yet occurred, and that of the "many, many buildings we're testing, most are testing 100% fine." Nevertheless, the company is now making the O-rings out of silicone instead of EPDM and has offered to test and replace the part, at no cost to consumers, in any of the two million units containing the EPDM rings.


Meanwhile, a lawsuit has been filed in California against the company, seeking unspecified damages, though the suit does not claim any sprinklers have failed to operate when needed.

Sprinkler installers seem unimpressed by the hoopla. According to sprinkler contractor Mike



Central Sprinkler Company, one of the country's biggest makers of fire sprinklers, recently voluntarily launched a campaign to replace potentially faulty EPDM O-rings in its Omega line of residential sprinklers. The red dots on the models shown here denote newer versions with updated O-rings; heads without the dots should have their EPDM O-rings replaced with silicon O-rings.

Ricks, president of Katco Fire Protection Systems of Anaheim, Calif., "The problem's been blown out of proportion. Central has voluntarily addressed the issue and done a good job of getting the word out."

To tell if a sprinkler system has the Omega heads in question, look first for "CSC" stamped on the deflector to identify it as a Central Sprinkler Company product, then for the one to three "fins" (actually heat sensors) on the sprinkler's tip that identify it as an Omega model. A red dot on the unit indicates it was made after June 1996 with a silicon O-ring and needn't be replaced. No red dot means it has an EPDM O-ring, and you should call Omega (800/563-6512) for testing and replacement instructions. 

Leland Stone is an associate editor at the Journal of Light Construction.

Offcuts ...

Vinyl continues its steady gains in market share for both windows and siding. Vinyl windows accounted for 27% of all window sales for new homes in 1996 and is expected to claim 50% of that market by the year 2000, according to a report in *Energy Design Update*. In 1990, only 7% of new-home windows were vinyl. Meanwhile, a National Association of Home Builders July 1997 report, "Characteristics of New Single-Family Homes," shows that vinyl siding went on 33% of all new homes last year, further opening its lead over wood (23%), brick (21%), stucco (16%), and aluminum (2%). Vinyl siding has made its gains primarily at the expense of wood (which it first passed in 1994, 28% to 27%) and aluminum, which it has pretty much buried.

The only job worse than construction is that of a cowboy, according to a survey of 10,000 high school students that ranked construction 251st out of 252 possible jobs. NAHB's *Nation's Building News* reported the results of the ABC News survey in a story that described widespread shortages of skilled labor shortage. To judge from the survey results, not many among the 16- to 19-year-olds entering the job market will be eager to take up a hammer.

Calif. Okays Dual Piping to Use Recycled Water

by Kathy Price-Robinson

A few years from now, if you break open the wall of an office building, school, or prison in California, don't be surprised to see purple tape spiral-wrapped around copper piping. The purple wrap is not the latest fashion craze, but the marker for newly approved plumbing runs desig-



Purple tape on water piping indicates reclaimed, non-potable water.

nated for reused, nonpotable water.

Reused water is a hot topic in water-starved California, where a new bill (AB 1522) has broadened and clarified the types of buildings in which recycled water can be used for toilet and urinal flushing. The bill approves such dual-piping systems for all commercial, retail, and office buildings, as well as for theaters, auditoriums, schools, barracks, dormitories, jails, prisons and reformatories, and some apartment buildings and hotels.

Using recycled water in this way is only one of several solutions that states and communities across the country, and particularly in the arid West, are trying as they seek new ways to reuse treated wastewater. The recycled systems are not complex, says Bob Castle, a Marin, Calif., water official and a strong supporter of using recycled water. "It's just like other plumbing," he says, but instead of delivering crystal clear drinking water for flushing toilets, the second set of pipes brings recycled water from a wastewater treatment center — water that often comes close to meeting drinking water standards, but which would otherwise be discharged to the general environment. Now the water will be delivered along recycled water mains that in many areas already parallel potable water mains, and which will be installed or activated in more areas as demand increases.

The potential water savings are significant. In office buildings without a cafeteria or restaurant, only 10% of the water consumed is used for drinking, washing hands, and other uses requiring potable-quality water; 80% is used to flush toilets and urinals, and 10% is used for cooling towers.

The new purple-wrapped pipes will help California reach its goal of recycling 700,000 acre-feet of water by 2000 and 1 million acre-feet by 2010. As Castle says, in a state as short of water as California, "water is too precious to use only once."



Tax Law Changes continued

This and That

The bill contained several other tax law changes or additions that might benefit contractors: A special estate-tax provision for family-owned businesses, effective Jan 1, 1998, raises the estate-tax exemption for such businesses from \$600,000 to \$1.3 million — meaning the first \$1.3 million of value in an inherited business is exempt from estate taxes.

Beginning next year, businesses can take advantage of new welfare-to-work tax credits for hiring a certain class of employees.

In addition to the existing IRAs, to which contribu-

tions are deductible but withdrawals from which are taxable, a new type of IRA features non-deductible contributions and tax-free withdrawals. And as noted above, all IRAs may now be drawn from tax-free at any time to help first-time homebuyers.

The regular "Tax Talk" column will explore some of these changes in more detail in months to come. In the meantime, all of these changes are worth reviewing with your accountant to see how your tax situation will change over the coming years — or preferably, before year-end 1997, in case you need to make some adjustments this year to take advantage of them.



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