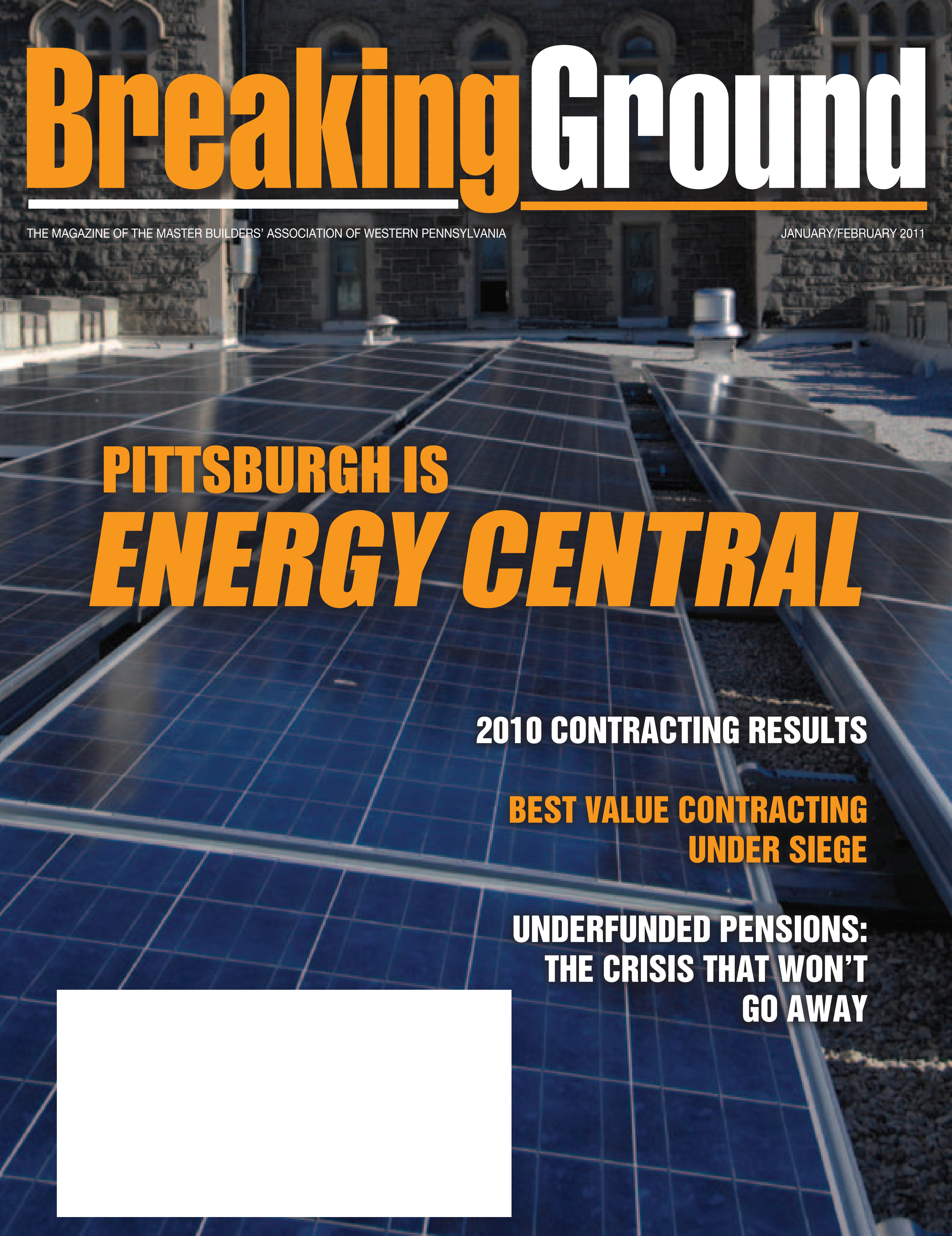

Breaking Ground

THE MAGAZINE OF THE MASTER BUILDERS' ASSOCIATION OF WESTERN PENNSYLVANIA

JANUARY/FEBRUARY 2011

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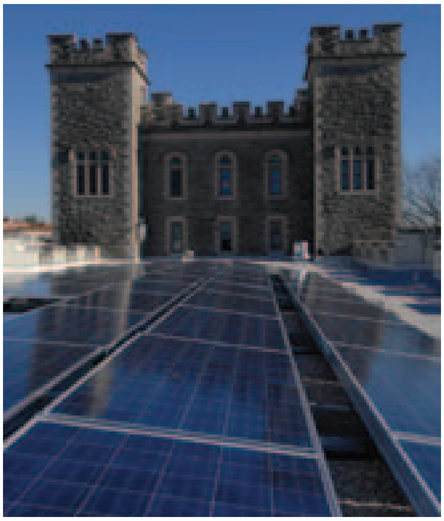

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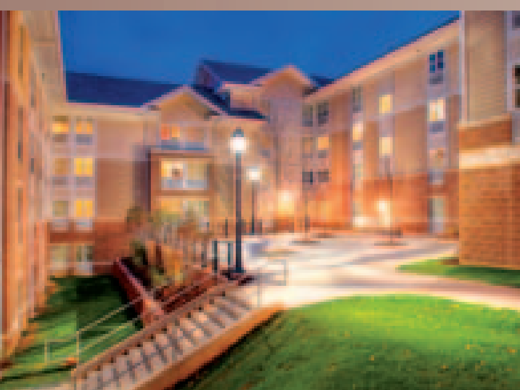

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Publisher's Note

There is a certain redundant feel to this edition that I have accepted can't be avoided. Our editorial calendar always focuses on a few major industry segments every year and tries to detail how that segment is impacting construction and real estate. It's been almost three years since we looked at the impact of energy, so it was time to do so, but on the heels of our annual 'Big Picture' edition the energy update is a little redundant. I certainly hope you won't feel it is too much so when you've completed your reading.

The lifespan of *BreakingGround* has paralleled the rise of the energy industry in Western PA, although that has been inadvertent, I assure you. When we began researching the inaugural edition in the late spring of 2006, the price of oil was around $50 per barrel but beginning with the $20 per barrel spike attributed to Hurricane Katrina, the cost of energy became a focus of industry from that point on. About six months into publishing, Westinghouse made its fortuitous announcement that it was building a new headquarters in Cranberry Township. And about a year later, as oil and natural gas prices set record highs, we began to hear about something called the Marcellus Shale formation.

When you think about all the hottest trends in the region – natural gas, nuclear, green building, and urban rebirth – over the past five years, there is an energy story line in most of them.

The growth of the businesses involved in energy provides a lot of economic benefits to the region, but maybe the most interesting may be the opportunity for a rebirth of what regional leaders refer to as 'good paying manufacturing jobs.' The phrase is somewhat mutually exclusive as it relates to the kinds of manufacturing that were once done in Southwestern PA. As long as the American consumer expects to buy toasters for $15 and refrigerators for what they cost in 1979, it won't be possible for Americans to make things and be paid well for it. As demand for energy creates growth in coal, natural gas and power plant employment however, a substantial number of field and plant jobs are being created. For a region whose economic recovery has been built on healthcare, technology and higher education, an increase in blue collar employment is a real bonus.

Maybe it is because the economic benefits of the energy boom are so enticing that we often overlook another important benefit – national defense. The specific sectors of the industry that are flourishing here vary from cutting edge to almost prehistoric but they have in common that all represent alternatives to oil.

The country has been through a lot of turmoil during the past decade, both economically at home and politically on the world stage. The economic turmoil has more to do with deleveraging from an overextended credit hangover than with an oil crisis (which was the cause of the 1970's malaise). Our overseas issues all relate directly or indirectly to a small region of the world that owes its political relevance only to oil.

Imagine the Middle East in a world where oil demand was a few million barrels per day instead of the 85 million that are consumed each day currently. Prices would be a fraction of what they are now and supplies would seem endless again. Our interest in the region would likely be what it was 100 years ago, with the exception of our political ties to Israel. Without the capital that their oil fields provide, the troublesome nations simply couldn't be much trouble.

The key to making these politically troubling areas less influential is to reduce, if not eliminate, the oil that we consume. This can be done through conservation of energy and by developing technologies that substitute other fuels – like nuclear and natural gas – for the oil that meets our energy demand today.

Converting diesel fleets to liquid propane, replacing oil-fired plants with natural gas and using nuclear fusion are but three examples of changing technology away from oil. They are also examples of changes that move towards using energy that has ties to Southwestern PA. Oil prices seem destined to remain high. Reducing the amount of oil we use is a good idea for our businesses and our national security. And nearly all the alternatives to oil are extracted or produced or engineered by many companies based in this region. It sounds like Southwestern PA is going to be a center for energy for the foreseeable future.

Certainly, there are some downsides to our local energy industry. Nuclear energy is very clean and has had a safe track record for more than two decades. The problem for that industry is that there are no small incidents and the rise in nuclear power plant production is only one incident away from a big chill. Natural gas exploration has its own environmental concerns as well, and we are unfortunately still in the early stages of finding out about that. Both sides of the argument have exaggerated their positions so that it's difficult to judge just how real the environmental risks are. The reality is that our economy is only beginning to heal and the prosperity that the natural gas industry offers is too good to pass up, so we're probably going to learn about those risks on the fly. Our new governor has a big budget hole to fill and is highly committed to rejuvenating the state's economy. Don't expect Harrisburg to get in the way until there are obvious problems.

If the rosy predictions coming from the gas, nuclear and clean coal industries are even close to being accurate it will be an interesting time to live in Western PA. It's felt a bit like a boom town around here for the past five years but the truth is our economic fortunes – while healthy – haven't seen a boom yet. I certainly have never lived in a city that was truly experiencing a boom (although Pittsburgh from 1979 to 1983 and Dallas from 1986 to 1991 definitely were in the bust mode), and I think that's an experience I'd like to have.

Jeff Burd

REGIONAL UPDATE

Business conditions for the regional construction industry at the beginning of 2011 are shaping up just about the way you would expect if the trend in the economy was shifting to growth again. As it turns out, business cycles run their course without regard to calendars and so the positive momentum that is shoving the market forward will play out in a way that won't help many of the construction firms this year, at least not those whose fiscal year coincides with the calendar year.

For those firms who didn't foresee the recession's effects restraining business until 2012, this isn't good news but the silver lining in this slightly gloomy news is that the indicators of better conditions will be present from January 1. That won't necessarily improve income statements or balance sheets at year's end but it will mean growing backlogs throughout the year.

For real estate brokers, developers and design firms the conditions are pointing toward improved business at the outset.

Most of what has been dampening activity over the past two years has been the residue of national macroeconomic woes. Unlike most major metropolitan areas, Pittsburgh has not suffered greatly from the loss of a major financial institution. True, the demise of National City had some negative impact on the local businesses, and on an emotional level seemed to mark the end of the Union National/Equibank legacy, however the net result of Nat City's problems is a stronger Pittsburgh bank – PNC – and an opportunity for another regional bank – First Niagara – that is financially solid. Both Pittsburgh's major bank employers prior to the meltdown – PNC and BNY/Mellon – have navigated the fallout well and had much less exposure than other banks.

Other major employers felt the impact from the global recession as well but have also benefitted from the first stage of the recovery. Among these are the steel manufacturers and the major education and healthcare institutions. While not fully recovered from the endowment and investment income hits received during the stock market crash, UPMC, the University of Pittsburgh and Carnegie Mellon are showing income in excess of expenses, as is even troubled West Penn Allegheny Health System of late, and their capital plans have come back to life.

Of course, the continuing evolution of the natural gas, nuclear and alternative energy industries, plus strength in regional manufacturing is also raising the economic tide. The sum of all these incremental improvements and structural strength is an employment picture that is much rosier than America's in general. Just before Christmas, the economic data showed the Pittsburgh metro area unemployment rate declining again, while the state and national rates inched higher. At 8.6% (down from 8.8% in October), the November data confirms that regional employers are adding to their payrolls. Further evidence of this came from a December study of employment listings by the Three Rivers Workforce Investment Board, which showed 30,000 unfilled jobs. Although almost all of the jobs required something other than a college degree, most offered above poverty level wages.

In addition to the more optimistic economic conditions, the supply/demand dynamics for the major real estate categories have continued to improve throughout 2010. According to Grubb & Ellis, vacancy rates for the overall Pittsburgh office market were running at 16%, with the central business district (CBD) one percent lower. Grant Street Associates reported net absorption of office space in 2010 of roughly a quarter million square feet, with over 500,000 square feet of new construction completed during the year.

CBRE Pittsburgh reports declining vacancies in industrial properties, with an overall market vacancy rate of 8% for 115 million square feet of industrial properties. With little or no speculative industrial or warehouse space constructed in 2010 the availability of Class A industrial is extremely limited, especially in the I-79 corridor north and south or the airport/Parkway West corridor. The shortage of space has prompted early development work for several large projects in the west. Site work has begun for Chapman Commerce Center, where a 90,000 square foot building is anticipated in 2011. The Airport Authority cleared the way for a major expansion of the Clinton Commerce Park at I-376 and the Clinton Road interchange.

	SFD	SFA	Total
Total Pittsburgh MSA 2009	1,517	1,290	2,807
Total Pittsburgh MSA 2010	1,540	941	2,481
% Change	1.5%	(27.1%)	(11.6%)

Permits for new homes declined from 2009 to 2010. Source: Pittsburgh Homebuilding Report.

Preliminary planning has been done for new construction at Jendoco's Settlers Cabin Industrial Park and Imperial Business Park. Other flex/industrial projects are being planned or entitled in the Cranberry/Jackson Township area north, and in the Canonsburg area near the Marcellus Shale sweet spot in Washington County.

What's impeding all of this commercial construction – including a number of projects in the pipeline for more than two years – is the limited availability of financing. With historically low rates, developers should have been borrowing and building for the past year now, but lending conditions remain below levels that are comfortable or commensurate with the risk of development. Loan-to-value ratios continue to creep up, but remain closer to 70 percent than the historical norms. And appraisals are still conservative, despite the steadily climbing occupancy rates, leaving developers with projects facing equity contributions that are effectively 35 percent or more. While Pittsburgh remains an attractive commercial market, the demand for space here doesn't justify rental rates that would offset the substandard returns that the financing conditions are yielding.

Housing starts mimicked the softness of the national market, albeit for differing reasons. With pre-crisis foreclosure rates and year-over-year appreciation of almost three percent, the conditions should be right for higher new home construction. Like most of the nation though, buyers are still de-leveraging here and sufficient anxiety remained in 2010 to have kept people in their existing homes. At year end, the Pittsburgh Homebuilding Report listed 2,481 total dwelling units started, an 11% decline compared to the 2,840 started in 2009. Traditional detached units showed a one-and-a-half percent increase, but the drop-off of nearly 400 units of attached or multi-family units dragged the total into negative territory.

At the start of the year, however, there are signs of life in the housing market. In November, builder Heartland Homes reported a single day sales record of 28 new homes and forecasted topping 600 new home sales for the year. After several years of little or no development in the region, new subdivisions have been going through the municipal process in more than a dozen areas throughout the region. Part of the reason for the continued home price appreciation in metropolitan Pittsburgh has been the cutback in construction, keeping inventories from swelling beyond demand levels. The downside of that has been that no incentive has existed to create new subdivisions, so lot inventories have been depleted in recent years. What bears watching in the new construction market is that no ramp up in demand occurs before the new subdivisions come on line, which would create a short-term lot shortage and temporarily spike prices.

On the non-residential side of the business, activity in 2010 unfolded much as was expected, for better or worse. The total contracting volume for the year was $2.73 billion, a total which includes contracting at AK Steel and the beginning of the work at the USSteel Clairton Works. While the overall commercial and institutional segments of the market were slower than average, a few building types – notably hotels/motels, grocery stores and retail – had higher than expected contracting volume. Retail was especially surprising given the sluggish consumer economy, with more than 1 million square feet of new retail space.

On the basis of anecdotal evidence alone, the start of 2011 appears to be much brisker than the last two years. Architectural offices, particularly the small-to-medium sized general practices, are busy as the first quarter begins, which portends improved bidding activity in the early months of the year.

Supporting this non-quantitative analysis of the market as 2011 begins is an increase in the overall number of projects in the planning stages. The Construction Pipeline lists over 400 projects currently being designed in the seven county metro, totaling $7.5 billion. The historical trend for burning through planning backlog is that there is usually three years worth of projects on the boards at any one time, approximately 50 percent of which will be built in the first year. There are times, like when a market is emerging from a recession, when more of the planning stage backlog will occur in year two but a forecast of between $3.5 and $4 billion for the nonresidential sector in 2011 is on target, especially since the $1.2 billion rolling mill for Allegheny Ludlum in Brackenridge is expected to finally begin.

Among the sectors that should be stronger in 2011 than last year are universities, hospitals, private office and industrial development and apartments. Among the projects slated to bid in January and February are the $30 million Parran and Crabtree Halls at Pitt, the $100 million Mt. Lebanon Junior/Senior High School, $30 million Hermitage Wastewater Treatment Plant, and a re-bid of the $45 million Connellsville High School. BG

NATIONAL MARKET UPDATE

Just two years removed from the 'black swan' crash of the financial markets that exposed a deep global recession, the national economy seems to be on its firmest footing since the winter of 2007-2008. Many questions still remain about the duration and vigor of the recovery, but several respected observers have released outlooks for 2011 that show at least guarded optimism. Couple with recent economic data, these forecasts all point to the passing of the bottom of the market.

In its 2010 Construction Outlook report, released on Oct. 29, McGraw-Hill Construction estimates that construction starts nationwide will show a decline of 2 percent in 2010, followed by an increase of 8 percent in 2011. That forecast is in line with forecasts made earlier in the month by Reed Construction Data, the American Institute of Architects and the Associated General Contractors of America. Having four concurring forecasts is absolutely no surety of a better market, but the tight range of the expected growth – from a low of 3 percent to a high of 8 percent – suggests that all are drawing a similar conclusion from the myriad of data.

McGraw-Hill's estimate follows declines of 24 percent in 2009, 13 percent in 2008 and 7 percent in 2007. Commercial construction, which is expected to pull back by 17 percent from 2009 levels, had the sharpest decline of any market sector and was significant enough to drag down growth in all other sectors. "2010 was another year of double-digit declines for commercial construction," said Robert A. Murray, MHC vice president of economic affairs. "The declines slowed compared to 2009, and commercial construction looks to be on the uptick in 2011." The Outlook report forecasts a 16 percent increase in commercial building starts in 2011.

Looking to 2011, the report predicts that growth will mainly be driven by single-family housing (+27 percent) and multi-family housing (+24 percent) starts. Other expected growth areas in 2011 include manufacturing buildings (+9 percent) and health care facilities (+9 percent). McGraw-Hill foresees declines in highways, bridges and other transportation construction, largely due to the weak fiscal condition of states and the end of stimulus spending.

Urban Land Institute (ULI) and PwC US released their Emerging Trends in Real Estate® 2011, which showed that investors and commercial professionals are expressing guarded optimism about the real estate market for the first time in three years.

Survey respondents indicate a lowering of performance expectations, anticipating high single digit returns for core properties and mid-teen returns for higher risk investments. Even with sidelined capital at historically high levels, market conditions won't allow the higher leverage, and therefore higher risk, necessary to command higher returns across the board. The survey respondents believe that lenders with strengthening balance sheets will finally step up foreclosure activity and dispositions of properties during 2011 and 2012, helping values reset 30-40% below 2007 peaks.

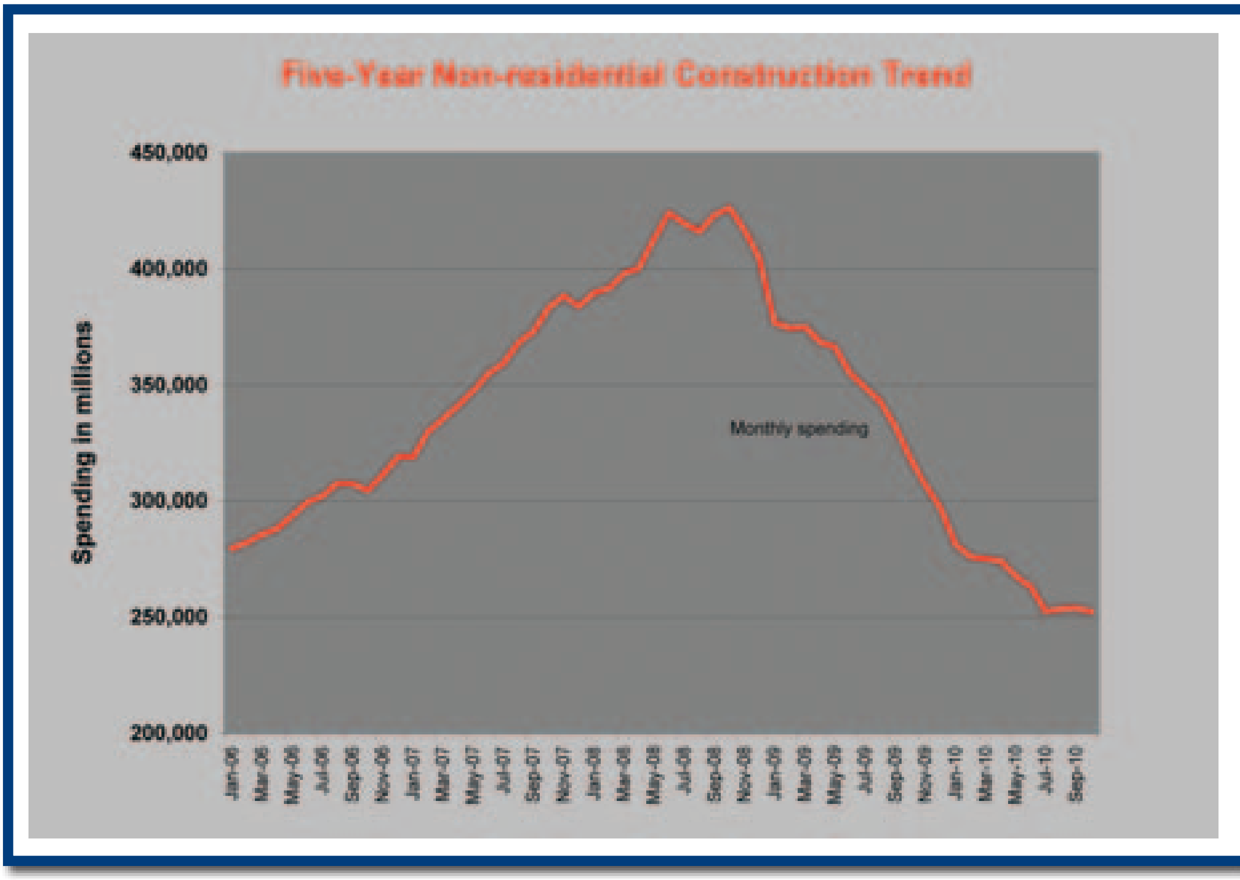
The pent-up demand for capital investment is expected to increase the gap between desirable properties and run-of-the-mill assets. Offices, apartments, industrial and retail properties in good locations, with high occupancy and strong cash flow will attract a disproportionate share of attention, while risk aversion will remain high enough to keep marginal performing properties unwanted.

"...AND COMMERCIAL CONSTRUCTION LOOKS TO BE ON THE UPTICK IN 2011."

The report predicts debt markets thawing further in 2011 as banks continue to strengthen balance sheets, take their losses and step up lending, resulting in higher transaction volumes. But borrowers should expect similar dynamics in underwriting as in investing. As lenders get back into the commercial real estate game they will seek leased-up, cash flowing buildings and shun those with vacancy or rental rate issues.

ULI foresees 2011 as the year that cash comes off the sidelines. "Real estate market participants continue to see a gulf between buyers and sellers, however, there is an expectation that the 'bid-ask" spread will begin to close in 2011 as selling sentiment improves dramatically from last year's all time survey lows and buyers temper expectations for giant discounts," said ULI Senior Resident Fellow for Real Estate Finance Stephen Blank. "Investors with cash could have excellent opportunities to seize market bottom plays by recapitalizing cash-starved owners or buying foreclosed assets."

The rebounding dynamics of the commercial real estate market seem to be reflected in the data for new construction. The Commerce Department reported non-residential starts for its most recent month – October 2010 – and the data showed virtually flat volume for the fourth consecutive month. Starts were a seasonally-adjusted $252.2 billion in October, which was within 6 one-thousandths of a percent of the starts from July through October. After a precipitous decline of almost 50 percent from the October 2008 high, the leveling off suggests a bottom in contracting, and interestingly



Non-residential starts from July-October show a bottom to the two-year decline. Source: Bureau of Census.

matches the same four-month start volume of mid-year 2005. Non-residential construction climbed steadily from that point until the peak in 2008.

A more general indicator of economic health, The Conference Board reported a 1.1 percent rise in its November index of leading economic indicators. Nine of the 10 component indicators included in the index rose in November, with the largest positive contribution coming from the index of supplier deliveries. Building permits were the only negative contributor.

The Conference Board's report sees November's indicators as evidence of a broadening of the economic recovery.

Also, the Federal Reserve Bank's Beige Book reports improving business conditions in 10 of its 12 districts during the fourth quarter. Slight to modest improvement was reported in Boston, Cleveland (which covers Western PA), Atlanta, Dallas and San Francisco, while New York, Richmond, Chicago, Minneapolis and Kansas City reported stronger improvement. Most districts reported an improvement in commercial or infrastructure construction and marginal improvements in real estate fundamentals. All of the districts reported continued weakness in housing markets, with no prospect for significant improvements in 2011 until excess inventories could be burned off.

The two factors most significantly impacting the national housing market are the high unemployment and high inventory of unsold homes, which keeps values depressed.

Data on employment is still mixed but the fourth quarter included several positive surprises about hiring. Private payrolls continued to expand and jobless claims fell. A survey of 18,000 employers showed that 9 percent more (seasonally adjusted) intended to hire in the

MOST DISTRICTS REPORTED AN IMPROVEMENT

IN COMMERCIAL OR INFRASTRUCTURE CONSTRUCTION ...

first quarter of 2011 than to lay off. This represents a big improvement over the 5 to 6 percent net gain of the past four quarters.

On the housing inventory front, the data is less optimistic. Prices for housing continue to show modest improvement month-over-month but intermittent monthly declines still plague the industry, an indication that inventory is not on a steady declining trend. New home construction for 2010 remained below 600,000 units for the third straight year, a level that is less than half that of the new household formation rate. With that level of supply constriction and record low mortgage rates the stage should be set for an explosive recovery in housing, yet nothing seems to be less likely than that for 2011.

As 2010 closes there is little or no data to give clarity to the foreclosure situation. High levels of foreclosures have been ongoing since the sub-prime mortgage market imploded in mid-2007, yet the number of problem mortgages that have been worked through is yet unknown. The foreclosure 'mini-crisis' of early fall, which doesn't seem to have unearthed evidence of unwarranted foreclosures, put a temporary drag on foreclosure proceedings and further clouded the picture. Without some solid data on what remains in the foreclosure pipeline, buyers will have reluctance to enter the market for fear that another significant drop in values is to come.

The prospect of an economic recovery without a recovery in the housing market seems counterintuitive, but evidence is growing that such a recovery is underway. Uncoupling a robust housing market from economic prosperity seems almost un-American, especially since history shows that improvements in an individual's economic status usually translates into an improvement in his or her housing status. As of today, however, there is still little data to indicate just how many borrowers improved their housing status without improved finances during the past boom. Until that piece of the puzzle is found, the future of the housing market remains unclear.

What is clear is that the economy is improving to a greater degree than the housing market. And of the two possibilities – a recovering general economy or a recovering housing market – only the former seems likely in 2011. BG

WHAT'S IT COST?

Construction inflation – and deflation – has become a broken record as the New Year dawns. Metals and petroleum products continue to rise. Producer prices for construction are rising about four times as fast as consumer prices. Most building materials' prices have remained flat or fallen slightly but the sharp rise in metals and petroleum refined products is offsetting the declining materials. And prices for finished buildings, which include pricing for profit and overhead, remain flat compared to 2009.

The result of that pricing action is that contractors and subcontractors, in particular, are not able to pass on the four-to-five percent increase in materials in their bids. This is especially true in new commercial construction, where it's difficult to avoid the impact of the higher prices in steel, copper, paving materials and diesel, and in renovations that are heavier in the share of work effected by the rising materials, like roofing, electrical or plumbing.

And the trend seems to be continuing. In the weeks since the Bureau of Labor Statistics measured the November producer prices, copper has continued higher, reaching $4.20/pound on December 14. This level is a new high, even above the summer 2008 prices. The Energy Information Association reported that diesel reached $3.23/gallon that same week, a two-year high and some 18 percent above mid-December 2009. Industry leader Nucor Steel announced on December 8, that transaction pricing for concrete reinforcing bars, merchant bars and structural products was increasing by $45/ton effective January 1.

At the same time the continued weakness in residential construction has put downward pressure on the materials used extensively in new homes, although the finished cost of new residential construction was up 3.9 percent in the last year. Lumber, plywood and drywall have all fallen back in the second half of the year since manufacturers attempted to get aggressive price increases to stick in the spring. Products used heavily in commercial as well as residential have seen the effects of softer construction demand on their pricing. Prices for masonry materials, concrete, and paint have all remained flat or fallen over the past twelve months.

What is driving the inflation that is occurring is that same thing that pushed prices higher in 2008: growing global demand. While the U. S. economy is getting stronger, more robust recoveries in Asia and parts of Africa and South America are creating demand that is higher for basic materials. One clue to this trend is the higher rate of inflation on iron and copper scrap than on the finished steel and copper, which are less portable than scrap. With no new U. S. plants coming on line or being shuttered in 2011, expect the scrap market dynamics to drive pricing until the major emerging markets slow or overheat.

PERCENTAGE CHANGES IN COSTS	Nov 2010 compared to		
	1 mo.	3 mo.	1 yr.
Consumer, Producer & Construction Prices			
Consumer price index (CPI-U)	0.0	0.2	1.1
Producer price index (PPI) for finished goods	0.4	1.3	3.5
PPI for construction	0.5	1.0	4.6
Costs by Construction Types/Subcontractors			
Residential buildings	0.4	0.7	3.9
New industrial building construction	0.0	0.2	0.2
New warehouse construction	0.0	0.5	0.2
New school construction	0.0	0.2	1.3
New office construction	0.3	0.0	-0.1
Concrete contractors, nonresidential	0.1	-0.6	0.5
Roofing contractors, nonresidential	0.1	0.3	-2.1
Electrical contractors, nonresidential	-0.1	0.7	0.8
Plumbing contractors, nonresidential	-0.2	-0.5	1.4
Costs for Specific Construction Inputs			
#2 diesel fuel	4.8	10.6	18.5
Asphalt paving mixtures and blocks	-0.3	-1.1	4.6
Concrete products	0.0	-0.1	-0.3
Brick and structural clay tile	-1.5	-0.6	-0.3
Plastic construction products	0.7	1.2	3.3
Gypsum products	-0.2	-3.0	0.8
Lumber and plywood	0.1	-2.1	5.8
Architectural coatings	1.0	1.7	-1.5
Steel mill products	-1.7	0.8	12.1
Copper and brass mill shapes	5.6	17.0	16.4
Aluminum mill shapes	3.5	7.6	14.3
Fabricated structural metal	0.0	-0.5	0.3
Prefabricated metal buildings	-1.1	-1.5	8.4
Crude petroleum (domestic production)	6.6	13.4	11.8
Asphalt (at refinery)	1.9	-7.3	3.7

EXPECT THE SCRAP MARKET DYNAMICS TO DRIVE PRICING UNTIL THE MAJOR EMERGING MARKETS SLOW OR OVERHEAT.

Assuming supply and demand tied to construction remain relatively steady, the other potential impact on pricing – especially copper and petroleum – will be if the prices reach the point where contractors and owners seek substitute materials. This phenomenon happened most recently in 2008, when record prices forced the substitution of aluminum for copper in electrical materials and record gasoline and diesel prices curtailed driving. With copper already again at record levels and diesel only 20% below its high, higher demand from a faster recovery than expected will motivate behavior similar to that of 2008.

Expectations for the national and global construction markets are higher than at the same time last year. BNY/Mellon's chief economist Richard Hooey recently upped his forecast of U. S. GDP growth to between 3.5 and 4 percent, a pace that is triple the rate of 2010's consumer inflation. The upside of that forecast (and it is only that) would be that economic prosperity accompanies periods of growth above inflation. The downside of that potential reality is that higher GDP growth would most likely loose the reins on inflation of commodities. Even more conservative growth forecasts are still expecting rates that double the current CPI level, so some measure of inflation seems baked into the forecast for 2011.

With building product manufacturers suffering losses or reduced profits since 2008 it's hard to imagine many of them maintaining 2010 pricing levels. The drywall industry attempted a 20% increase in 2010 without any supply/demand support. Growth in demand should create an atmosphere where similar price increases will be tried by more industries. BG

20-CITY INDEX (1913 = 100)		Dec-10 Index Value	% change Month	% change Year
Construction Cost		8,952.40	0.0	3.6
Labor		19,103.29	0.0	3.5
Hourly wages	$	36.30	0.3	3.5
20-CITY INDEX (1913 = 100)		**Dec-10 Index Value**	**% change Month**	**% change Year**
Building Cost		4,973.89	0.1	3.6
Skilled Labor		8,644.68	0.0	3.3
Hourly wages	$	47.98	0.0	3.3
20-CITY INDEX (1913 = 100)		**Dec-10 Index Value**	**% change Month**	**% change Year**
Materials		2,730.89	0.1	3.9
Cement (per ton)	$	102.62	-1.2	0.9
Steel (per 100 lbs.)	$	45.85	-0.3	5.5
Lumber (per 1,000 ft)	$	396.27	1.5	2.1
Source: Engineeering News Record Cost Index				

ENR's historical index of costs in 20 U. S. cities shows recent stagnant pricing in recent months and a more uniform increase in costs year-over-year.

ENERGYCEN

TRAL

When you think back over the successes of the region during the past half-decade or so, one of the common denominators has been the rise of the energy industry as an economic anchor. A quick highlight reel of the real estate and construction industry is dotted with energy related projects: Consol's new headquarters; Westinghouse chooses Cranberry Woods for its new home; Flabeg builds a state-of-the-art solar plant; and Marcellus Shale everywhere. Even a structure totally unrelated to the energy industry – a new hockey arena – has an energy company's name on it.

For more than a generation, the economic and civic leaders of the region have accepted that the days of having a dominant industry in Pittsburgh were gone, and have been successful at promoting the region's new diverse economy. It must seem like Christmas morning then to have another industry grow up that may employ more people than the steel industry in its prime.

According to the Allegheny Conference on Economic Development, the energy sector has replaced manufacturing as the driver of the regional economy. Its research finds that the industry contributed $13.7 billion to regional GDP in 2009, a figure that is 10 percent of the regional economy. The energy sector directly or indirectly supports 105,000 jobs. More relevant to the construction industry is the impact energy has had on regional real estate.

Summary of Actual, Planned, and Forecast Economic Impacts

Year	Local Taxes *	Employment	Wells Drilled	Output Bcfe/day **	Value Added *
Actual					
2009	$ 389	44,098	710	0.3	$ 3,877
Planned					
2010	$ 785	88,588	1,743	1.0	$ 8,039
2011	$ 987	111,413	2,211	2.5	$ 10,129
Forecasted					
2015	$ 1,417	160,205	2,903	7.6	$ 14,415
2020	$ 1,872	211,909	3,587	13.5	$ 18,853

* In millions current value ** Bcfe = billion cubic feet of natural gas & equivalents

Source: PSU The Economic Impacts of the Marcellus Shale Play, May 24, 2010 Update

Energy companies have been the developer, lead tenant or sole occupant of more than 3 million square feet of new construction since 2008. In the midst of a global recession, vacancy rates continue to fall in office and industrial buildings in the region. In three submarkets the office and industrial space is effectively unavailable except to users of less than 10,000 square feet, and in two of the three – Cranberry and Southpointe – the dominant force is the growth of energy businesses.

CB Richard Ellis industrial broker Rich Gasperini prepared a report in December showing the Marcellus Shale related transactions in 2010 that were over 10,000 square feet and more than 24 months in duration if leased. Thirteen different industrial space transactions occurred, including build-to-suit, land for new construction and several leases. The gross floor area of the transactions topped 700,000 square feet.

It's clear that companies involved in the energy sector have found their way to Western PA. The future success and growth of those industries will depend on the strength of their markets and how the state and municipal governments respond to these industries. For the near term, the outlook is for more not less.

How Did It Happen Here?

The opportunity for the energy industry to develop as a global center is the result of two main forces, only one of which was the result of hard work. During the past 30 years the private sector and government leaders have spent billions and innovated in countless ways to create an environment that would attract industry. As laudable as those efforts have been, the energy sector wouldn't have found Pittsburgh without what lies beneath it.

As the industrial revolution took root in Western PA, the companies that prospered here loved the intermodal transportation that the rivers and riverbeds (where rail lines easily went) provided, as well as the water that was available for manufacturing purposes. But in retrospect, the driving force behind the growth of industry – especially steel manufacturing – was the abundance of coal. During the early years of the manufacturing boom, plants were located on sites where the coal could literally be picked off the ground. Coal didn't grow up to serve industry, however. Records show coal mining to supply Fort Pitt as far back as 1760.

In 1859 the next big thing in energy occurred here when the first commercial oil well was drilled in Titusville. As might be expected the first crude oil pipelines and long-distance pipelines followed shortly thereafter.

The commercialization of electricity ran through Western PA. George Westinghouse developed the first practical transformer here in 1885. And when nuclear power was in its infancy, Shippingport became the first commercial nuclear plant in the world. Pittsburgh has been at the center of energy's evolution right up until the focus of the world's energy markets shifted to the Middle East.

All that history doesn't ensure anything but museums and a lot of buildings referred to as the 'former' something or other. Manufacturing assured that producers of energy would have a big market in Western PA, and even after the steel industry shifted production away from the region the energy production and distribution infrastructure remained. All that was missing was another catalyst. During the last five years, two catalysts arrived.

In the middle of the last decade, technology for extracting natural gas developed the capability to drill horizontally at depths sufficient to explore the geological formation known as the Marcellus Shale. That formation is believed to have such potential for gas production that the industry essentially pulled up stakes from its exploration operations in the southwestern states to descend upon an area encompassing the better parts of three states. The epicenter of the exploration area turned out to be just south of Pittsburgh.

It's clear that companies involved in the energy sector have found their way to Western PA.

Global demand for nuclear reactors has spiked since 2008 (Source: Westinghouse Electric)

How Long Can it Last?

Like good skeptical Pittsburghers, we have a tendency to look for the other shoe to drop, the unforeseen event that will quell the need for energy or whisk the industry away to the south. This time, however, what the energy sector is after is already here. Energy companies chase the resources (you don't think the oil business gravitated to the Middle East because of the pretty sand dunes). The global demand for energy is on a pace to exhaust the world's oil supply within a lifetime and the most populous nations have yet to hit their economic peaks. Alternatives to oil are essential to meeting the energy needs of the global economy and for the foreseeable future the best of those alternatives involve natural gas, coal and nuclear energy.

Discussions of energy consumption are really discussions about how electrical power is being generated. Roughly 40 percent of the world's electricity is generated by plants using oil or diesel. That volume represents a good bit of the roughly 85 million barrels of oil that are consumed daily to generate the 350 quadrillion Btu's consumed globally. As big a number as that is, global population and economic growth is expected to push demand to 750 quadrillion Btu's in 25 years.

The other, equally dramatic catalyst was the tripling of the price of crude oil and its derivatives in less than a year, culminating in a price of $144 per barrel in July 2008. With the economy beginning to unravel, the skyrocketing energy inflation (natural gas was at $14/MMcf at the time) shocked industry and government into frantic searches for other sources of fuel and energy.

As society began to search for alternatives, few other regions had the convergence of a mature coal industry, nuclear generation engineering, locations for wind and solar alternatives and a leadership in green building to effectively advocate energy efficiency. Two major universities with energy related engineering schools were located in Oakland. The icing on the cake was the reputation that the region had engendered as a desirable place to live. As it turned out, the energy sector came looking for Pittsburgh.

The proof of the pudding is, of course, jobs. A study of the Bureau of Labor Statistics' report on employment by sector shows why Western PA has become central to the energy sector. Of the top 25 markets for employment in the seven major energy categories only three – Detroit, Chicago and Pittsburgh – rank in all categories. Only one of the three is located within the range of all the working oil and coal production sites. That's Pittsburgh.

It is surprising that liquids are still forecasted to be the largest fuel source for energy generation in 2035, but the share of the market for liquids at that point in time should be 30 percent. Assuming the same demand estimates, the increase in global consumption in 25 years should create a market for energy sources other than oil that is twice the size of the total demand today. Resources that fuel just over 200 quadrillion Btu's today will be asked to generate more than 500 quadrillion Btu's in 2035.

The Future in Coal

The surprising winner in all this is the coal industry. Coal is the fuel that drove trains across America, heated Ebeneezer Scrooge's office and was in decline when the manufacture of steel fell precipitously in the early 1980's. But it was also the fuel of choice for a large percentage of the world's power plants.

Coal's downside is the pollution that comes from burning it. Coal was one of the main contributors to the 'smoky Pittsburgh' photographs and memories of earlier generations. When he was mayor, David Lawrence decided that the negative health

consequences of burning coal for home heating were too high and pushed through the unpopular law that required the conversion of furnaces to gas or oil. Over the past few decades the industry has responded to tighter regulation and legitimate concerns about human health by developing technologies to burn coal cleaner and scrub the exhaust from coal burning. Industry estimates are that pollution has decline by 40 percent, while environmental groups believe the reduction is less. Regardless of the reality of the reduction, you shouldn't interpret the visibly cleaner air to mean that the use of coal has declined.

Because of the energy needs of emerging economies the consumption of coal has tripled over the past three decades and the industry estimates that the number of people using electricity generated by coal-fired plants will grow from 1.4 billion to 3.4 billion in the next quarter century.

The advent of scrubber technology that reduces emissions from plants and creates usable byproducts, like fly ash, has created the perception that coal plants can run cleaner than oil or diesel fired plants. One advantage that coal has never relinquished is its affordability and relative abundance. Because the biggest increase in energy consumption is coming from developing economies that are more sensitive to cost and supply, coal is estimated to grow its share of the world's energy market the largest, more than doubling by 2035.

The Rebound in Nuclear

The 1970's marked a high point in the development of nuclear energy. As Arab oil embargoes in 1974 and 1979 escalated prices four-fold during the decade, nuclear power plants presented a clean and plentiful fuel that was an alternative to oil.

Within five years, however, the Three Mile Island and Chernobyl accidents put the industry into a tailspin. Until the cost of crude oil raced upward again in the mid-2000's few noticed that the industry had been working to develop reactors that were more efficient and markedly safer than the first generation reactors. The combination of an increased appetite for oil alternatives and explosive growth in countries like China and India, where nuclear energy was welcomed, created a surge in demand for new nuclear reactors.

One of the principal beneficiaries of this surging demand was Westinghouse Electric. The company's sales were boosted dramatically in 2007 when it received $5.3 billion in orders to build four reactors in China. Those reactors are under construction and will come on line in 2013. Since then the company has grown its sales in India, South Africa, the United Kingdom and European Union. Sales have quadrupled since the mid-2000's and the company currently supplies reactors to serve 20% of worldwide energy demand.

What that has meant for Western PA is related to the success of an effort to keep Westinghouse in the region when it outgrew its Monroeville headquarters. The decision to do a build-to-suit deal in Cranberry Woods resulted in the largest corporate lease in the country in 2007 and the project has been a boon to the North Hills. As it exists today, the Westinghouse campus consists of four buildings totaling 960,000 square feet. The company has also leased another 200,000 square feet in other Cranberry and Marshall Township buildings and is reportedly considering more than 175,000 square feet of new space in the Keystone Summit Business Park in Marshall.

The payoff for the deal to keep Westinghouse from bolting to North Carolina was the new jobs, many of them in engineering,

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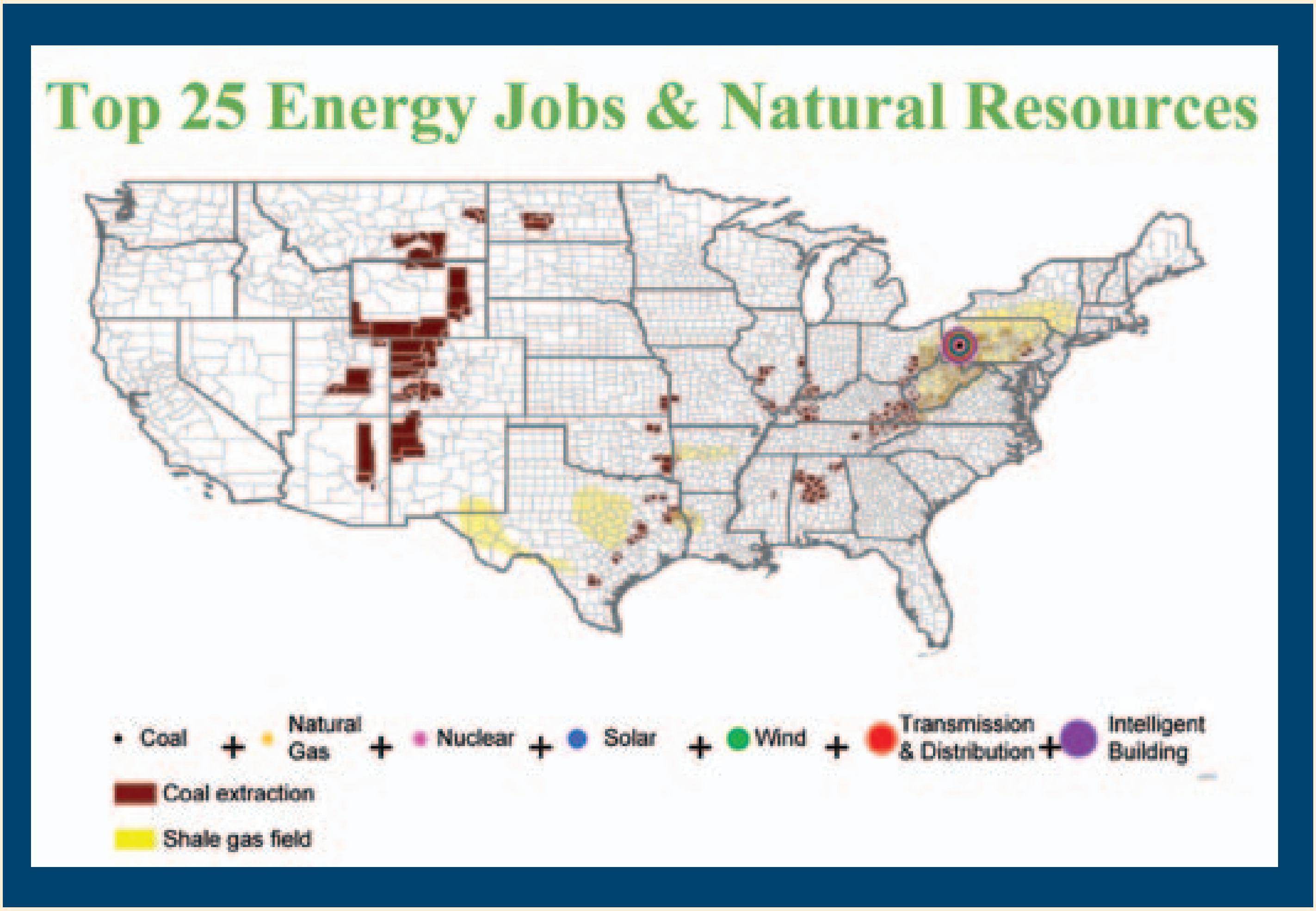

Pittsburgh is the only U. S. city that ranks among the Top 25 in jobs for all seven energy-related sectors and is located within an existing coal or gas field. (Source: Allegheny Conference on Economic Development)

that the expansion would create. The company estimated that it would add 1,000 jobs in a five-year period after the move, but has been hiring at an even faster pace. According to spokesman Vaughn Gilbert, Westinghouse will have 4,200 employees at the Cranberry campus by the end of January. Prior to the move there were 2,500 in Monroeville.

Another interesting facet of nuclear power's growth is the story behind the hiring going on at Westinghouse, which is even higher than the new jobs created. The company estimates it has hired 5,000 people during the past five years and will continue to hire 1,000 per year for the foreseeable future. At least as many of these hires are replacements as new hires. Because of the deep chill in the industry that the accidents precipitated, very few engineers entered the nuclear industry for 25 years. Those dynamics have created a hole between the first generation of nuclear engineers and the current crop. With an average age of almost 50 years, first generation engineers are retiring as fast as new hires can come on board.

While the age gap creates something of a zero-sum game for the industry, the region benefits by having an even larger market for younger, highly educated workers.

The upswing in nuclear power has been largely reported as a Westinghouse story but another nuclear energy company, Bechtel also has a presence in Western PA. The company operates the Bettis Atomic Lab in West Mifflin for the Department of Energy and its engineering presence helped backfill some of the lost positions in Monroeville when Bechtel leased the 105 Jamison Lane facility in 2008. The Elmhurst Group invested $10 million adding 54,000 square feet and renovating 125,000 square feet, a project done by Burchick Construction.

Bechtel's presence, along with a continued presence of 400-500 employees of Westinghouse has helped buffer Monroeville from any economic dent that Westinghouse's relocation may have caused.

Natural Gas Matures

The industry that is making the loudest noise in Western PA's energy sector is natural gas. We began hearing about the Marcellus Shale exploration just a few years ago, and it is only within the past 18 months that the effects of the exploration have become visible to residents outside the areas where drilling is actually occurring.

During the past six months, however, the natural gas companies have increased their visibility. Several companies, most notably Range Resources, have begun print, radio and television

of the new worker. The impact of the consumer demand from the new jobs is likely represented in the relative health of restaurants and retail stores between Peters Township and Washington, but little quantitative evidence of that has been reported. Probably the best measure of the positive impact of the natural gas industry has been in office and production-related new construction.

Secondary businesses have benefitted from the exploration and driven new construction as well. Trucking companies have been adding capacity to meet the over-the-road needs of both the well site construction and ongoing hauling that gas exploration requires. Railway companies have seen spiking traffic and construction of new or expanded yards are underway in Conway and Green Tree. Some of the businesses that have benefitted dramatically are those in industrial supply, providing everything from fire-resistant clothing to filters, valves, and measurement tools needed in gas processing. Local lumber yards and building supply stores struggle to keep adequate inventories of rough lumber, saw blades, adhesives and jobsite consumables. And the drilling activity has been a boon to the local truck and tire dealerships.

advertising. Consolidations, like Chevron's acquisition of Atlas Energy and EXCO's purchase of Chief Oil and Gas's Marcellus assets, have made it easier to see the evolution of the industry from rumor to day-to-day reality.

What has been harder to identify as the natural gas industry has ramped up production has been the growth of jobs. Penn State University's oft-quoted study anticipated hundreds of thousands of jobs created by the exploration and production of natural gas, and the industry is touting that nearly 100,000 new jobs have been created since the beginning of the Marcellus Shale play. Many of these jobs have gone, understandably, to workers from out-of-state who have experience in the industry and are willing to relocate temporarily to the region. The broad nature of the industry has also produced a diffusion of the new jobs, so that in either case it is difficult to stand in any one place at any point in time and see the jobs created. Even with Marcellus Shale organizations dedicated to tracking the action in place, there is no monolithic information clearing house to identify all the jobs being created.

Two years into active exploration, however, it is possible to pick up consistent anecdotal evidence that many more people are working in natural gas than before. Just a quick perusal of the tenant directory at Southpointe's buildings finds 58 firms involved in the energy field, many of whom weren't here just a few years ago. Motel vacancy is non-existent in any of the areas near active well fields, particularly in the outlying areas. And smaller service companies, like those supplying or maintaining drilling or pump equipment, have begun to arrive and swell in size.

While the industry itself has not compiled any totals for jobs created, the Marcellus Shale Coalition's website does have a jobs portal. During November the portal listed between 700-800 jobs consistently.

For real estate and construction, the importance of the jobs created is that each job requires a certain amount of space to operate, some amount of space for support of those activities and ultimately creates real estate needs for the lifestyle consumption

The one unrelated industry that has benefitted most from the expansion of all phases of the natural gas play is construction. The Penn State economic study anticipates that gains in construction employment for 2010 were 13,061 jobs, with 16,601 more jobs coming in 2011.

In Southwestern PA the immediate impact has been felt in increased demand for construction and engineering services used directly to prepare well sites and massive processing and distribution facilities. It's also been felt strongly in downstream businesses who serve the needs of an active gas industry. Paving companies in the areas of drilling activity have been busy during the recession replacing or building new roads after new well sites have been put in service. The cost of road work is in the driller's site budget and municipal officials are discovering that the gas companies are making good on their word to restore roads with surfaces that are better than the existing conditions were.

"Our activities have been mainly in the northeastern corner of the state, where we've been spending almost twice as much to maintain roads as PennDOT has," asserts Dave Spigelmyer, vice president for government affairs for Chesapeake Energy. "In Bradford County we spent $65 million compared to $25 million from PennDot. In Susquehanna County we spent $18 million to the state's $10 million."

Construction projects have followed an evolution from drilling and production facilities in 2008 and 2009, to the construction of more permanent engineering and administrative facilities (e. g. Talisman Energy, Eastern Resources, Baker Hughes, Range Resources) in 2009 and 2010, to the start of the permanent infrastructure for distribution and mature exploration in 2011 and 2012. The latter includes the recent rash of compressor stations that have been built and the frac water treatment facilities that are being planned.

Two alternative industries that have gained a foothold are wind and solar power.

The compressor stations are somewhat limited in scope, involving heavy site work, concrete and process mechanical work, but on average they are $5 to $10 million and up.

Frac water facilities are much larger and involve investments that are much greater than the compressor stations. One of the first of the new facilities is Frac Tech Services new plant off Route 519 in North Strabane Township. Two more facilities that are in the planning stages are Integrated Water Technologies' treatment plant in North Fayette Township and the Cal Frac Well Services facility in the Fayette Business Park in Georges Township.

The next wave of fracking facilities will involve more large-scale facilities as well as a larger number of smaller frac water plants located in outlying areas. McCrossin Development of State College is planning a dozen such facilities in the Johnstown area and an Ohio developer is working on as many as twice that number in eastern Ohio and the Pennsylvania border area. Although smaller than the Frac Tech or Cal Frac plants, these mini-plants still represent about $10 million in construction each.

Calfrac's decision to invest $140 million in new construction and equipment highlights both the shortcomings and advantages of the region. For natural gas exploration, the variable topography of Southwestern PA is much less advantageous than the relatively flat topography of the Barnett shale formation; however, the region's industrial legacy is a transportation infrastructure that reduces the amount of new development needed to support the gas industry that is growing.

"There's no question that the big attraction for Calfrac was the railroad access," says Barry Seneri of the Fay-Penn Economic Council, which developed and markets the park. "Calfrac intends to put their own rail spur in to run sand and chemicals right into their silos at the facility."

The proximity to railroad, as well as access to the Mon-Fayette Expressway and Interstate 68, gives Calfrac great flexibility in transportation to a site that will treat and recycle massive amounts of water, but will also be home to 86,000 square feet of office, shop and laboratory facilities. Fay-Penn estimates that 200 employees will require access to the facility daily and the commercial service to the site will require the easy interstate highway access that comes to the Fayette Business Park's front door.

As the natural gas industry evolves here the legacy infrastructure will continue to be more of a regional advantage than the topography is a hindrance. The plentiful railroad infrastructure that follows the rivers in all directions has been receiving investment by the rail companies in anticipation of the heightened usage. The rivers themselves will likely become more active arteries, especially if the many riverfront brownfield sites that remain are adapted for new industrial use like LP processing and distribution, or waste coal-to-gas facilities that can make use of the intermodal transportation that already exists.

Fayette County has also been the beneficiary of a growing number of low profile Marcellus Shale related business successes. In the past couple of years a handful of companies have acquired

Top World Oil Consumers, 2009 (thousand barrels/day)

	2009	2008	2009 Share
United States	18,686	19,498	22.2%
China	8,625	7,831	10.3%
Japan	4,396	4,785	5.2%
India	3,183	2,962	3.8%
Russia	2,695	2,916	3.2%
Saudi Arabia	2,614	2,376	3.1%
Germany	2,422	2,569	2.9%
Brazil	2,405	2,485	2.9%
South Korea	2,327	2,175	2.8%
Canada	2,195	2,261	2.6%
World Total	**84,077**	**85,239**	

Top World Oil Producers, 2009 (thousand barrels/day)

	2009	2008	2009 Share
Russia	10,032	9,790	12.9%
Saudi Arabia	9,713	10,782	12.0%
United States	7,196	8,514	8.5%
Iran	4,216	4,174	5.3%
China	3,790	3,973	4.9%
Canada	3,212	3,350	4.1%
Mexico	2,979	3,186	3.9%
United Arab Emirates	2,599	3,046	3.2%
Iraq	2,482	2,741	3.2%
Venezuela	2,481	2,643	3.2%
World total	**81,995**	**79,948**	

Top World Gas Producers (billions of cubic feet/day)

	2009	2008	2009 Share
United States	55.4	57.4	20.1%
Russia	58.1	51.0	17.6%
Canada	16.7	15.6	5.4%
Iran	11.2	12.7	4.4%
Norway	9.6	10.0	3.5%
Qatar	7.4	8.6	3.0%
China	7.7	8.2	2.8%
Algeria	8.3	7.9	2.7%
Saudi Arabia	7.8	7.5	2.6%
Indonesia	6.7	7.0	2.4%
World Total	**295.3**	**289.0**	

Source BP 2010 Statistical Review of World Energy
US Energy Information Administration

existing Fay-Penn Economic Development Corp. buildings or acquired land and built new.

Atlas Energy (now Chevron) completed a 24,000 square foot warehouse and office near Smithfield in 2008 and is constructing a 24,000 square foot expansion currently. Universal Well Services also built a new facility, a 30,000 square foot building in Mt. Braddock, PA. Fay-Penn has leased space to R & H Oilfield Supply, GHX Industrial LLC, Chief Oil & Gas and Caiman Energy. Another Marcellus Shale well services company, Express Energy Services LP has leased a facility through a private developer.

Chesapeake's Spigelmyer sees the current activity as building the foundation for the permanent viability of the natural gas industry in Pennsylvania. As he looks out to the end of the decade, Spigelmyer envisions the growth of the industries that are downstream in the supply chain.

"We've always imported gas from the southwest to this region but in four years this area will be a net exporter of natural gas," he says. "Once the commercial infrastructure has matured you'll see the rise of the industries that use gas as a feedstock. I'm talking about glass, plastics, chemicals, fertilizers, powdered metals and the energy needed for steel manufacturing and electrical generation."

Finding Alternatives

One portion of the energy sector for which Western PA is uniquely positioned to serve is alternative energy. On the heels of the hyperinflation of oil prices in 2008 came dozens of plans for creating power using a variety of alternative methods. As these methods came under commercial scrutiny many were found to be inadequate to provide a viable alternative.

Businesses did sprout that gave customers alternatives to fossil fuels but in many cases the costs proved to be too high to be commercially viable unless the price of oil remained at elevated levels. Corn-to-ethanol was found to be cost prohibitive. The output of organic materials or biomass was insufficient to justify large-scale investment in production of alternative fuels. And in the case of most alternative electrical generation, both the output and the capacity of the grid that would receive the electricity were inadequate.

Two alternative industries that have gained a foothold are wind and solar power. When driving on the PA Turnpike

Pittsburgh is at the center of some of the most important resource conservation issues ...

you can see a handful of wind farms, which represent only a portion of those developed in the past half decade. An $80 million farm along the south ridge of Chestnut Ridge in Fayette County is still in the works for Iberdola, but the cost of development for wind farms and the new competitive situation in Pennsylvania's electricity market have slowed the progress of new farms.

Photovoltaic (PV) arrays in not-so-sunny Western PA would seem to be a bad match but the conditions in greater Pittsburgh are only slightly less favorable than the Deep South for solar energy collection. Recent tax credits for adding solar arrays at both the federal and state levels make the investment in PV panels feasible, and the nascent renewable energy credit (REC) market offer incentives that are making solar power more marketable on commercial structures. One regulatory change that would probably boost the use of PV on commercial and residential structures would be the allowance for net billing of power. Being paid to add electricity back to the grid is a much greater incentive than the collection of an ongoing credit balance that cannot be cashed out.

For a variety of reasons Pittsburgh is at the center of some of the most important resource conservation issues and energy is certainly at the top of the list of those issues. American innovation and conservation – like that of the Europeans in earlier decades – can have an impact on the global consumption level. We are still the biggest energy consumer nation, more than double China's consumption and six times as much as India. But even our significant energy conservation measures will be offset by the consumption of the world's emerging powers during the coming decades.

Cheaper and more efficient energy will remain in huge demand as growing economies mature into consumer economies. Into the middle of this century, the trend towards more energy will continue. Whatever problems arise for the energy sector, Western PA will be at the center of the solutions. BG

BAKER HUGHES

NEW STANTON OPERATIONS CENTER

All photos by Massery Photography.

Like all executives, Anthony Martini, president of A. Martini & Company, gets a lot of phone calls. After the summer of 2008 he's glad he always checks his voice mail.

"I was out of town on vacation and checked my voice mail to hear a message from this guy named Ralph Crabtree from Baker Hughes, and would I please give him a call about a project they're planning," he remembers. "I asked my dad [Angelo Martini Sr.] to follow up with Ralph and he set up a meeting at the Holiday Inn in Moon."

Martini was one of a small group of contractors that were referred to Baker Hughes, says Crabtree. "We talked to people in that part of the world to get recommendations and they were one of a handful that we had come out to interview. We work with an architect in Houston who has done our facilities everywhere so our approach to a new area is to find local firms that know the codes and local marketplace and do design/build to get the project done."

Working with an out-of-town owner can pose some unusual challenges, especially if it's a first-time experience. Prudent contractors will have extra due diligence to perform if they wish to avoid working for an owner that will cost them money. Baker Hughes didn't have much of a local presence in 2008, but they were hardly an unknown quantity and the commitment they were making to the Marcellus Shale exploration was going to make them a local presence for quite a while to come. Like his competition, Martini was interested in what Baker Hughes was planning and intrigued enough to meet with Crabtree and his associates.

"We asked about what to bring to the meeting and were told nothing," Martini says. "Dad and I went to the meeting and spent a few hours with them. We talked about how we'd approach the job, how we worked and just got to know each other. At some point they asked about what we thought a building like they were planning would cost and we went through that with them, but most of the time we just got to know how each of the companies worked."

As a third generation Pittsburgh contractor, the Martini's have had their share of similar interviews that ultimately led to having to bid the project against a handful of their competitors, so they were pleasantly surprised to get a call from Crabtree the following day telling them that they had been chosen to build the project in New Stanton.

Landing a $12 million job in the late summer of 2008 turned out to be very fortuitous. During the fall and winter that followed, when A. Martini & Co. and local architect Desmone & Associates worked their way through programming and design, the global economy went into freefall. The chill that went through the markets slowed down many construction projects that were being planned, but the Baker Hughes job continued moving along a fast track. Baker Hughes is a high tech oil and gas exploration company and even though prices for the commodities were falling, the company was as busy as ever around the globe. And its desire to get up and running in Pennsylvania was strong. During the winter of 2009 the Martini-Desmone team was trying to adapt their client's prototypical building requirements to the New Stanton site at the same time the project was becoming something of a moving target.

"Baker Hughes is made up of dozens of companies and at that point it wasn't decided which of them would go into the facility in New Stanton," says Beth Nelson, one of the project architects for Desmone. "The problem was the urgency of getting into Western PA for the Marcellus Shale exploration. There were a number of Baker Hughes divisions wanting to be here but the facility had to be defined at some point. Some pieces of the project were ultimately omitted for now."

It was during this early phase that Nelson, project architect Eric Booth and A. Martini project manager Jeff Feret discovered that the normal process of gathering information about needs and presenting a design that accounts for those needs wasn't going to happen on this project. With each progress print it seemed Baker Hughes had different needs and it wasn't uncommon for changes to be made and then unmade within a few days. Aside from the changing needs, another drag on the design process was the difficulty in communicating questions and answers with Baker Hughes. Jeff Feret recognized early on that the communication issues weren't because of a lack of urgency or organization.

"Baker Hughes has hundreds of facilities in 102 countries around the world," he explains. "Ralph was doing buildings in different continents at the same time as our project, so I realized that the normal way of putting together a design wouldn't work. Instead of asking questions and waiting for answers we began to get with Desmone and prepare answers that we thought would anticipate their approval."

"I'm not sure how we could have done this as anything other than a design/build," says Nelson. "Baker Hughes' architect sites the building and gives the general guidelines about square footage needs, but there are few architectural standards."

For the New Stanton facility the standards may not have meant all that much. Baker Hughes was using the facility to plant a flag

"Because they would be bringing guests in from around the world they were concerned about keeping up the brand," says Nelson. "The blue glass used in the curtain wall is part of their corporate identity. In the warehouse building they were very intentional about having lots of outdoor light come in. The nature of the work drove that design, with the high bays and craneways, but because of the natural light it doesn't feel like a warehouse. We tried to remember that there are scientists working there too."

After the programming and schematic process was complete the space needs were developed for a handful of Baker Hughes groups. Baker Oil Technologies needed general use of the warehouse, which was planned to be 46,000 square feet. The office building was to be two 8,700 square foot floors that were flexible enough to accommodate ebbs and flows in staffing from any of the divisions. The Petralite Division required highly outfitted labs with serious environmental controls. INTEQ was another division with lab needs, as well as clean space to assemble small computer components. The Atlas Division, which was alternately going to be housed in the main buildings or separated, ultimately ended up in a stand-alone 7,500 square foot facility.

in the Marcellus Shale, and would be using the facility to test new technologies and showcase the successes. Exploring shale formations to extract natural gas located at great depths is a relatively new method for the gas industry. Getting access to gas formations a mile deep can revolutionize how America views energy, but it also creates the need for innovation. Baker Hughes is one of the companies constantly working to engineer new solutions for exploration and its methods bring high technology to the age-old business of getting energy out of the ground, technologies that Ralph Crabtree refers to as "like throwing your laptop down a hole a mile in the ground."

The office building was going to be toured by energy professionals from all over the world and Baker Hughes responded to that purpose with changes to its normal office standards.

"We took their basic requirements and the design was pretty basic for the office building until Ralph came in for a progress meeting and immediately started upgrading most of the finishes," recalls Feret. "He wanted ceramic tile used throughout, upgraded millwork, better finishes and granite sidewalks approaching the entrance. All in all he added about $100,000 in finishes."

Baker Hughes chose the Westmoreland County Technology Park, located in Hempfield Township, as the site for the new facility. Although that site is relatively flat for Western PA the topography presented some challenges. The company wanted to take advantage of the site's visibility – it sits along Route 119 – and located the building parallel to the ridge overlooking the highway. That decision meant extending the utilities and created the need for a lift station to serve Baker Hughes. The location also proved to be an unlucky one for the soil, as the pyrites that appeared to be present intermittently during testing turned out to be everywhere that Baker Hughes wanted to develop.

"They bought a site that was a reclaimed strip and deep well mine, so Baker Hughes knew that it wasn't a clean site," says Feret. "But the pyrites turned out to be located exactly where the building and access areas were located. We had to over-excavate

"...LIKE THROWING YOUR LAPTOP DOWN A HOLE
A MILE IN THE GROUND."

Beth Nelson found the pace and the focus of the process to be very energizing. "One thing that this project really did was sell me on the idea of doing design/build jobs," she says. "We have a great relationship with Martini and I was happy designing something that I knew was being built. As an architect I'm much happier being able to focus on what the client needs and getting the job done."

Pushing the schedule was important to A. Martini & Co. Their project management team wanted to take advantage of the opportunity to drive the schedule. Beginning in May 2009, Martini had committed to a construction schedule of twelve to fourteen months, and made sure that the facility was ready to turn over by May 2010. The completion may have been sooner than Baker Hughes expected, as only one department actually moved in by mid-June. Getting a facility ahead of schedule wasn't something about which Ralph Crabtree was prepared to complain.

the building pad; and the access road and utility trenches required a special coating called MC-70. It's an oil based sealant that we had to spray on the pyrites wherever we excavated a trench to keep them from expanding and breaking joints. It turned out to be 1,400 linear feet."

During construction, Feret and architect Nelson discovered that they had to remain flexible in their thinking because they were serving a client in a very fluid industry. Changes in equipment or staffing needs by a user group created changes to the project scope. Power requirements, clearances and HVAC loads had to be revised as the specific requirements unfolded, usually as or after the space was constructed. For example, the water usage of a hydro-lathe was underestimated, causing flooding during the first week of cutting. The solution involved saw-cutting the new floor and significantly increasing the drainage capacity. That's the kind of change that can cause rough client relationships normally, but Baker Hughes seemed to view it and others like it simply as problems that needed to be solved.

"Our buildings have to be built so that they can be changed," says Crabtree. "You have to be open to that possibility because the technology of the equipment changes so rapidly. This job went very smoothly. The key to a smooth job is the pre-planning that we do. We have very experienced people – our architect has done buildings all over the world – and Martini has very knowledgeable people so we were pretty prepared to handle any situation that came up."

"After a while, [project superintendent] John Petronic and I could anticipate what Ralph and his people were expecting," says Feret. "We felt comfortable about just doing things without asking every time we encountered a question because we had to get things done. We were prepared to change something that they didn't agree with but there was little that didn't work out."

"We were very happy with Martini's and Desmone's performance," he says. "I think the building is a beautiful building. I think it sits well overlooking Route 119. We may have the need to expand the facility in the near future and that's a team I'd be happy to go back to." BG

KEY SUBCONTRACTORS

Schultheis Electric .... Electrical
Limbach Co. .... HVAC/Plumbing
Easley & Rivers Inc. .... Interiors
J & H Excavation .... Site work
A. Folino Construction ...... Paving
Multi Metals Inc. .... Misc. steel
Butler Manufacturing .... Metal building
A. J. Vater Co. .... Painting
Redstone Acoustical
& Flooring .... Flooring
Caseworks .... Millwork
H. B. Reynolds Inc. .... Glazing/curtain wall
Tuscano Maher Roofing .... Roofing

STANDARD SOLAR INC.

IN AN INDUSTRY AS VOLATILE AS ALTERNATIVE ENERGY, BUSINESSES POP UP AND FALL AWAY WITH REGULARITY. THAT'S WHY SCOTT WIATER VIEWS HIS COMPANY AS ONE OF THE MORE ESTABLISHED CONCERNS IN THE SOLAR ENERGY MARKET. "EVEN THOUGH WE WERE INCORPORATED IN 2004, STANDARD SOLAR IS ONE OF THE OLDEST COMPANIES IN OUR SPACE," HE EXPLAINS. "MOST OF THE SOLAR COMPANIES WEREN'T FOUNDED UNTIL 2008 OR 2009."

WIATER IS THE PRESIDENT OF STANDARD SOLAR, BUT LIKE MANY OF THE BUSINESSES HE DESCRIBES, HIS PLACE IN THE SOLAR ENERGY INDUSTRY TRACES ONLY BACK TO 2008.

A typical residential solar installation.

Standard Solar was founded by Tony Clifford to serve the booming residential market in Maryland. Clifford, who is now the firm's CEO, was passionate about solar energy as an alternative to fossil fuels. Back in 2004, the addition of solar panels on a residential roof was not a cheap proposition, so Clifford was looking for homeowners and builders who were installing solar as a personal choice, who saw alternative energy generation as the right thing to do. As Scott Wiater describes it, Standard Solar was "looking for the environmentally conscious buyer with excess cash." While that profile eliminated a high percentage of buyers, Standard Solar was at least in one of the best markets to find buyers with excess cash and the company was growing steadily, if not spectacularly.

Company president Scott Wiater

In 2008, a private equity company, Truecast Capital, purchased the company with plans to grow aggressively by pushing solar into a broader spectrum of markets. As part of the new company's organization, Scott Wiater was hired as president. By that summer, market conditions and government response would reward that plan handsomely.

As oil prices soared to record highs in July 2008, the federal government launched a number of initiatives to try to decrease demand for oil and suppress the price. One of those measures was a 30% incentive instituted in late 2008. The incentive rewards the owner of a solar array with a tax credit or government grant in lieu of the credit equivalent to 30% of the retail installed cost or fair market value of the system. Most states also enacted legislation to create incentives. For Standard Solar, the timing of their acquisition couldn't have been better, as Maryland created a grant program and established a renewable energy credit (REC). Moreover, the state began penalizing producers of electricity who fell short of renewable energy goals, which created an even bigger market for the purchase of offsetting REC's. The company's business took off.

During the latter part of 2008 the pace of growth pushed Standard Solar to broaden their business even more by pursuing commercial building solar opportunities and competing for utility installations, which increased the company's capacity to solar arrays generating up to 20 megawatts. Standard Solar also expanded its business to include an energy efficiency and conservation consulting practice, and started to look at markets in adjacent states.

One of the defining characteristics of the solar – or other alternative energy – industry is that it has historically followed the incentives. Because New Jersey and California were for many years the only states to offer tax and financial incentives, the lion's share of the solar companies are either located in those two states or focus most of their sales efforts there. As Standard Solar was preparing its growth strategies in 2009 their top executives decided on a different approach. With the majority of their competitors still heavily committed to business in California and New Jersey, the management at Standard Solar saw Pennsylvania and Delaware as excellent opportunities. Earlier this year they opened an office in Pittsburgh.

"Pittsburgh was an untouched market for the most part," says Wiater. "The strongest parts of the market in Pittsburgh – academic buildings, institutional and local government – are segments where we have had the most success. We're very anxious to partner with local contractors to ramp up the solar market quickly."

Standard Solar's business model is that of an enabler to solar installations. The company doesn't manufacture the solar panels but will undertake or manage virtually all other aspects of a solar project, including financing. Their engineers spend time helping architects and engineers understand what allowances are necessary for solar panels in the design. While they have crews capable of installation, Standard Solar is looking more for local contracting partners – usually electrical contractors or roofers – to be the installers and sales force for the company. In Pittsburgh, they are intending to create a renewable energy 'hub' from which they can provide training, financing, engineering and back office support to local contractors.

Part of the support is training contractors to get certified by the North American Board of Certified Energy Practitioners (NABCEP), which promotes industry standards for photovoltaic and thermal solar installers. Wiaters explains that the certification is important to Standard Solar's strategy of partnering with a limited number of contractors in a market to establish high quality standards.

"The industry is still new so it's highly unregulated," he says. "We're very concerned with quality in a new market so we require that any new contracting partner have or get someone NABCEP certified."

What Standard Solar sees as a sweet spot in Pennsylvania is the Power Purchase Agreements (PPA) it markets to institutional owners. The financial incentives that exist are for the owners of the solar equipment. Institutional owners – like hospitals, universities or public owners – generally own larger buildings and have the time horizon necessary to reap the payback from the initial investment in the solar installation. Most institutional owners are non-profit organizations, however, so the tax credits aren't very useful to them. Standard Solar's model for non-profits is to finance and own the solar installations on the institution's facilities and offer a PPA instead of the renewable energy credits.

PPA's are medium-to-long range agreements that enable the institution to lock in a below market rate for electricity for a fixed period of time in exchange for the REC's. Standard Solar maintains the solar array and has the rights to the REC's for what is typically a ten-to-fifteen year term, while the university or government facility purchases below market power. REC's now trade openly on the Chicago Board of Exchange and Standard Solar is willing to bet that the market for REC's will increase over time as the pressure to find renewable energy sources increases.

While Standard Solar will also sell and install the solar equipment to companies that have an appetite for tax credits, it sees the PPA as a more common way to monetize solar power.

One of the local projects that the company has responded to is for a solar installation at Duquesne University. Colleges and universities are among Standard Solar's earliest and largest commercial projects, with installations at the University of Delaware, American and Catholic Universities. Among prospective students a university's "green-ness" is an important factor. Venerable rating publications, like the Princeton Review, now rank green campuses along with academics and affordability. Most universities can't take the tax credits from a solar project but their credit worthiness is very high, and Standard Solar can readily find investors for the leases and PPA's.

Purely commercial buildings present more of a challenge, since the commercial developer has a difficult time working the cost of investing in solar equipment into his or her pro forma or can't take on a long-term purchase agreement with tenant leases that are much shorter. For commercial buildings Standard Solar has found limited installations to be a better solution, with the goal being solar panels with enough capacity to cover the electrical usage of the common areas.

Scott Wiater likes the outlook for Standard Solar's business model. He knows that the investment in solar energy is a great environmental decision on its own, but he recognizes that the current incentives make the decision to add solar panels to new construction or an existing physical plant much easier.

"I can't think of any deal we've done in the last year where there wasn't a savings to the host right from the word go." BG

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DGS (And Contractors) Struggle With Best Value Procurement

By David Raves, Esq.

Since the enactment of the Commonwealth Procurement Code in 1998, Commonwealth Agencies, which includes the Department of General Services, have been, under certain circumstances, statutorily authorized to procure goods and services by way of competitive sealed proposals in lieu of competitive sealed bidding. Since being authorized to do so, state agencies have been involved in a myriad of court cases litigating the issues surrounding attempts to procure goods and services through the proposal process rather than sealed bidding. The Department of General Services has been brought into the litigation foray as a result of its initiation of Best Value Request for Proposals.

In 2005, DGS issued its "Best Value Policy" which authorized the use of RFP's to accomplish DGS' goals of improving upon timely delivery of quality multiple prime construction projects by qualified contractors. The RFP process was to be considered for complex projects with allocations exceeding $5,000,000. The policy statement also required that DGS' Deputy Secretary make a written determination that competitive sealed proposal process was either not practicable or not advantageous to the Commonwealth.

Best Value was designed to give the Commonwealth flexibility in contracting larger, more complex projects, but was also believed to give Best Value projects a better chance of avoiding the high level of claims that were common on DGS projects prior to the previous DGS administration. Architects and contractors favored Best Value because it offered an opportunity for selection based upon technical qualifications in concert with price. And the projects that have gone through the Best Value process have, for the most part, attracted contractors who had previously refrained from bidding DGS work.

The method also had its detractors, particularly from prime mechanical and electrical contractors with extensive DGS resumes, and from contractors who felt the standards were not consistently applied. From the earliest Best Value projects, lawsuits have followed.

Two recent Commonwealth Court cases have weighed in on DGS' methods of procurement involving Slippery Rock and Cheyney Universities. Of the two, Cheyney, decided in May of this year, came first and has persuasive weight – this means others potential litigants can reference it as decided law. While first initiated in 2005 because of appeals to the Supreme Court, it took nearly five years to run its course. The Slippery Rock case, decided in November of this year, was not reported and only applies to the parties involved. From a legal perspective, the Cheyney case is the Court's decision on the issues surrounding DGS' use of RFP's rather than bidding.

In both the Cheyney and Slippery Rock cases, the final decision focused on DGS' initial decision to use the RFP process and did not focus on the selection process. Both of these cases found that DGS did not sufficiently conclude that the normal bidding process was either not practical or not advantageous to the Commonwealth under the Procurement Code. Section 513(a) of the Procurement Code requires, "When the contracting officer determines in writing that the use of competitive sealed bidding is either not practicable or advantageous to the Commonwealth, a contract may be entered into by competitive sealed proposals."

The Court's looked at what level of particularity is needed when the contracting officer determines, in writing, that the competitive sealed bidding is either not practicable or advantageous. DGS, in its written determination to use the RFP process for the Cheyney project, stated:

The use of the standard competitive sealed bid process for the renovation of Foster Union would not be advantageous to the Commonwealth. Competitive sealed proposals are a more practical method of procurement since this will allow Proposers flexibility in developing their proposals to address their experience with this type of work and the ability to complete coordinated construction in a timely manner. In addition to expediting the process, this method will be more advantageous by allowing the Commonwealth the ability to consider criteria other than cost in the award process. The prime contracts to be awarded, if any, will be agreed-upon lump sum awards reflecting the costs submitted in the proposals.

Finding that the proposed construction was not unique and that any contractor was always obligated to coordinate its work with other contractors and timely complete its work, the Court found that DGS did not provide enough specificity for finding impracticability or disadvantageous. On the Slippery Rock project, DGS' determination stated:

The complexity of the project, the difficulties of the site, the tightness of the construction schedule, and the requirement to have the building LEED certified make the cooperation and coordination of the prime contractors essential to the success of the project.

I certify that the use of competitive sealed bidding for this construction project is either not practicable or advantageous to the University.

The Slippery Rock Court, heavily relying on the reasoning in the Cheyney again found that DGS' underlying reasoning that competitive sealed bidding was not practicable and not advantageous contained no basis for the Court to review the complexity or difficulties of the site. While the Court did grasp on the LEED nature of the project, it concluded that there was no reasoning why seeking LEED certification would preclude competitive sealed bidding.

While the above cases do reveal that in order for DGS to utilize the RFP process on construction projects the written determination must be specific and state with particularity the reasons that bidding is not "practical" or is not "advantageous" they provide little more guidance on the issue other than this general proclamation. What can be determined is that such impracticability and/or disadvantage will need to be more than just general project conditions that make construction difficult. Based on DGS' posted Best Value documents on its web-site, they have developed a determination matrix listing various job conditions to consider when making the decision to utilize the RFP process rather than bidding. From this writers experience, none of the considerations listed are considerations that have not otherwise been addressed on a previously bid project. This begs the question, that if the conditions have been successfully dealt with on a bid project, would a repeat of those conditions justify utilization of the RFP process? For example one of the considerations is a prison project. Has DGS previously bid and successfully completed a prison project? Why would this now be a basis for determining that bidding a prison is impractical? It will be more likely that an agency will conclude that the bidding process is not advantageous rather than not practical. "Advantageous" appears to be a subjective criteria that will allow the agency great latitude in its determination, rather than an objective standard with established criteria.

Although this article focuses on DGS, as a result of the recent cases, it would equally apply to other Commonwealth Agencies that have the ability to invoke section 513 of the Procurement Code. Additionally, while some may try and raise the issue of the Separations Act, the requirement of entering into separate contracts for general, mechanical, electrical and plumbing contracts, that issue has been resolved by the Cheyney case. On appeal of the initial decision of the Commonwealth Court, the Supreme Court did decide that if the RFP process is properly utilized, the Separations Act is not applicable to the RFP process. It is interesting to note that the Court's decision was accompanied by two dissenting opinions that reached different conclusions.

While there are no clear answers on DGS' use of the Best Value RFP process in construction, there will be more litigation on a case by case basis to ferret out the details on when bidding a construction project is not practical or not advantageous to DGS.

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Claims Avoidance as Means and Methods

By Andrew Rhodes & Jeff Burd

More successful and profitable contractors are typically the ones who evaluate various means and methods for a project in order to identify ways they can build the job in a more timely and efficient manner. For a contractor, a creative or innovative plan for delivering the project can mean success in landing the job, and it certainly can improve a project's profitability.

Particularly in a competitive construction environment, contractors and owners will do better if they also develop effective means and methods for identifying and addressing cost overruns and the handling of related disputes, if any.

Just to be clear, the subject here isn't making claims a part of means and methods. Instead, the focus is on establishing means and methods that enable a contractor to identify and address cost overruns as early as possible and to avoid, if possible, the litigation of claims after a project is completed.

Claims for compensation, whether they are for delays or change orders, arise from misunderstandings or misinterpretations (unintentional or otherwise) of the project scope. Most often this results from construction documents that are unclear or don't completely represent the owner's intention for the project. Blame for this can be shared among all parties to a design. While there are many roads that lead to poor documentation of the project intent but they all lead to the same place: a project with conflicts waiting to happen.

The byproduct of a robust bidding period and scope review is the identification of areas of project scope that could be disputed during construction. Estimators learn where the contradictory plan and spec instructions are. Scope reviews yield a sense of which subcontractor may be planning to execute differently than the design seems to intend. And the early submittals reveal clear differences in interpretation. Once these issues come to light, each day that passes without resolution increases the potential cost.

Owners, designers and contractors would be well-served to resist the human impulse to avoid confrontation in the hope that the problem won't materialize. Each party needs to recognize his or her stake in seeing that potential disputes are resolved systematically in advance of construction.

A generation ago the market dynamics were very different. Competitive pressures were less and contractors and subcontractors generally priced a project with allowances for the uncertainties built into the bid. When construction documents were unclear or contradictory, experienced estimators could figure the project based on what they knew was the proper or accepted method of construction. For the most part, contractors could count on the same being true of their competitors. Contractors viewed the risk of losing the job as being less than that of getting a project that had problems going in.

As an example, a contractor pricing the construction of a canopy that wasn't properly detailed felt an obligation to estimate that portion of the work by anticipating the costs of correctly building that portion of the project, or at least felt obliged to request more information about how the canopy was to be built. If the assembly method estimated by the contractor wasn't one that could be approved by the architect or owner, there was enough relationship capital between the parties to allow for 'horse trading' so that no one lost any money solving the problem.

The competitiveness of the market means that it's tougher to horse trade than it used to be. Owners often want the lowest price possible and in a low bid environment unclear details will often get priced with the cheapest solutions instead of the best.

Another reality is that a new generation of project managers for owners, contractors and designers is now taking charge, and it's a generation that hasn't experienced the benefits of solutions that start with "I know what the specs say but…"

Even in hypercompetitive environments, however, a construction project is still like a marriage in that the negotiation of differences is easiest during the honeymoon period. Early in the project all parties still have relationships from which to draw capital and disputes can be corrected before they are put in place.

A current local private-sector project is a great example of how to use the 'honeymoon' to manage a potential claim. The project involves the use of micro-piles in new construction and as part of the submittal process the contractor was obliged to verify the actual location of the piles in comparison to the theoretical locations shown on the foundation plan. The specs called for a report of any

Two hours of discomfort AVERTED DOZENS OF HOURS OF CLAIMS EXAMINATIONS ...

micro-piles which varied from the plan by more than a specific tolerance. The project manager for the engineer demonstrated some belligerence early in construction and demanded a schedule of the precise location of all micro-piles. The owner of the project had favorable past experience with the contractor and the owner of the contracting company felt the engineer was overreaching, particularly since this was one of several information requests that had slowed accelerated progress by the contractor. The contractor believed the engineer was simply behind on his submittal review and was creating distractions to slow construction.

How the next step unfolded could determine the course of the project. Acceding to the engineer's demand would have further eroded progress (which at one point was 30 days ahead of schedule), and may have cemented unreasonable expectations in his mind. Simply ignoring or refusing to honor the request would lead to denial of progress approvals and likely to a series of delay claims as the project proceeded. The contractor chose to use his relationship capital with the client, especially while he was performing ahead of expectations, to confront the engineer's expectations.

That strategy led to an uncomfortable meeting, but one in which the expectations of all parties were brought back in line with the construction documents and the owner's needs. Two hours of discomfort averted dozens of hours of claims examinations and potentially, thousands in legal fees.

While the contractor in this example chose to nip the problem in the bud, he also demonstrated a willingness to risk his relationship with the client to confront the client's engineer. That is one of two somewhat contradictory trends that have developed during the recent recession.

Contractors and architects who had a significant share of their workload in private projects have always understood that they would have to be flexible with their interpretation of the scope of work to keep the client happy. In good times, firms can price a certain amount of that expectation into their bidding. The return on that flexibility was some level of additional business advantage. Part and parcel to that understanding of flexibility was an equality of value in what was given and taken. You were asked to fix small oversights or omissions. That was how relationship capital was accumulated.

The new generation of owners has less experience with both sides of the give and take equation, and the severity of the recession removed the flexibility from contractors and designers. Owners who have had little or no experience with changes and claims are finding they are dealing with them regularly of late.

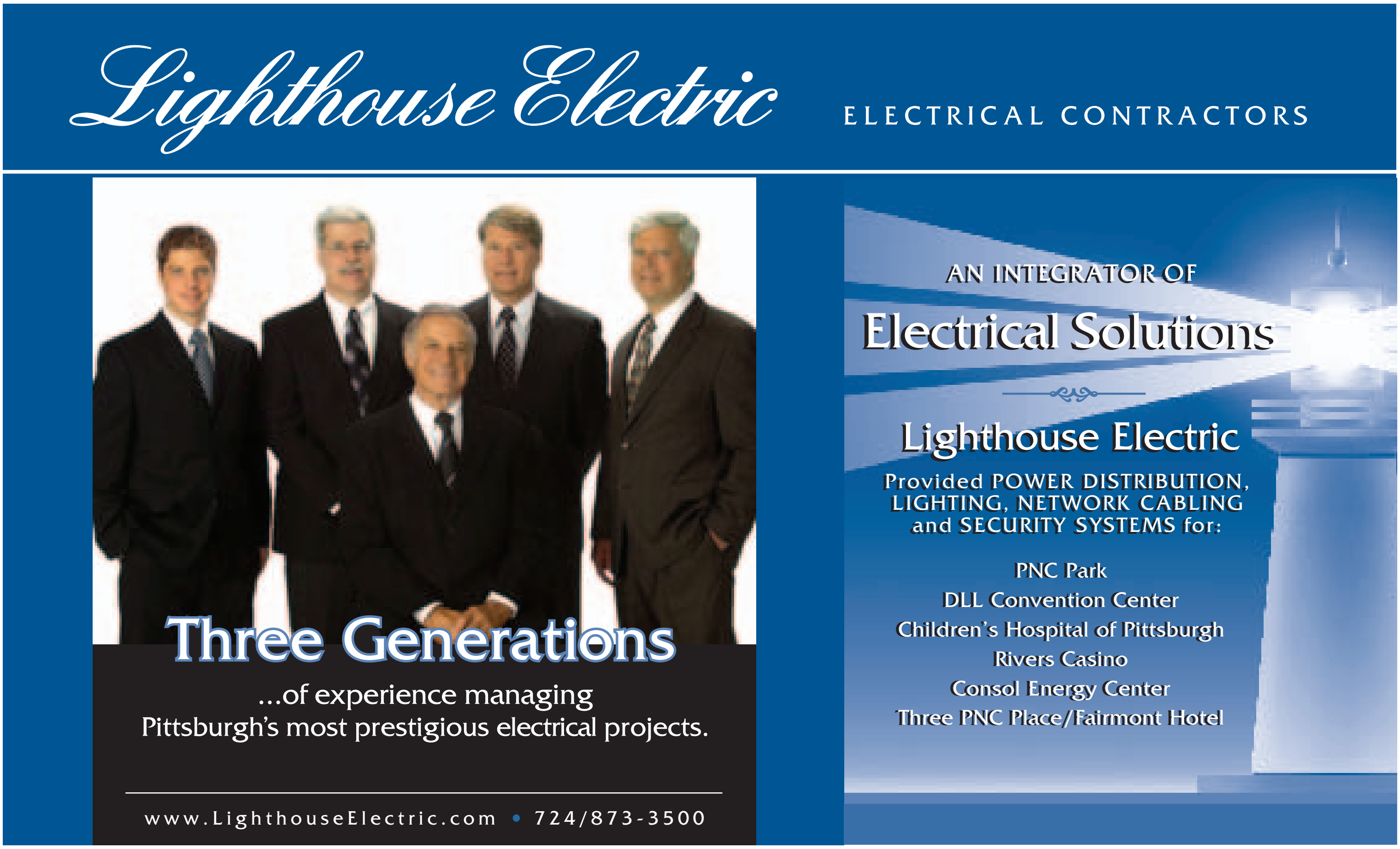
Another trend that is a departure from the norm is that the number of disputes going to litigation has declined during this recession. Tougher economic times yield more disputes because the tolerance for give-and-take goes away, as described above. There is less profit on a given project to cover little extras so disputes arise. To be sure the number of disputes has risen as expected, but it is the share of those disputes going to litigation that has not.

Typically, one aim of the claims consulting industry is to assist parties on construction projects with the avoidance or minimization of formal claims and costly litigation. To this end, the claims consulting industry can serve to educate contractors as to means and methods that will better equip parties to the early identification of impacts and cost overruns and the active and immediate management of the related risks. While these efforts may seem counter to the claims industry's health, construction parties that are tuned into the advantages of avoiding prolonged and costly claims will likely be more willing to invest in efforts to manage risks and disputes during the project; which in turn, may result in long term, mutually beneficial relationships and the minimization of costly claims. Furthermore, the investment in a construction claims consultant during an active project will allow the owner and contractor personnel to focus on the completion of the project.

More time will need to pass before we can judge whether this latter trend is the residue of the claims industry's education or just a different response to a severe recession. Given that the claims consulting business is relatively young, there is hope that contractors and owners have begun to better appreciate and understand the value of early identification and active management of risks.

Good times will return to the construction industry – probably sooner than we think – and the good habits developed during lean times should remain in place.

Andrew Rhodes is co-founder and managing principal of The Duggan Rhodes Group, a consulting firm providing claims consulting services, dispute resolution and expert testimony services, CPM scheduling services, project control/risk management services and 3D / 4D modeling services. BG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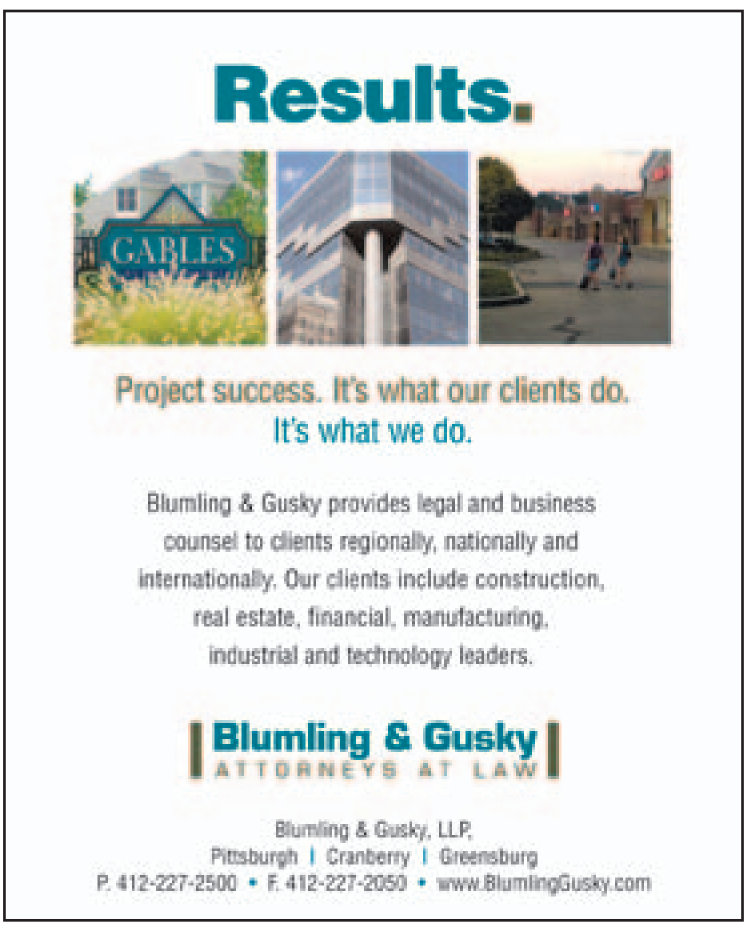
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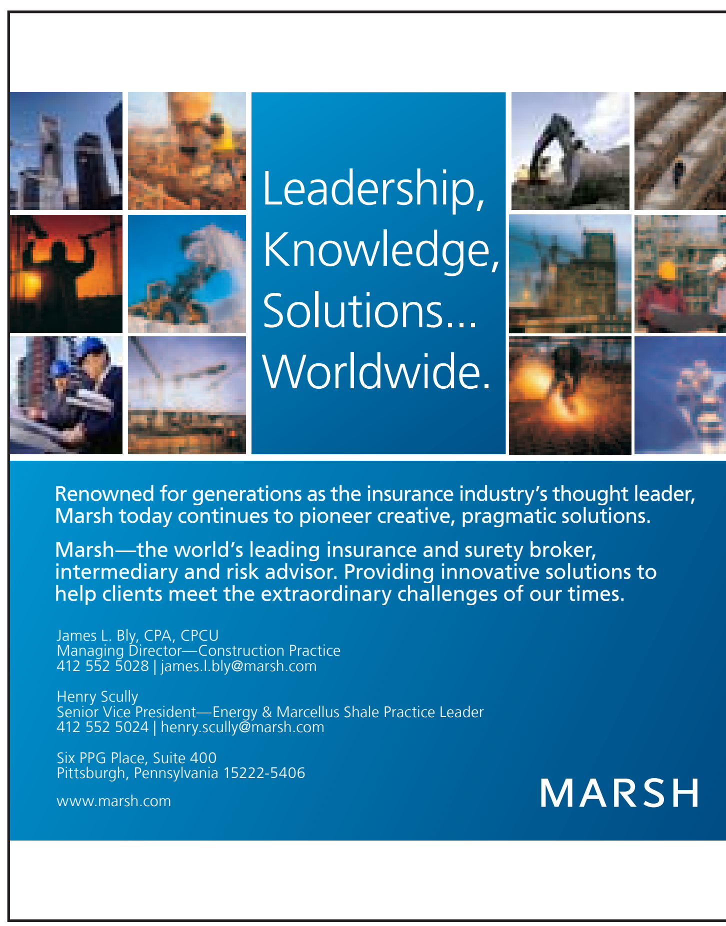
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Financial Perspective

The Financial Accounting Standards Board (FASB) has completed the comment period for its proposed changes to the generally accepted accounting practices (GAAP). The changes are part of an effort to bring U. S. and global accounting standards into alignment. During the next few quarters, FASB will attempt to incorporate the professional feedback and commentary received during the fourth quarter of 2010 and will hold a series of regional meetings in advance of its final determinations.

Three of the changes being proposed could have significant impact on construction and real estate. As reported in the November/December edition of *BreakingGround*, the revisions proposed to leasehold accounting are attempting to more clearly report the potential liability and gains that a commercial lease represents to a business, but the changes could have negative effects on liquidity and debt-to-equity ratios.

Another aspect of the FASB proposed changes is in requirements for the reporting of potential liabilities for withdrawal from multi-employer pension plans. This change will impact how firms with union or association agreements account for withdrawal obligations, regardless of whether or not they have any intention of withdrawal. This facet of the proposed standards will be detailed in the March/April *BreakingGround*.

The third significant proposed change is in revenue recognition. In June 2010, FASB issued an exposure draft on revenue recognition, titled "Revenue from Contracts with Customers." Revenue recognition has been a target for FASB and the International Accounting Standards Board (IASB) in recent years. The current recommendations attempt to clarify the principles for recognizing revenue and develop a common revenue standard for GAAP and international standards.

The guiding principle is the recognition of revenue and profit in a manner that matches consideration to the amount of goods or services transferred over a specific period of time.

"Mainly it's an ownership issue," says Debra Pitschman, partner at Case Sabatini. "The new guidance is meant to recognize when the ownership of a contracted item is released to the owner. For construction, the asset – the construction project – transfers ownership by percentage of completion. A change to that could impact contractors and project owners."

To apply the proposed revenue recognition principle the following five steps are required:

- Identify the contract with a customer
- Identify the separate performance obligations in the contract
- Determine the transaction price
- Allocate the transaction price to the separate performance obligations
- Recognize revenue when the entity satisfies each performance obligation

The new guidance works well for manufacturing contracts, for example, where the specific performance obligation is an aggregation of a number of completed units, say 100 safety vests from an overall contract for 1,000. They can also be applied reasonably to services that are typically delivered with specific completed milestones, like a completed schematic design. Where the new guidance goes astray are contracts that measure progress as a percentage of completion, like construction projects.

"It's possible to identify separate performance obligations in a bigger project, if a contractor who performs big components of a project can break those into smaller obligations," says Dick Spence, partner at Hill Barth & King. "But even if you can separate contracts like paving or earthwork so that percentage of completion isn't relevant, there may be very different recognized profits for each obligation."

Because the winning bid for a project is not only an estimate of the cost of building the project but also a successful judgment of the competitive environment on bid day, the various subcomponents of a contract will include prices that reflect different pricing pressures from one to another, and also different levels of profitability from trade to trade.

"Where I have a concern is in the need to break contracts down into multiple performance obligations," says Schneider Downs principal Eugene DeFrank. "You essentially have to break it down into separate contracts within the contract. That means coming up with a separate estimate for each performance obligation that is created and those individual estimates will have different gross margins from the overall margin."

Because the new method relies just as heavily on estimates as any previous method for recognizing partial completion of a project, estimates of separate performance obligations will have the same individuality as the current progress payment estimate does. Since the proposed revenue recognition is principal-based rather than guided by specific rules, a greater level of subjectivity is likely in allocating costs, like overhead and general conditions, that are not inherent to any separate performance obligation. More important is the fact that the estimates done to win the contract will not be segregated in the same manner as the specific performance obligations will be. That allows for more interpretation rather than less, a result that is not in keeping with the goals behind changing the guidance in the first place.

One of the main concerns of auditors of construction firms is cost shifting, taking losses from one project and applying them to a more profitable project. In the end, the contractor will end up with the same amount of profit, regardless of how it's allocated, but the cost shifting can mask problems the company is experiencing. And that's a concern for one of the biggest readers of contractor's financial statements, the surety companies.

Surety companies rely on their analysis of a contractor's financial condition to determine how well the firm is doing at managing its business. The potential outcomes of the new guidance are making the surety business very uncomfortable.

"The sureties are very comfortable with reporting based on a percentage of completion paid as part of a construction contract," explains Seubert & Associates partner Jay Black. "Our work in progress reports include reports on job progress and the anticipated profit as the project moves along. It's vital to our judgment of a contractor's operation to be able to track his jobs and see if the profits erode. The work in progress sheet is simple – one line per project. If this goes through there may have to be 30 lines per project."

The attraction of the current accounting standards for percentage of completion is its simplicity. Surety companies are assessing risk by examining a contractor's capacity and character in addition to its financial condition, so maintaining the status quo isn't merely a case of resistance to change; it's a matter of keeping a simple and effective tool simple.

"A big part of underwriting bonds is looking over time at a contractor's estimates of profit margins at the beginning and end of a job," agrees Jim Bly, vice president at Marsh. "We develop a model using the statistical analysis of the contractor's actual history of profit projections and use that to look at his work in progress, what his P & L statement and balance sheet is saying, and compare that to what he says is coming from the balance of his work in progress."

Bly says that underwriters are always concerned about overstated profits, particularly overstated profit projections early in the job. What the sureties worry about is not that all contractors are overstating their profits, but that

contractors who are experiencing losses during a project will seek to recognize those losses as late as possible. And the additional subjectivity in the proposed revenue recognition guidance will make it easier to produce more favorable estimates of profit.

For all the concern about the changing guidance it's important to remember that only an exposure draft has been released and received comment. The adoption of new standards isn't expected until the second half of 2011 and most of the local professionals expect significant modification.

"My opinion is that the surety companies reported to FASB that they are happy with current revenue recognition, and that will keep construction from being held to this," says DeFrank.

Dick Spence agrees. "The current method is so well understood. It's been used in the practice for 30 years or more," he says. "CFMA [Construction Financial Managers Association] has issued a strong comment and I feel that there will be an exclusion from the new guidelines for construction contracts."

As might be expected, the surety industry isn't taking a passive approach to the proposed guidance. "If the FASB revenue recognition changes are finalized as drafted, it would certainly have an adverse effect on sureties' ability to assess true profitability of an uncompleted construction project," says Huntington Insurance vice president Ryan Burke. "Hopefully FASB will determine that percentage of completion is the most prudent revenue recognition method for the construction industry. If not, the surety industry will face challenges in accurately evaluating a contractor's financial strength, which is largely determined by work in progress."

"What will ultimately happen if the new method is forced upon us is that surety companies will still require a separate schedule that reports percentage of completion," says Jay Black "That will require more work for our customers but I don't see trying to adapt to a new accounting method."

HNMS Inc.

Eric Roberson

Eric Roberson is like many entrepreneurs in that he's surprised by the path that has taken him to a decade of operating a successful window treatment business. While he may be uncertain as to how he got here, he's sure it wasn't a lifelong desire. "I grew up on the west side of Chicago and you don't grow up in the projects of West Chicago thinking about a career in window blinds!"

Founded in 1999, HNMS Window Blinds is an installing distributor for blind manufacturers in Western PA. Not only has he adapted his plans to a career in the window treatment business, Roberson is also working to bring his corner of the construction industry into the 21st century. "I'm looking to begin fabricating as well as supplying blinds," he says. "Because I'm a vet there's a lot of opportunity with the work the VA is doing all over the country and I think there's an opportunity to automate our industry. We should be able to measure and order [components] digitally and increase the accuracy of the fabrication and installation."

When he founded HNMS, Roberson was interested in automating another industry. Roberson's eight years in the Marine Corps and a stint in healthcare doing purchasing and procurement gave him administrative skills that he could envision being valuable across the expanding healthcare industry. It was his misfortune that he wasn't the only one with that vision.

"The company was called Health Network Management Services at the time and I intended to do purchasing and procurement consulting and be an outside resource for that industry," he explains. "I had begun calling on doctors and nursing homes to talk about providing purchasing services but I got shortcutted by UPMC when they started doing that."

The setback didn't dampen Roberson's desire to create his own business and he followed up on a chance to get into the business of cleaning, installing and maintaining window blinds. The new business allowed Roberson to continue developing his existing relationships within the healthcare institutional market and to expand into commercial facilities. Like many minority or women business owners, he underestimated the effort needed to complete the minority business certification process and may have overestimated the benefits of the certification initially. As an MBE-certified contractor and a service-disabled veteran, Roberson knew that he would have opportunities but couldn't anticipate the trade-off.

"It was a lot easier for me to join the Corps and sign my life away than to prove I was a minority," he laughs. "What I wasn't prepared for was how much time I would spend making sure that I'm continuing to be certified. When I look back at all my sales, maybe 30% of the work came from the certification." Roberson doesn't minimize the value of the 30% of his volume but feels that the time invested hurt his ability to hustle. "In the end, I should be spending my time chasing business, calling on the contractors to find out what they are bidding, making sure that I'm doing what I can to be competitive. At the end of the day your number is still your number."

Roberson cites the example of his biggest sale to date, the recently completed 3 PNC Plaza. "We were very happy to get the opportunity to do 3 PNC but it took more than two years of hustling to get there," he says. "I know the people at PJ Dick were skeptical at first because of our small size but I made sure they knew we could handle it. The contractor needed to see samples of what was being installed and I offered to set budgets for the blinds while they were being planned."

HNMS QUICKLY OPENED CHANNELS UP TO MANUFACTURERS DIRECTLY AND OPERATED AS A DISTRIBUTOR SINCE THEN.

That project was something of a next step for HNMS, which has in past had smaller contracts on big projects like the Hillman Cancer Center, CAPA High School, EQT and the DelMonte Center. HNMS had some early successes maintaining blinds for building managers and parlayed that into new construction as a first big step up in volume.

"Our first new construction project was the FBI Building that Oxford Development did on the South Side," Roberson remembers. "George Whalen [of Oxford] referred us to Rycon Construction, who gave us a chance to do the project. I was green enough not to know where to buy the blinds and got them from a competitor. They stuck us pretty good on the price and I learned a hard lesson. These days I think I've become a headache for that competitor." HNMS quickly opened channels up to manufacturers directly and operated as a distributor since then.

Roberson has worked exclusively as a distributor because of concerns about not growing his overhead excessively, but he is re-thinking his business model. One big missed opportunity continues to nag at Eric Roberson and has him making plans for fabricating blinds.

"I was at an MBE conference in Las Vegas when I was a distributor for Draper, who made an insulated shade that was perfect for the Sunbelt," he says. "The CEO of MGM was at the building and at one point approached me and started a conversation. He asked what I did and I started talking to him about the concept of automated window shades for his hotels. I was going on about how the shades would open and close automatically as the rooms were occupied and how much money it would save in air-conditioning and the next thing I knew I was sitting there with the head of design for MGM. They were pretty sold on the idea but when I took it back to Draper, they didn't want to produce it."

While the chance to supply automated energy-saving blinds to the Las Vegas hotel market has come and gone (for a while at least), Roberson looks forward to growing HNMS's business again by fabricating as well as supplying window blinds. By fabricating, HNMS can become the single value-added step between the manufacturer and the end user. And Roberson's veteran status can bring opportunities beyond his installation area by teaming with local installers on VA projects where no veteran-owned competitors exist.

"I'm scouting manufacturers now to find the right fit to set up a fabrication operation," he says. "If we can make it work I'd like to build a shop on the North Side to employ workers from the local neighborhood." BG

Company Facts

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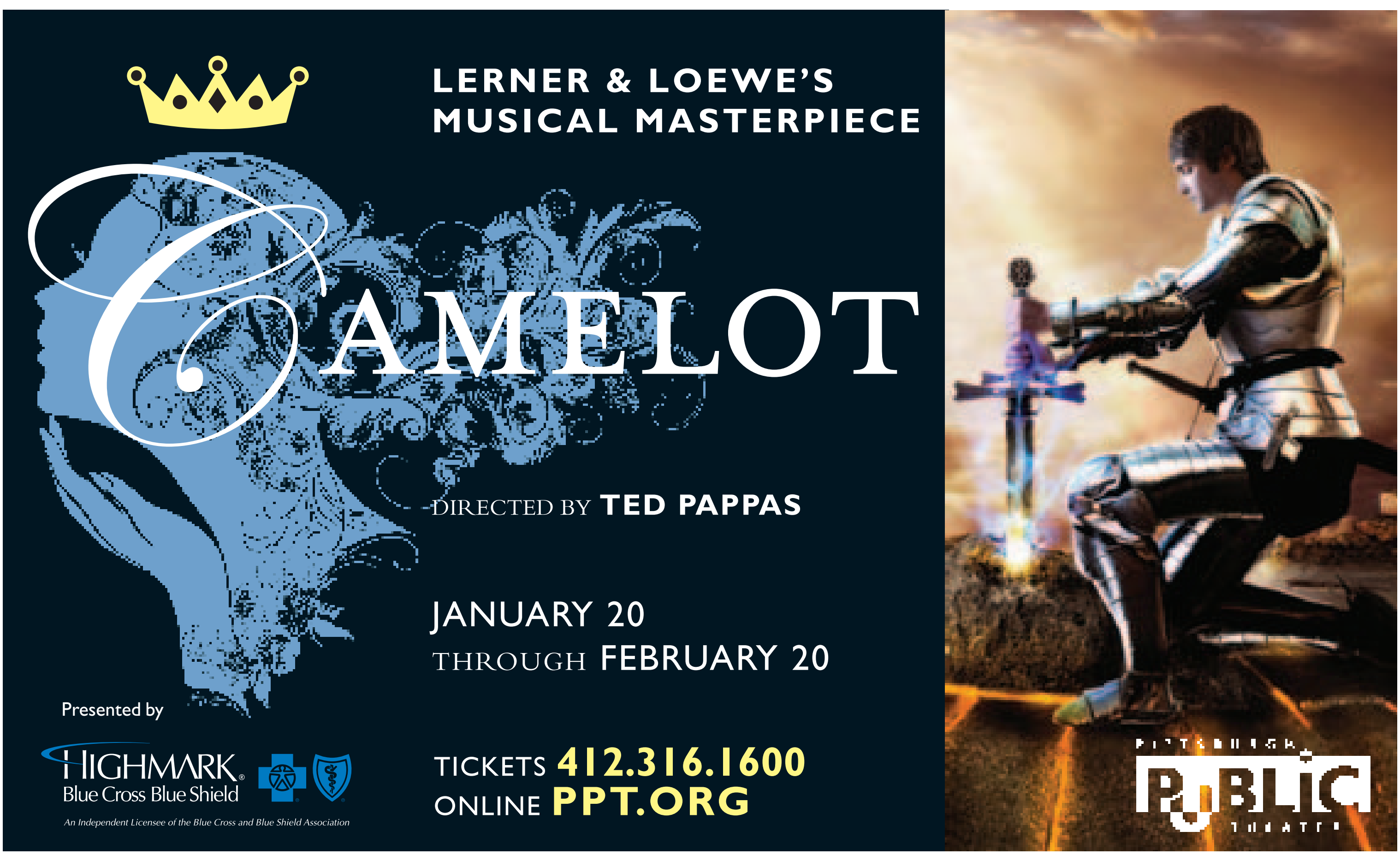

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Trend to Watch

Pension Distress is Real

The December 19 episode of 60 Minutes included a very sobering look at the growing budget crises in the state houses across the country. Correspondent Jeff Kropf interviewed a number of government and financial experts who detailed some of the worst of the state deficits. The dramatic drop in revenues that resulted from the recession and financial crisis was coupled with a continued increase in spending in many states, leaving almost every state with a deficit of some size. The upside of the report, if you can find one, is that the day of reckoning has arrived for most governments; and the report itself seems to have awakened millions of voters to the magnitude of the problem.

The CBS report may have awakened viewers to the budget problems, but they were hardly an unknown. What the report gave only brief mention of was an equally serious problem with unfunded pension plans that could hinder public capital plans for a generation. In Pittsburgh, the issue of an underfunded pension plan is not a secret, yet for the weekly headlines few residents of the city or state really comprehend the causes and potential effects of the problem.

First it's important to understand that the problem of inadequately funding public pension funds has been with us for more than a generation. In fact, the underfunding was not confined to public pensions; however the private sector had the opportunity to alter – or in many cases – eliminate its pension plans when they became economically unfeasible. Private pension plans also operate under the governance of the Employee Retirement Income Security Act of 1974 (ERISA), which established the Pension Benefit Guarantee Corp. (PBGC). PBGC is an insurance backstop that pays the pension obligations of failed companies out of premiums paid in by all current pension plan sponsors.

For taxpayers the problem is that the state and municipal government pension plans fall outside the purview of ERISA and have been surprisingly unregulated. In Pennsylvania there was no organized system for contributing to pension funds or mandated accountability for municipal pension funding. In a number of municipalities, pension obligations were being paid out of current operating funds. It was this chaotic situation that Act 205 was designed to remedy when it was passed by the Legislature in 1984. Act 205 set up the administration of pensions so that there was tracking of assets and performance, transparent reporting of current and forecasted obligations, mandated minimum contributions and a state-level funding mechanism to help close municipal funding gaps. For a couple of decades the funding gap slowly declined.

"The problem with Act 205 was that it didn't require that municipalities create workable plans for getting caught up to their obligations," says Brian Jensen, executive director of the PA Economy League. "Worse yet, it provided more funding to the municipalities that had the most trouble. Those who managed their pensions badly were rewarded."

Jensen says that while the recent recession had deepened the gap in funding, the problem had been brewing ever since Act 205 was passed. While the law established reporting standards it didn't prevent politicians from altering assumptions or smoothing losses like the devastating pop from the dot com bubble in 2003. "Harrisburg has known for a while that this was coming but minimized the pending problem," he says. "Politicians have chosen to kick this down the road to the next group for some time."

Cranberry Township's manager, Jerry Andree, says political moves are how the pension plans always got in trouble.

"I've been watching this happen for over 30 years and my experience is that people tinker with [pension plans] to make them say whatever they want," he says. "You can alter the actuarial assumptions, reduce the estimates of salary increases or overestimate the rates of return to make the current position look better than it is. Public policy always seems to push the problem off to the next administration."

The calculation for pension plan management is complicated to understand but very straight forward in principle. The most complicated parts are the actuarial assumptions for the plan participants – both current employees and retirees. Once the assumptions about mortality of the participants are figured the fund manager factors in the estimates of the effective salaries of the participants at retirement and the return on the investments over the plan's lifetime to reach conclusions about how much must be in the system to fund the estimated obligations. Even minor adjustments to any of the factors influencing the funding calculations – even if they are totally artificial – can produce very different results.

Several key miscalculations (or calculated misrepresentations, depending on your viewpoint) have brought the system to the verge of a perfect storm. At one time or another over the past couple of decades all of the following have caused dramatic pension plan shortfalls. Underestimating the percentage of salary increases has created a significant gap between the actual pension base of retiring workers and the one used to calculate obligations. Overestimating the interest rate and other investment returns also created a smaller fund balance from which to draw the underestimated obligations. Compounding these errors is the fact that the wrong assumptions also led to collecting lower contributions from employees than were needed to maintain appropriate balances. Throw these fiscal problems into the backdrop of the dot com bust, the 1994 derivatives scandal in Orange County, CA (yes, Pennsylvania funds had some of those investments as well), extended low Treasury rates and the financial crisis of 2008 and you get, well, the perfect storm.

Doubtless any number of politicians and government managers passed the problems along intentionally to perpetuate their own jobs over the years; however, the majority of the mistakes were made by people who didn't understand the complexity of the problem or the ramifications of putting the problem off.

"Pension planning is complicated and most officials don't know how to do it. They hire Uncle Buck who handles insurance in their town," explains Andree. "Any financial planner will tell you that most people avoid financial planning in general and managing a municipal pension is really just financial planning."

Here's why decades of avoidance now matters. According to the Economy League, Pennsylvania has 25 percent of all the municipal pension plans in the nation. Some 40 percent of those municipalities operated in 'financial distress' in 2009. As of the current date, those plans are a combined $7 billion underfunded, based on current estimates of their obligations.

The $700 million in unfunded obligations that have garnered the media coverage of the City of Pittsburgh are a major crisis; however they pale in comparison to Philadelphia's $4.9 billion. The balance of the Commonwealth's hundreds of smaller municipalities has $1.4 billion in unfunded obligations. None of these shortfalls accounts for any of the state's obligations. As the largest generation of Pennsylvanians prepares to join an already disproportionately large percentage of retired citizens, the shortfall in funding is about to spill into current operating funds to meet pension payments. That impending reality will mean reduced services and higher taxes. Government reinvestment in capital construction projects will shrink to the bare minimum.

For most Pennsylvanians the breadth of this problem is blissfully unknown. When the effects of pension distress reach the average resident the solution will be painful. There is no silver bullet.

"The pension problem is a two-sided equation and the only way to solve it is by fixing both the asset and liability problems," explains Elliot N. Dinkin, president and CEO of Cowden Associates Inc., a Pittsburgh benefits and actuarial consultant. "The asset base has to be grown but the crisis can't be managed without attacking the growth of the liability side of the equation."

The kinds of solutions that Dinkins references have negative political ramifications, which is why they have not been implemented sooner. One obvious solution is to use the private sector approach and move from defined benefit plans to defined contribution plans. Another is to adjust the salary basis for defined benefits to something less than the retiree's highest compensation. Dinkins suggests something tied to the funding level of the individual plan, a solution that freezes the liability when funding falls below a specific level. For example, current employees would hold at their current accrued benefit levels until funding in the plan rose above 50 percent or another agreed upon level that permitted sustainable future funding. That would at least keep the accrued obligation from growing.

Another more radical solution is to alter the benefits of those already retired or those currently working under negotiated contracts. It is an article of faith that these negotiated public employee agreements are lifetime guarantees, but none have ever been challenged in court.

Of course, none of these solutions will be acceptable to the constituents of the pension plans, which means that elected or appointed officials who press them can expect to have active opposition to their continued employment or reelection. What will be required is an aggressive solicitor willing to challenge a contract or a responsible legislature willing to risk an election. The problem could receive big relief if the Commonwealth were to enact some enabling legislation that permitted local officials to attack the problem, but legislators have shown the least will over the years to put their positions in jeopardy.

The problem's status as we begin 2011 isn't improving, however, and the option of kicking the problem to the future is close to being gone. Pension distress is like a game of musical chairs for the current legislature and the record is nearing the end. Brian Jensen knows the cost of inaction will be billions in new taxes and service reductions, and is as cynical as most residents about the prospects for change. The Economy League has proposed tough measures to the General Assembly to deal with the issue and Jensen watched them discard almost all of the significant measures in a 2009 attempt to reform pensions. Still, he sees some hope in the elections that put Tom Corbett in the governor's mansion.

"The outcry is getting to the point where the legislature is starting to get it," he says. "They get that this can't be pushed down to the local level. There's no money there and they know that the state doesn't have any money either. The new administration seems like they may have the will to address the problem." BG

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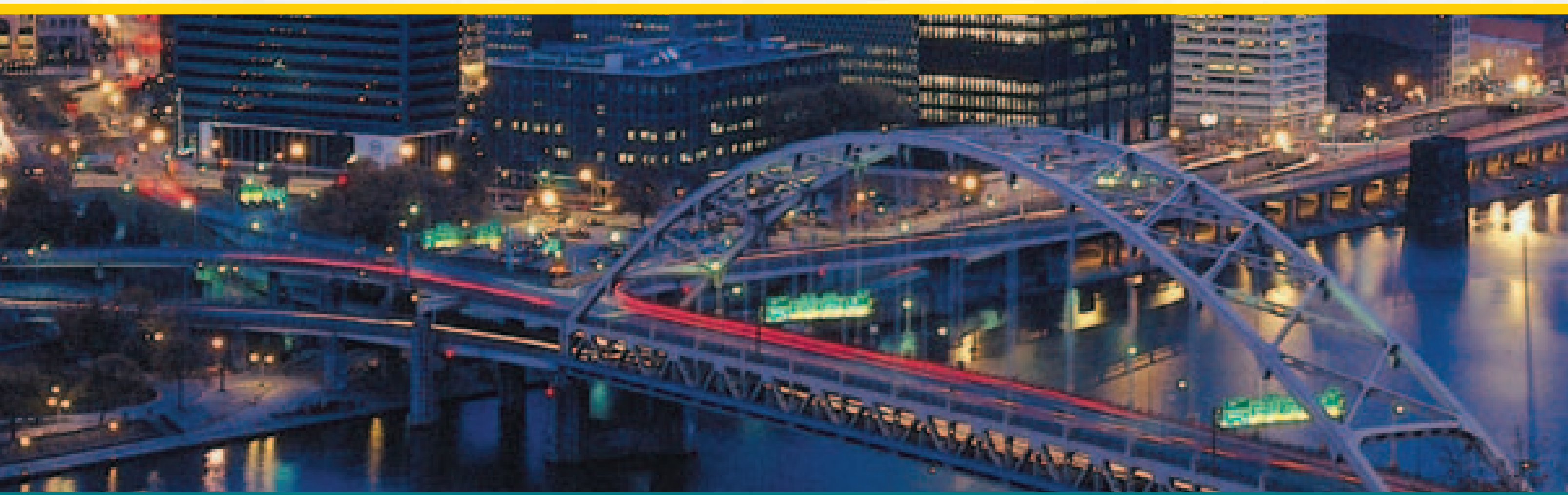

INDUSTRY & COMMUNITY NEWS

Young Constructors Benefit Casey's Clubhouse

The MBA's Young Constructors and local U. S. Marines held the fifth holiday event to raise money and gifts for children in need at the Hofbrauhaus at the South Side Works on Dec. 9. This year, in addition to the donation of more than 200 gifts for Toys for Tots, the YC event raised $5,000 to donate to Casey's Clubhouse, which is raising money to build a Miracle Field in Upper St. Clair for special needs children. Casey's Clubhouse is the foundation started by former Pirate and Upper St. Clair native Sean Casey and his wife Mandi. Construction of the $1 million field should take place in summer 2011. To learn more about the Miracle Field and donate go to www.caseysclubhouse.org.

Members of the Young Constructors, along with USMC representatives, present the $5,000 check to Casey's Clubhouse. Intermingled among the Marines & Hofrauhaus staff are (from left) Kevin McQuillan of The McQuillan Group, Dustin Giffin of Giffin Interiors, Gateway Engineer's Tom Turner, YC chair Brett Pitcairn of PJ Dick, Nello's Gino Torriero and TEDCO's Dan Bell.

Among the supporters at the YC holiday event at the Hofbrauhaus are TEDCO president Jim Frantz (left), Alpern Rosenthal's Tom Menk and TEDCO's Todd Anderson (right).

Duggan-Rhodes Shops for Gwen's Girls

On Friday, December 10th, members of The Duggan Rhodes Group (DRG) filled the Toys for Tots wish list for Gwen's Girls, a Pittsburgh-based organization whose mission is to empower girls, ages 8 to 18, to have productive futures through holistic, gender-specific programs, education and experiences. DRG's third annual Toys for Tots day of service, organized through its partnership with Pittsburgh Cares, began with a "shopping" trip at the Toys for Tots warehouse, run by the U.S. Marine Corps Reserve. DRG staff selected age appropriate gifts for the children on the Gwen's Girls wish list, many of whom are part of the agency's foster child program. To learn more about Gwen's Girls, visit www.gwensgirls.org. To find your local Toys for Tots donation center, visit the Marine Toys for Tots Foundation at www.toysfortots.org.

Seubert Serves Soldiers

Employees of Seubert & Associates got into the swing of the holidays and patriotism at the same time. A simple idea for each employee to bring in one useful item that could be sent to the son of one of their clients serving in Afghanistan quickly became a "Seubert for Soldiers" Project. The employees brought in enough food, toiletries, batteries and other goods that the soldiers found in short supply to fill 39 large boxes.

Uhl Marks 90th Anniversary with 90 Gifts

Uhl Construction Company marked its 90th anniversary by donating 90 poinsettia plants to St. Barnabas' two assisted living centers, located in Gibsonia and Valencia. The 90 plants were hand delivered to each patient on Friday, December 17.

"We want to say thank you to our community for nine decades of doing business with us and helping us grow," said James Hengelsberg, president of Uhl Construction. "This time of the year can be an especially joyous one for many people, but it can also be a lonely experience for others." Hengelsberg said the employees at Uhl decided the poinsettias would brighten the holidays for a large number of patients, while marking the number of years in business by donating 90 plants.

Massaro Helps Hill House

In October, 29 Massaro employees participated in the Hill House Association Day of Service. The group cleaned the nursery and its toys, painted the Blakey Center and planted several trees and scrubs for the Cliff Side Park block group association and the "Village in the Woods" project for the Hill House.

Massaro supplied cleaning materials and other needed tools and materials and also went around to local businesses and solicited donations of trees and shrubs to be planted at Cliff Side Park- over 40 scrubs trees. Their donations helped transform this space in a matter of hours.

Pictured: (L to R) Brian Miller, Terry Baltimore of the Hill House Association, Greg Jack, Brad Brock, Chad Salerno, Jeremy Bowlby, Brian Syska, David Rothert, Adam DiMenno, George Germany, Mike Yohe, Nick Depperman, a member of the community, Bruce Fox and Kevin Nestor. Not pictured but also attended the day of service from Massaro: Pat Stone, Chuck Crawford, Della Miller, Alyssa Kuhns, Mark Hartman, John Kristof, Jessica Bennett, Jason Adams, Anthony Pokusa, Ryan Haught, Jason Sigal, Hilary Brown, Linda Massaro and Rob Chambers.

Mascaro Tends Bar for CF

On November 18, 2010, Mascaro held its third annual "Get Together with a Cause" at McFaddens on the North Shore. Nate Martin and John Mascaro Jr. were the celebrity bartenders and all tips benefitted the Cystic Fibrosis Foundation. The grand tally for the night including tips, Chinese auction, silent auction, and 50/50 raffle was over $6,200.

Carpenters' executive secretary Bill Waterkotte, Elmhurst Group's Bill Hunt and Tad Imbrie of PenTrust Real Estate Advisory Services.

GREEN BUILDING NEWS

GSA Raises Standard to LEED Gold

The U.S. General Services Administration (GSA) is upgrading the requirement for new federal building construction from LEED Silver to LEED Gold certification. The new requirement will also apply to substantial renovation projects. GSA administers more than 361 million square feet of space in 9,600 federally owned and leased facilities.

Dave French (left) and John Skorupan (right) from L. Robert Kimball & Associates flank Mike Belsky of Columbia Gas at NAIOP Pittsburgh's Night at the Fights.

Army Adopts New Sustainability Policies

The U.S. Army issued two new policy memorandums on October 27, one to improve its high-performance green building standards and another to require light bulbs such as compact fluorescent lamps that are more efficient than standard bulbs. Both measures are designed to increase energy security, energy efficiency, and sustainability for the Army. BG

Michael Morris (left) of Sampson Morris with Genesis Partners' Mark Dellanna.

AWARDS & CONTRACTS

Volpatt Construction Co. was the successful contractor on St. Clair Memorial Hospital's $600,000 renovation of the fourth floor of the 733 Washington Road medical office building in Mount Lebanon. Image Associates is the architect for the project.

Southwood Hospital awarded a contract to Volpatt Construction for renovations to its administrative offices at its Boyce Road facility in Upper St. Clair.

Rycon Construction, Inc. was the successful contractor on the $7.5 million general trades package for the 27 month, renovation to University of Pittsburgh's Benedum Hall. The project was designed by Edge Studio.

Thermo-Fisher Scientific is planning to move into the old Dick's Sporting Goods Headquarters and has recently chosen Rycon Construction, Inc. to renovate their space. Strada Architecture designed the 190,000 square foot remodel.

At the University of Rochester, Rycon Construction will start work on a 20,000 SF renovation to Danforth Dining Hall starting in May.

Rycon Special Projects Group is currently renovating the 2nd & 3rd floor of Craig Hall at the University of Pittsburgh. This $750,000 project involves renovations to approximately 14,000 square feet.

A Giant Eagle GetGo store in Butler, PA is under construction by Rycon Special Projects Group. This project is scheduled for completion in mid-January.

A few other interior renovations being handled by Rycon Special Projects Group are PNC Bank Ellwood City branch, UPMC offices at USX Tower 56th Floor and Chick-fil-A restaurant at West Virginia University.

dck north america, a dck worldwide company, was awarded a renovation project at UPMC Falk Clinic. This project involves the renovation of a portion of the sixth floor at Falk Clinic Dermatology Department and will include a new laboratory, multiple exam rooms, and other necessary rooms to support the staff. Image Associates is the architect.

The Art Institute of Pittsburgh selected Poerio Incorporated as contractor for the renovations of 200 Display Showcases. The display cases were modernized so the contents are stored safely and the contents can be viewed easily by the public. Construction is to be completed in February 2011.

Poerio was the successful contractor for the Fed Ex Ground Hub Expansion in St Paul Minnesota. The $3.8 million construction project is to be completed in February 2011 and the architect on the job is Leo E. Daly. The project includes extensive site work improvements including 223 additional trailer parking spaces in an adjacent lot, additions to existing Fed Ex Hub, 3 new buildings, a New Gateway Building, New PD Garage and a New Truck Service Garage.

Poerio was the successful bidder for the University of Pittsburgh's 5th floor Cathedral of Learning Colloquium Room. The 2500 square foot renovation of offices and study areas is slated for completion in January 2011. Pfaffmann & Associates is the Architect on the project.

Poerio Incorporated was awarded a contract from JC Penney Department Store in Barboursville, WV. The project includes renovations of the entire sales floor. The work includes updating all flooring, wall fixtures, ceilings, fitting rooms, and restrooms. In addition there will be improvements to Shoes, Catalog, Salon, Jewelry, Portrait Studio, and an addition of a New Sephora makeup division. The project is tentatively scheduled for completion in 22 weeks. KA Architect is the Architect on the job.

A. Martini & Co. was the successful contractor for Peoples Natural Gas's $400,000 renovation in the DelMonte Center on the North Shore. Next Architecture designed the project.

Mascaro Construction received a contract from Magee Women's Research Institute for the renovation of the fourth floor. Interior renovation to the 6,600 square feet includes significant upgrades to the mechanical and fire protection systems and renovation of lab spaces, offices, fume hood, medical gasses, and new finishes to the floors and ceilings. Astorino is the architect.

Mascaro is part of Capstone Development's design-build team to develop a four-story, 682-bed residence hall at Lock Haven University that will provide over 210,000 square feet of living space. STV is the architect. Design and construction is expected to take 24 months.

The Heinz Foundation awarded a contract to Mascaro for renovations to offices in the Heinz 57 Center. The Design Alliance is the architect for the project.

PJ Dick Inc. was the successful contractor on Duquesne University's new Des Places Residence Hall, a $25 million, twelve-story structure. WTW Architects is the architect for the 131,000 square foot building.

PNC Financial Services awarded Jendoco Construction Corporation a contract to renovate its Millvale Branch. Fukui Architects designed the 9,520 square foot project, which includes a new teller line, conference room, mechanical and electrical upgrades.

Jendoco Construction was the successful contractor on Western Pennsylvania Hospital's Variable Acuity Room Renovation. The project involves 1,620 square feet of renovations to patient rooms on the 9th floor of the hospital. IKM, Inc. is the architect.

Carnegie Mellon University selected Jendoco Construction for renovations to the Tepper School bathrooms. EDGE Studio is the architect for the project.

Jendoco Construction was awarded a contract for exterior renovations at Flexsys/Solutia, Inc. in Monongahela, PA. The project was designed by GAI Consulting.

Burchick Construction was awarded $17.6 million in contracts by the Dept. of General Services for general construction, structural steel and site work as part of the $32.7 million expansion of Salk Hall at the University of Pittsburgh. Ballinger is the architect for the project. PJ Dick is the construction manager.

Massaro Corporation was the successful general contractor on the new Penn Hills High School. This $38 million new construction project began in December of 2010 and will run through spring of 2013. The architect on the project is Architectural Innovations.

Phipps Conservatory and Botanical Gardens selected Landau Building Company to build a new elevator and elevated pedestrian walkway in the Rain Forest of the Phipps Center for Sustainable Landscape. The architect is The Design Alliance.

Landau Building Co. was awarded the contract for UPMC Shadyside Hospital, New Operating Room & PACU Renovation. Construction will begin mid Jan 2011. The project consists of a new clinical engineering laboratory and new operating room with special functions for a da Vinci Surgical Robot. The architect is Radelet McCarthy Polletta. BG

FACES & NEW PLACES

Rycon Special Projects Group is pleased to welcome two new employees to their team: David Dull, Project Manager, and Mike Krehlik, Estimator. Dave has over 18 years experience in the construction industry and carries a Bachelor of Science Degree in Construction Management from the University of Cincinnati. Mike brings over 26 years experience in the construction industry to Rycon Special Projects Estimating Department.

Rob Sklarsky has been appointed to the position of Co-Chairman for the AIA-MBA Joint Committee. Mr. Sklarsky is Senior Vice President at John Deklewa & Sons Inc. The Committee also appointed Joseph Chaffin, AIA director of architecture for Michael Baker Corporation's design department, Baker & Associates, to serve on the Joint Committee as a representative of AIA Pittsburgh. Chartered in 1965, the AIA-MBA Joint Committee consists of ten architects and ten contractors representing the American Institute of Architects Pittsburgh Chapter and the Master Builders' Association of Western PA, respectively. For more information on the AIA-MBA Joint Committee, please call 412-922-3912 or visit http://www.mbawpa.org/aia-mba.

dck worldwide has announced that John Sebastian, LEED AP, Executive Vice President, is now responsible for all Business Development, Sales, Marketing, Strategy, and Property Development for the entire company. With over 30 years of experience, Mr. Sebastian has worked on or been responsible for a wide range of courthouse, commercial building, hospital, airport, correctional, and other dck worldwide projects.

dck worldwide has promoted Brian Contino, P.E., LEED AP, to Vice President of Corporate Strategy & Marketing. In this role, he is responsible for overseeing dck's corporate strategy initiatives and emerging market opportunities, including the company's ongoing efforts in Abu Dhabi, as well as the overall management of the proposal and marketing group. Mr. Contino is a professional engineer with more than 17 years of experience in the construction industry, nearly all of which have been with dck.

Chuck Chrissis has joined dck worldwide as Vice President of Business Development. Mr. Chrissis is responsible for growing dck's commercial business and developing and managing a staff of business development managers across the company.

Joe Deluliis has also joined dck worldwide as Business Development Manager, Pittsburgh Region. Joe is a native Pittsburgher and brings to dck over 20 years of experience in the construction industry, including being a former owner of Magnolia Construction.

The Gateway Engineers, Inc. is pleased to announce the promotion of Jason D. Jesso, PMP to Chief Operating Officer (COO). Jason will lead the Project Support Services Team, and will also serve on the company's board of directors.

Huntington Insurance welcomes Michael Brodzinski as a Sales Executive within their Commercial Lines division. Mike will be focused on providing risk management solutions to contractors, architects, and engineers. Mike earned a Masters in Business Administration from Regis University, a BA Degree from the University of Pittsburgh, and a Construction Risk and Insurance Specialist (CRIS) designation.

Rick Fultineer and Brad Wolf, directors and Robert J. Lewis, P.E. and James Falconi, principals, announce the formation of Berkeley Research Group, LLC at One PPG Place, Suite 2910 Pittsburgh, PA 15222. Berkeley Research Group provides expert testimony, strategic advice and analysis for the construction industry. www.brg-expert.com

Brandon McGlothlin, a Senior Project Consultant with Duggan Rhodes Group, recently became credentialed as a LEED Green Associate. BG

NAIOP

COMMERCIAL REAL ESTATE
DEVELOPMENT ASSOCIATION

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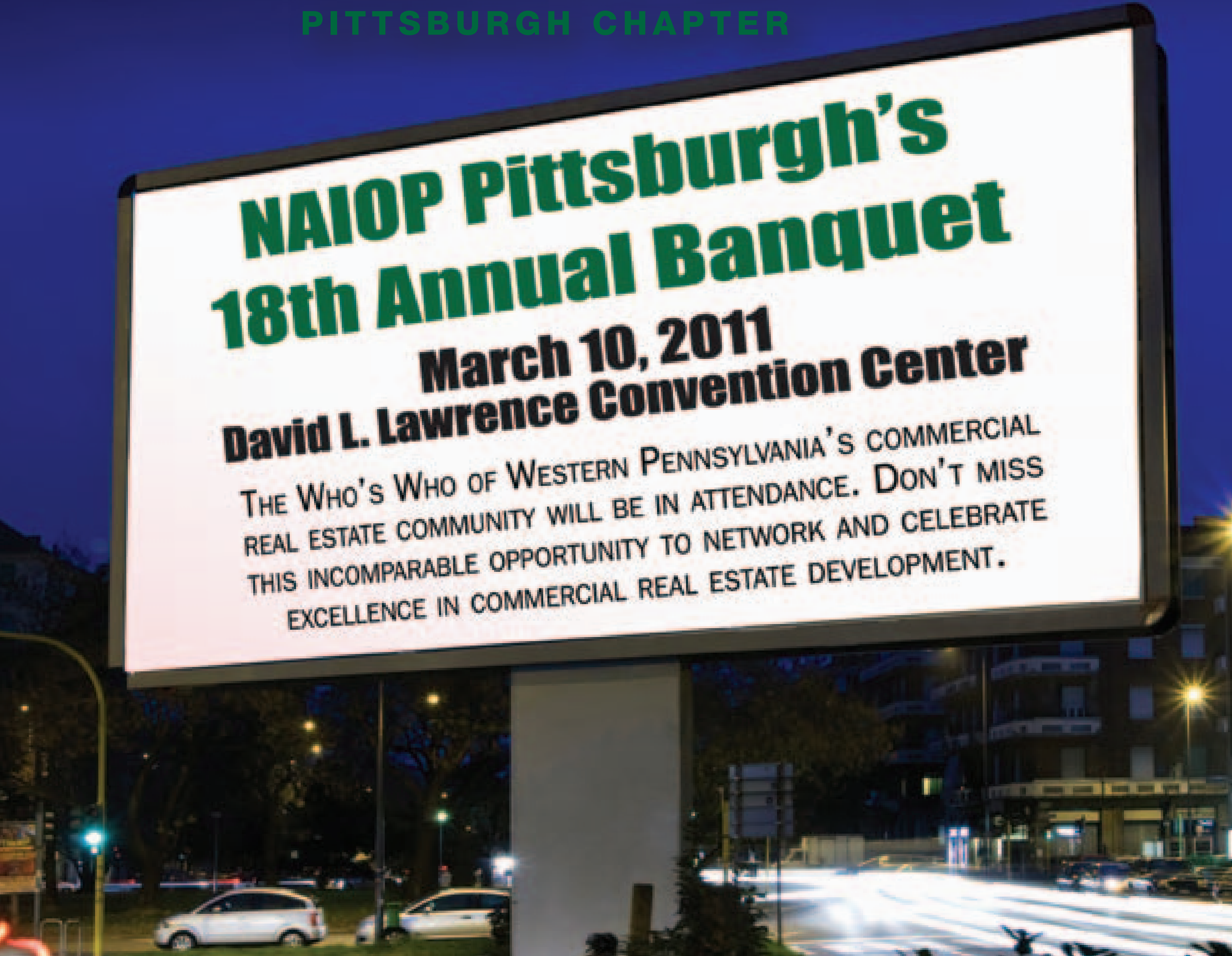

NAIOP Pittsburgh Members		Non-Member	
Individual Registration	*$125*	*Individual Registration*	*$150*
Table of 10	*$1000*	*Table of 10*	*$1250*

To register call 412-928-8303 or visit naioppittsburgh.com

MBA Membership

MBA MEMBERSHIP

The Master Builders' Association (MBA) is a trade organization representing Western Pennsylvania's leading commercial, institutional and industrial contractors. MBA contractors invest in a skilled workforce, implementing award-winning safety programs and offer the best in management and stability.

The MBA is a chapter of the Associated General Contractors of America, the nation's largest and oldest construction trade association. The MBA is committed to improving the construction trade association through education, promoting technological advancements and advocating building the highest quality projects for owners. To learn more go to www.mbawpa.org.

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Closing Out

By Leo Castagnari

Most of my career has been spent during a time in Pittsburgh when we've been rebounding from tough times. Since the industrial base of the economy in southwestern Pennsylvania shut down or moved, there has been an ongoing battle to replace the jobs that were lost and create a new economic infrastructure for our region.

During the past decade I've been associated with NAIOP Pittsburgh as that organization has played its role in trying to create a new economic prosperity for the commercial real estate industry and the region. In recent years the fruits of the hard work of our regional leaders have ripened and Pittsburgh is finally being recognized for its great work force, exceptional standard of living and strong employers. A hard fought prosperity seems to be the legacy that will be left to the next generation of business leaders.

Perhaps because the region's new economy resulted from perseverance through many ups and downs, it's understandable that many business people are taking a wait and see attitude about the promises made by those in the energy sector. I've witnessed most of the NAIOP member firms (as well as many construction and design firms) gain business with companies from the oil and gas, or nuclear, or electrical power industries. My conclusion is that the time to wait and see has come and gone. The companies working to provide energy around the globe are prospering and making a significant impact on our region.

It is not a stretch to speculate that the different pieces of the energy industry will grow to replace the jobs and the economic foundation that the steel industry once provided southwestern Pennsylvania.

For commercial real estate, the steel industry and heavy manufacturing created demand for countless businesses, and underpinned the economy throughout the region. My father worked in construction his whole career, many years with Jendoco Construction, and I understood from him that when the plants were going full steam it meant more construction too. In my view the biggest challenge in rebuilding the regional economy has been to foster growth that wasn't reliant on one industry. Now Pittsburgh has a diverse economic base that includes advanced manufacturing, information and communications technologies, health care and life sciences and financial and business services that makes us less vulnerable to the effects of recession than we once were. Add energy to the mix and Pittsburgh becomes one of the "hot" places that attract new talent and new jobs.

During the last few years most of the region's major commercial real estate stories have been about energy. The Westinghouse Electric campus in Cranberry Woods was the nation's largest lease deal in 2009 and it remains the largest build-to-suit in Pennsylvania's history. Southpointe has been a successful office development for more than a decade but the park is now essentially full, with energy and natural gas companies gobbling up any vacant space. Three of its most recent new buildings have been energy build-to-suit deals – Consol's new headquarters, along with a new building for the Fairmont Supply company and the new Range Resources office. Most of the major leases or build-to-suit projects of the past three years have been for energy-related businesses: Siemens and EQT downtown, Eastern Resources, Talisman Energy, Bechtel in Monroeville just to name a few. And the companies drilling and servicing the Marcellus Shale play have snapped up dozens of buildings and parcels of land throughout the region, many in places that most of us don't ever see.

Western Pennsylvanians should also be proud of the fact that the turnaround in our region has been engineered at the same time we turned around our environment. Jobs used to mean smoke but we've broken that paradigm. The challenge that lies ahead is balancing the desire for growth with the stewardship of this region's beautiful outdoors.

For many of us in the commercial real estate industry it has been a long time since we've had to worry about growth getting ahead of our ability to manage it. The developers in western Pennsylvania have had to deal with many of the same problems as those in other cities during the recent recession. Tight credit and unfavorable lending conditions have hampered the financing of projects. The normalization of financing conditions coupled with demand means an "energetic" future for western Pennsylvania.

Leo Castagnari is executive director for NAIOP Pittsburgh, the Commercial Real Estate Development Association. (naioppittsburgh.com) BG

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