STERLING CONSTRUCTION CO INC
Form 10-K
March 16, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

[X] annual report pursuant to section 13 or 15(d) of the securities exchange act of 1934
For the fiscal year ended: December 31, 2008
[ ] transition report pursuant to section 13 or 15(d) of the securities exchange act of 1934
For the transition period from ____
Commission file number 1-31993

STERLING CONSTRUCTION COMPANY, INC.
(Exact name of registrant as specified in its charter)

Delaware	25-1655321
State or other jurisdiction of incorporation or organization	(I.R.S. Employer Identification No.)
20810 Fernbush Lane Houston, Texas	77073
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (281) 821-9091

Securities registered pursuant to Section 12(b) of the Act:	Name of each exchange on which registered
Title of each class	
Common Stock, $0.01 par value per share (Title of Class)	The NASDAQ Stock Market LLC
Preferred Share Purchase Rights (Title of Class)	

Securities registered pursuant to section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. [ ] Yes [√] No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. [ ] Yes [√] No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. [√] Yes [ ] No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer [ ] Accelerated filer [√]
Non-accelerated filer [ ] (Do not check if a smaller reporting company)Smaller reporting company [ ]

Indicate by check mark if the registrant is a shell company (as defined in Rule 12b-2 of the Act). [ ] Yes [√] No
Aggregate market value of the voting and non-voting common equity held by non-affiliates at June 30, 2008: $228,573,765.
At March 2, 2009, the registrant had 13,189,838 shares of common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

None

Sterling Construction Company, Inc.

Annual Report on Form 10-K

Table of Contents

Table of Contents

PART I

Cautionary Comment Regarding Forward-Looking Statements

This Report includes statements that are, or may be considered to be, "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements are included throughout this Report, including in the sections entitled "Business," "Risk Factors," and "Management's Discussion and Analysis of Financial Condition and Results of Operations" and relate to matters such as our industry, business strategy, goals and expectations concerning our market position, future operations, margins, profitability, capital expenditures, liquidity and capital resources and other financial and operating information. We have used the words "anticipate," "assume," "believe," "budget," "continue," "could," "estimate," "expect," "forecast," "future, " "intend," "may," "plan," "potential," "predict," "project," "should, " "will," "would" and similar terms and phrases to identify forward-looking statements in this Report.

Forward-looking statements reflect our current expectations regarding future events, results or outcomes. These expectations may or may not be realized. Some of these expectations may be based upon assumptions or judgments that prove to be incorrect. In addition, our business and operations involve numerous risks and uncertainties, many of which are beyond our control, that could result in our expectations not being realized or otherwise could materially affect our financial condition, results of operations and cash flows.

Actual events, results and outcomes may differ materially from our expectations due to a variety of factors. Although it is not possible to identify all of these factors, they include, among others, the following:

- delays or difficulties related to the commencement or completion of contracts, including additional costs, reductions in revenues or the payment of completion penalties or liquidated damages;
- actions of suppliers, subcontractors, customers, competitors, banks, surety providers and others which are beyond our control including suppliers' and subcontractor's failure to perform;
- the effects of estimates inherent in our percentage-of-completion accounting policies including onsite conditions that differ materially from those assumed in our original bid, contract modifications, mechanical problems with our machinery or equipment and effects of other risks discussed in this document;
- cost escalations associated with our fixed-unit price contracts, including changes in availability, proximity and cost of materials such as steel, concrete, aggregate, oil, fuel and other construction materials and cost escalations associated with subcontractors and labor;
- our dependence on a few significant customers;
- adverse weather conditions - although we prepare our budgets and bid contracts based on historical rain and snowfall patterns, the incident of rain, snow, hurricanes, etc., may differ significantly from these expectations;
- the presence of competitors with greater financial resources than we have and the impact of competitive services and pricing;
- changes in general economic conditions and resulting reductions or delays, or uncertainties regarding governmental funding for infrastructure services;
- adverse economic conditions in our markets in Texas and Nevada;

- our ability to successfully identify, complete and integrate acquisitions;
- citations issued by any government authority, including the Occupational Safety and Health Administration;

Table of Contents

- the current instability of financial institutions could cause losses on our cash and cash equivalents and short-term investments; and
- the other factors discussed in more detail in Item 1A. —Risk Factors.

In reading this Report, you should consider these factors carefully in evaluating any forward-looking statements and you are cautioned not to place undue reliance on any forward-looking statements. Although we believe that our plans, intentions and expectations reflected in, or suggested by, the forward-looking statements that we make in this Report are reasonable, we can provide no assurance that they will be achieved.

The forward-looking statements included in this Report are made only as of the date of this Report, and we do not undertake to update any information contained in this Report or to publicly release the results of any revisions to any forward-looking statements to reflect events or circumstances that occur, or that we become aware of after the date of this Report, except as may be required by applicable securities laws.

Item 1. Business.

Access to the Company's Filings.

The Company's Website. The Company maintains a website at www.sterlingconstructionco.com on which our latest Annual Report on Form 10-K, recent Quarterly Reports on Form 10-Q, recent Current Reports on Form 8-K, any amendments to those filings, and other filings may be accessed free of charge through a link to the Securities and Exchange Commission's website where those reports are filed. Our website also has recent press releases, the Company's Code of Business Conduct & Ethics and the charters of the Audit Committee, Compensation Committee, and Corporate Governance & Nominating Committee of the Board of Directors. Information is also provided on the Company's "whistle-blower" procedures. Our website content is made available for information purposes only. It should not be relied upon for investment purposes, and none of the information on the website is incorporated into this Report by this reference to it.

The Securities and Exchange Commission (SEC). The public may read and copy any materials filed by the Company with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Room 1580, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330 (1-800-732-0330). The SEC also maintains an Internet site at www.sec.gov on which you can obtain reports, proxy and information statements and other information regarding the Company and other issuers that file electronically with the SEC.

Overview of the Company's Business. Sterling Construction Company, Inc. was founded in 1991 as a Delaware corporation. Our principal executive offices are located at 20810 Fernbush Lane, Houston, Texas 77073, and our telephone number at this address is (281) 821-9091. Our construction business was founded in 1955 by a predecessor company in Michigan and is now operated by our subsidiaries, Texas Sterling Construction Co., a Delaware corporation, or "TSC", Road and Highway Builders, LLC, a Nevada limited liability company, or "RHB", Road and Highway Builders Inc. a Nevada corporation, or "RHB Inc." and Road and Highway Builders of California, Inc., a California corporation or "RHB Cal". The terms "Company", "Sterling", and "we" refer to Sterling Construction Company, Inc. and its subsidiaries except when it is clear that those terms mean only the parent company.

Sterling is a leading heavy civil construction company that specializes in the building, reconstruction and repair of transportation and water infrastructure. Transportation infrastructure projects include highways, roads, bridges and light rail. Water infrastructure projects include water, wastewater and storm drainage systems. Sterling provides general contracting services primarily to public sector clients utilizing its own employees and equipment, including excavating, concrete and asphalt paving, installation of large-diameter water and wastewater distribution systems; construction of bridges and similar large structures; construction of light rail infrastructure; concrete and asphalt batch plant operation; concrete crushing and mining aggregates. Sterling performs the majority of the work required by its contracts with its own crews, and generally engages subcontractors only for ancillary services.

Table of Contents

Although we describe our business in this report in terms of the services we provide, our base of customers and the geographic areas in which we operate, we have concluded that our operations comprise one reportable segment pursuant to Statement of Financial Accounting Standards No. 131 – Disclosures about Segments of an Enterprise and Related Information. In making this determination, we considered that each project has similar characteristics, includes similar services, has similar types of customers and is subject to similar regulatory and economic environments. We organize, evaluate and manage our financial information around each project when making operating decisions and assessing our overall performance.

Sterling has a history of profitable growth, which we have achieved by expanding both our service profile and our market areas. This involves adding services, such as concrete operations, in order to capture a greater percentage of available work in current and potential markets. It also involves strategically expanding operations, either by establishing a branch office in a new market, often after having successfully bid on and completed a project in that market, or by acquiring a company that gives us an immediate entry into a market. Sterling extended both its service profile and its geographic market reach with the 2007 acquisition of RHB, a Nevada construction company.

Sterling operates in Texas and Nevada, two states that management believes benefit from both positive long-term demographic trends as well as an historical commitment to funding transportation and water infrastructure projects. From 2000 to 2006, the population of Texas grew 12.7% and the population of Nevada 24.9%. Expenditures for transportation capital expenditures by the Texas Department of Transportation ("TXDOT") in 2009 are projected to be $2.9 billion. In the November 2007 election, Texas voters approved the issuance of $5 billion of bonds for highway improvements which TXDOT proposes to include in its 2010 and 2011 budgets. In Nevada, total estimated highway capital expenditures in 2009 are projected to be $421 million. These amounts do not include any additional funds that may be received for highway infrastructure construction from the federal government's recently enacted economic-stimulus legislation. Management anticipates that continued population growth and increased spending for infrastructure in these markets will positively affect business opportunities over the coming years.

On October 31, 2007, we acquired our Nevada operations with our purchase of an interest in RHB, which is headquartered in Reno, Nevada. RHB is a heavy civil construction business focused on the construction of roads and highways throughout the state of Nevada and, through RHB Inc., operates an aggregates quarry. We paid $53 million to acquire a 91.67% equity interest in RHB and a 100% equity interest in RHB Inc. The remaining 8.33% interest of RHB is owned by Richard Buenting, the chief executive officer of RHB who continues to run RHB as part of our senior management team, and his ownership interest can be put to or called by us in 2011.

Our Business Strategy. Key features of our business strategy include:

Continue to Add Construction Capabilities. By adding capabilities that augment our core construction competencies, we are able to improve gross margin opportunities, more effectively compete for contracts, and compete for contracts that might not otherwise be available to us.

Increase our Market Leadership in our Core Markets. We have a strong presence in a number of attractive growing markets in Texas and Nevada in which we intend to continue to expand our presence.

Apply Core Competencies Across our Markets. We intend to capitalize on opportunities to export our Texas experience constructing bridges and water and sewer systems into Nevada markets. Similarly, we believe our experience in aggregates and asphalt paving materials in Nevada may open new opportunities for us in our Texas markets.

Expand into Attractive New Markets and Selectively Pursue Strategic Acquisitions. We will continue to seek to identify attractive new markets and opportunities in select western, southwestern and southeastern U.S. markets. We will also continue to assess opportunities to extend our service capabilities and expand our markets through acquisitions.

Position our Business for Future Infrastructure Spending. As evidenced by the federal government's recently enacted economic stimulus legislation, we believe there is a growing awareness of the need to build, reconstruct and repair our country’s infrastructure, including water, wastewater and storm drainage systems, as well as transportation infrastructure such as bridges, highways and mass transit systems. We will continue to build our expertise to capture this infrastructure spending.

Continue to Develop our Employees. We believe that our employees are key to the successful implementation of our business strategy, and we will continue allocating significant resources in order to attract and retain talented managers and supervisory and field personnel.

Table of Contents

Our Markets

We operate in the heavy civil construction segment for infrastructure projects in Texas and Nevada, specializing in transportation and water infrastructure. RHB Cal has bid on construction projects in California, but has not been awarded any such projects.

Demand for transportation and water infrastructure depends on a variety of factors, including overall population growth, economic expansion and the vitality of the market areas in which we operate, as well as unique local topographical, structural and environmental issues. In addition to these factors, demand for the replacement of infrastructure is driven by the general aging of infrastructure and the need for technical improvements to achieve more efficient or safer use of infrastructure and resources. Funding for this infrastructure depends on federal, state and local authorizations.

According to the 2006 census, Texas is the second largest state in population in the U.S. with 23.5 million people and a population growth of 12.7% since 2000, almost double the 6.4% growth rate for the U.S. as a whole over the same period. Three of the 10 largest cities in the U.S. are located in Texas and we have operating divisions in each of those cities: Houston, Dallas/Ft. Worth and San Antonio. Nevada has undergone even more rapid growth, with the state's population expanding 24.9% since 2000 to 2.5 million people in 2006.

Our highway and bridge work is generally funded through federal and state authorizations. The federal government enacted the SAFETEA-LU bill in 2005, which authorized $286 billion for transportation spending through 2009. Of this total, the Texas Department of Transportation ("TXDOT") and the Nevada Department of Transportation ("NDOT") were originally allocated approximately $14.5 billion and $1.3 billion, respectively, over the five years of the authorization. Actual SAFETEA-LU appropriations have been somewhat reduced from the original allocations. The USDOT proposed budget under SAFETEA-LU for the Federal-Aid Highways Program requests $39.4 billion of federal financial assistance to the States for 2009 versus actual appropriations of $41.2 billion for 2008 and $38.0 billion for 2007.

In January, 2009, the 2030 Committee, appointed by TXDOT at the request of the Governor of the State of Texas, submitted its draft report of the transportation needs of Texas. The report indicated that the population of Texas is projected to grow at close to twice the U.S. rate with the population of Texas growing from 23.5 million in 2006 to between 30.5 million and 40.5 million in 2030. The report stated that "With this population increase expected by 2030, transportation modes, costs and congestion are considered a possible roadblock to Texas' projected growth and prosperity."

The report further indicated that Texas needs to spend approximately $313.0 billion (in 2008 dollars) over the 22 year period from 2009 through 2030 to prevent worsening congestion and maintain economic competitiveness on its urban highways and roads, improve congestion/safety and partial connectivity on its rural highways and bridge replacement.

While TXDOT officials have indicated potential short-term funding shortfalls and reductions in spending on transportation, the TXDOT budget for 2009 for transportation construction projects is $2.9 billion versus estimated expenditures of $2.1 billion in 2008 and actual expenditures of $2.7 billion in 2007. Without any new funding resources beyond what are currently available, TXDOT estimates that the annual transportation construction project amounts would be $2.7 billion and $2.4 billion for 2010 and 2011, respectively.

To supplement these projected amounts for 2010 and 2011, TXDOT has proposed that all funds deposited in the State Highway Fund be made available to support transportation construction and maintenance projects—this would increase highway improvement expenditures by approximately $700 million in each of those years to $3.4 billion in 2010 and $3.1 billion in 2011. Further, TXDOT has proposed that the general obligation bonds approved by the voters of Texas in 2007 be appropriated for transportation expenditures in 2010 and 2011, which would add $2.0 billion and $2.3

billion in 2010 and 2011, respectively, to the above amounts. Assuming all these additional amounts are authorized, total TXDOT transportation expenditures would be approximately $5.4 billion in each of the years 2010 and 2011.

In Texas, substantial funds for transportation infrastructure spending are also being provided by toll road and regional mobility authorities for the construction of toll and pass-through toll highways and roads.

NDOT transportation construction expenditures totaled $449.2 million in 2006 and $455.5 million in 2007. NDOT's budget for 2008 and 2009 includes $355.0 million and $420.9 million for transportation capital expenditures, respectively. Projections by NDOT for 2010 and 2011 transportation capital expenditures are $400 million each year. NDOT has stated that Nevada's highway system needs are expected to be $11 billion by 2015; however, it has also stated that Nevada is currently facing a $3.8 billion shortfall (in 2006 dollars) for the 10 largest projects planned for completion in 2015.

Table of Contents

On February 17, 2009 the American Recovery and Reinvestment Act ("economic-stimulus legislation") was enacted by the federal government that authorizes $26.7 billion for highway and bridge construction. A significant portion of these funds will be used for ready-to-go, quick spending highway projects for which contracts can be awarded quickly. States are required, subject to certain exceptions, to obligate 50 percent of the apportionment within 120 days of the apportionment or lose 50 percent of the funds not obligated in that period of time. States would be further required to obligate the second 50 percent of their apportionment within one year of the apportionment. The highway funds will be apportioned to States according to the SAFETEA-LU formula which would be approximately $2.3 billion for Texas and $0.2 billion for Nevada. In addition, the legislation includes $16.4 billion for mass–transit and high speed railways and $7.4 billion for water infrastructure.

Accordingly, aggregate contract lettings, including stimulus funds, would be $4.1 billion in 2009 and $6.6 billion in 2010 in Texas and $521 million in 2009 and $500 million in 2010 in Nevada, based on the currently proposed TXDOT and NDOT budgets and strategic plans.

Our water and wastewater, underground utility, light-rail transit and non-highway paving work is generally funded by municipalities and other local authorities. While the size and growth rates of these markets is difficult to compute as a whole, given the number of municipalities, the differences in funding sources and variations in local budgets, management estimates that the municipal markets in which we operate are providing funding in excess of $1 billion annually. Two of the many municipalities that we perform work for are discussed below for projects.

The City of Houston estimated expenditures for 2008 on storm drainage, street and traffic, waste water and water capital improvements were $721 million. While the budget for these improvements for 2009 has not yet been approved, the most recently adopted five-year capital improvement plan includes $612 million in 2009, $557 million in 2010 and $504 million in 2011 for such improvements and projects; however, prior to the recent enactment of the federal government's economic-stimulus legislation, the Mayor of the City of Houston indicated he would defer $200 million of the 2009 improvements to future years.

The City of San Antonio has adopted a six-year capital improvement plan for 2009 through 2014, which includes $415 million for streets ($124 million in 2009) and $228 million for drainage ($103 million in 2009). The expenditures will be partially funded by the $550 million bond program that the voters of the City of San Antonio approved in May 2007. Included in those bonds was $307 million for streets, bridges and sidewalks improvements and $152 million for drainage improvements to be built over the period 2007 through 2012.

We also do work for other cities, counties, business area redevelopment authorities and regional authorities in Texas which have substantial water and transportation infrastructure spending budgets.

In addition, while we currently have no municipal contracts in the City of Las Vegas, that City’s capital improvement plan proposes expenditures for public works of $807 million for the years 2009 through 2013, including $311 million in 2009. The City Council of Las Vegas recently directed the city staff to delay capital improvement projects that will require additional staffing for one to two years which may cause significant deferrals of construction projects. However, management believes there will be opportunities for the Company to bid on and obtain municipal work in Las Vegas as well as Reno and Carson City.

While our business does not include residential and commercial infrastructure work, the severe fall-off in new projects in those markets in Nevada and to a lesser extent in Texas, has caused a softer bidding climate in our infrastructure markets and has caused some residential and commercial infrastructure contractors to bid on public sector transportation and water infrastructure projects, thus increasing competition and creating downward pressure on bid prices in our markets. These and other factors could adversely affect our ability to maintain or increase our backlog through successful bids for new projects and could adversely affect the profitability of new projects that we do obtain through successful bids.

Recent reductions in miles driven in the U.S. and more fuel efficient vehicles are reducing the amount of federal and state gasoline taxes and tolls collected. Additionally, the current credit crisis may limit the amount of state and local bonds that can be sold at reasonable terms. Further, the nationwide decline in home sales, the increase in foreclosures and a prolonged recession may result in decreases in user fees and property and sales taxes. These and other factors could adversely affect transportation and water infrastructure capital expenditures in our markets.

Due to increased competition and our concern about a possible decline in the future level of bid opportunities, the Company has submitted some of its more recent bids at margins that are lower than bids submitted earlier in 2008 and 2007. The resulting lower margin jobs may affect gross margins recognized in the financial statements for several quarters subsequent to December 31, 2008. Assuming TXDOT moves forward in 2009 with its planned level of spending, we expect to have bidding opportunities that could allow our gross profit margins to return to more historic levels.

Table of Contents

While the bidding climate varies by locality, we continue to bid projects that fit our expertise and current criteria for potential revenues and gross margins after giving consideration to resource utilization, degree of difficulty in the projects, amount of subcontracts and materials and project competition. Our markets are softer and more competitive in the current economic climate. Management believes that the Company has the resources and experience to continue to compete successfully for projects as they become available.

Our Customers. For decades, we have concentrated our operations in Texas. We are headquartered in Houston, and we serve the top markets in Texas, including Houston, San Antonio, Dallas/Fort Worth and Austin. In 2007, we expanded our operations into Nevada.

Although we occasionally undertake contracts for private customers, the vast majority of our contracts are for public sector customers. In Texas, these customers include TXDOT, county and municipal public works departments, the Metropolitan Transit Authority of Harris County, Texas (or Metro), the Harris County Toll Road Authority, North Texas Transit Authority (or NTTA), regional transit and water authorities, port authorities, school districts and municipal utility districts. In Nevada, our primary public sector customer has been NDOT. In 2008, state highway work accounted for 68% of our consolidated revenues, compared with 68% in 2007 and 67% in 2006.

Our largest revenue customer is TXDOT. In 2008, contracts with TXDOT represented 39.2% of our revenues. In 2008, contracts with NDOT represented 21.3% of our revenues. The North Texas Tollroad Authority represented 6.4% of our revenues. In both Texas and Nevada, we provide services to these customers exclusively pursuant to contracts awarded through competitive bidding processes.

In Texas, our municipal customers in 2008 included the City of Houston (8.5% of our 2008 revenues), City of San Antonio (4.2% of our revenues) and Harris County, Texas (4.4% of our 2008 revenues). In the past, we have also completed the construction of certain infrastructure for new light rail systems in Houston, Dallas and Galveston. We anticipate that revenues obtained from the Cities of Houston and San Antonio will continue to increase due to these metropolitan areas' steady gain in population through migration of new residents, the annexation of surrounding communities and the continuing programs to expand storm water and flood control systems and deliver water to suburban communities. We provide services to our municipal customers exclusively pursuant to contracts awarded through competitive bidding processes.

Competition. Our competitors are companies that we bid against for construction contracts. We estimate that Sterling has in excess of 160 competitors in the Texas and Nevada markets that we primarily serve, and they include large national and regional construction companies as well as many smaller contractors. Historically, the construction business has not typically required large amounts of capital, which can result in relative ease of market entry for companies possessing acceptable qualifications.

Factors influencing our competitiveness include price, our reputation for quality, our equipment fleet, our financial strength, our surety bonding capacity and prequalification, our knowledge of local markets and conditions, and our project management and estimating abilities. Although some of our competitors are larger than we are and may possess greater resources or provide more vertically-integrated services, we believe that we are well-positioned to compete effectively and favorably in the markets in which we operate on the basis of the foregoing factors.

We are unable to determine the size of many competitors because they are privately owned, but we believe that we are one of the larger participants in our Texas markets and one of the largest contractors in Houston engaged in municipal civil construction work. In Nevada, we believe that we are a leading asphalt paving contractor in suburban and rural highway projects. We believe that being one of the largest firms in the Houston municipal civil construction market provides us with several advantages, including greater flexibility to manage our backlog in order to schedule and deploy our workforce and equipment resources more efficiently; more cost-effective purchasing of materials, insurance and bonds; the ability to provide a broader range of services than otherwise would be provided through subcontractors; and the availability of substantially more capital and resources to dedicate to each of our contracts. Because we own and maintain most of the equipment required for our contracts and have the experienced workforce to handle many types of municipal civil construction, we are able to bid competitively on many categories of contracts, especially complex, multi-task projects.

In the state highway markets, most of our competitors are large regional contractors, and individual contracts tend to be larger and require more specialized skills than those in the municipal markets. Some of these competitors have the advantage of being more vertically-integrated, or they specialize in certain types of projects such as construction over water. However those competitors, particularly in Texas, often have the disadvantage of having to use a temporary, local workforce to complete each of their state highway contracts. In contrast, we have a permanent workforce who performs our state highway contracts in Texas; however, we do rely on a temporary, unionized workforce for performance of a portion of our state highway contracts in Nevada.

Table of Contents

Contract Backlog

Contract backlog is our estimate of the revenues that we expect to realize in future periods on our construction contracts. We add the revenue value of new contracts to our contract backlog, when we are the low bidder on a public sector contract and have determined that there are no apparent impediments to award of the contract. As construction on our contracts progresses, we increase or decrease contract backlog to take into account changes in estimated quantities under fixed unit price contracts, as well as to reflect changed conditions, change orders and other variations from initially anticipated contract revenues and costs, including completion penalties and bonuses. We subtract from contract backlog the amounts we recognize as revenues on contracts.

Our backlog of construction projects was $448 million at December 31, 2008, versus backlog of $450 million at December 31, 2007. During 2008, we were awarded $413 million in new contracts and change orders and recognized revenues earned of $415 million. The reduction in backlog was due to increased competition for contracts and economic conditions in certain of our markets. To date, the Company has had no material project cancellations or scope reductions in any of its backlog as a result of reduced funding authorization.

Of the contract backlog at December 31, 2008, approximately $379 million is scheduled for completion in 2009. At December 31, 2008, we had no contracts in backlog which had not been officially awarded to us.

Substantially all of the contracts in our contract backlog may be canceled at the election of the customer; however, we have not been materially adversely affected by contract cancellations or modifications in the past. See the section below entitled "Contracts - Contract Management Process."

Contracts.

Types of Contracts. We provide our services by using traditional general contracting arrangements, which are predominantly fixed unit price contracts awarded based on the lowest bid. A small amount of our revenue is produced under change orders or emergency contracts arranged on a cost plus basis.

Fixed unit price contracts are generally used in competitively-bid public civil construction contracts and, to a lesser degree, building construction contracts. Contractors under fixed unit price contracts are generally committed to provide all of the resources required to complete a contract for a fixed price per unit. Fixed unit price contracts generally transfer more risk to the contractor but offer the opportunity, under favorable circumstances, for greater profits. These contracts are generally subject to negotiated change orders, frequently due to differences in site conditions from those anticipated when the bid is placed. Some contracts provide for penalties if the contract is not completed on time, or incentives if it is completed ahead of schedule.

Contract Management Process. We identify potential contracts from a variety of sources, including through subscriber services that notify us of contracts out for bid, through advertisements by federal, state and local governmental entities, through our business development efforts and through meetings with other participants in the construction industry. After determining which contracts are available, we decide which contracts to pursue based on such factors as the relevant skills required, the contract size and duration, the availability of our personnel and equipment, the size and makeup of our current backlog, our competitive advantages and disadvantages, prior experience, the contracting agency or customer, the source of contract funding, geographic location, likely competition, construction risks, gross margin opportunities, penalties or incentives and the type of contract.

As a condition to pursuing certain contracts, we are sometimes required to complete a prequalification process with the applicable agency or customer. Some customers, such as TXDOT and NDOT, require yearly prequalification, and other customers have experience requirements specific to the contract. The prequalification process generally limits bidders to those companies with the operational experience and financial capability to effectively complete the particular contract in accordance with the plans, specifications and construction schedule.

There are several factors that can create variability in contract performance and financial results compared to our bid assumptions on a contract. The most significant of these include the completeness and accuracy of our original bid analysis, recognition of costs associated with added scope changes, extended overhead due to customer and weather delays, subcontractor performance issues, changes in productivity expectations, site conditions that differ from those assumed in the original bid, and changes in the availability and proximity of materials. In addition, each of our original bids is based on the contract customer's estimates of the quantities needed to complete a contract. If the quantities ultimately needed are different, our backlog and financial performance on the contract will change. All of these factors can lead to inefficiencies in contract performance, which can increase costs and lower profits. Conversely, if any of these or other factors is more positive than the assumptions in our bid, contract profitability can improve.

Table of Contents

The estimating process for our contracts in Texas typically involves three phases. Initially, we consider the level of anticipated competition and our available resources for the prospective project. If we then decide to continue considering a project, we undertake the second phase of the contract process and spend up to six weeks performing a detailed review of the plans and specifications, summarize the various types of work involved and related estimated quantities, determine the contract duration and schedule and highlight the unique and riskier aspects of the contract. Concurrent with this process, we estimate the cost and availability of labor, material, equipment, subcontractors and the project team required to complete the contract on time and in accordance with the plans and specifications. Substantially all of our estimates are made on a per-unit basis for each line item, with the typical contract containing 50 to 400 line items. The final phase consists of a detailed review of the estimate by management, including, among other things, assumptions regarding cost, approach, means and methods, productivity, risk and the estimated profit margin. This profit amount will vary according to management’s perception of the degree of difficulty of the contract, the current competitive climate and the size and makeup of our backlog. Our project managers are intimately involved throughout the estimating and construction process so that contract issues, and risks, can be understood and addressed on a timely basis.

The estimating process in Nevada is primarily the responsibility of the management of those operations. Management reviews all of the plans and specifications for a proposed project, estimates the costs to complete the project and the risks involved, adds an appropriate profit level, and, based on all of that information, determines whether to submit a bid on the project. Prior to submittal of any proposals, estimates are reviewed by Sterling management.

To manage risks of changes in material prices and subcontracting costs used in tendering bids for construction contracts, we obtain firm price quotations from our suppliers, except for fuel, and subcontractors before submitting a bid. These quotations do not include any quantity guarantees, and we have no obligation for materials or subcontract services beyond those required to complete the respective contracts that we are awarded for which quotations have been provided.

Beginning in January 2009, in order to reduce the volatility that we experienced in 2008 in our cost of diesel and gasoline fuel, we started a process of investing in certain securities, the assets of which are a crude oil commodity pool. The change in the unit price of these securities generally follows the change in percentage terms of the price of crude oil. Since there is a strong correlation between the price of crude oil and our diesel and gasoline fuel costs, we believe that over future reporting periods, the gains and losses on these securities will tend to offset the increases and decreases in the price we pay for diesel and gasoline and thus reduce the effect of the volatility of such fuel costs on our results of operations. There can, however, be no assurance that this process will be successful.

Substantially all of our contracts are entered into with governmental entities and are generally awarded to the lowest bidder after a solicitation of bids by the project owner. Requests for proposals or negotiated contracts with public or private customers are generally awarded based on a combination of technical capability and price, taking into consideration factors such as contract schedule and prior experience.

During the construction phase of a contract, we monitor our progress by comparing actual costs incurred and quantities completed to date with budgeted amounts and the contract schedule, and periodically prepare an updated estimate of total forecasted revenue, cost and expected profit for the contract.

During the normal course of most contracts, the customer, and sometimes the contractor, initiates modifications or changes to the original contract to reflect, among other things, changes in quantities, specifications or design, method or manner of performance, facilities, materials, site conditions and the period for completion of the work. In many cases, final contract quantities may differ from those specified by the customer. Generally, the scope and price of these modifications are documented in a “change order” to the original contract and reviewed, approved and paid in accordance with the normal change order provisions of the contract. We are often required to perform extra or change order work as directed by the customer even if the customer has not agreed in advance on the scope or price of the work to be performed. This process may result in disputes over whether the work performed is beyond the scope of the work included in the original contract plans and specifications or, even if the customer agrees that the work performed qualifies as extra work, the price that the customer is willing to pay for the extra work. These disputes may not be settled to our satisfaction. Even when the customer agrees to pay for the extra work, we may be required to fund the cost of the work for a lengthy period of time until the change order is approved and funded by the customer. In addition, any delay caused by the extra work may adversely impact the timely scheduling of other work on the contract (or on other contracts) and our ability to meet contract milestone dates.

The process for resolving contract claims varies from one contract to another but, in general, we attempt to resolve claims at the project supervisory level through the normal change order process or, if necessary, with higher levels of management within our organization and the customer's organization. Regardless of the process, when a potential claim arises on a contract, we typically have the contractual obligation to perform the work and must incur the related costs. We do not recoup the costs unless and until the claim is resolved, which could take a significant amount of time.

Most of our construction contracts provide for termination of the contract for the convenience of the customer, with provisions to pay us only for work performed through the date of termination. Our backlog and results of operations have not been materially adversely affected by these provisions in the past.

Table of Contents

We act as the prime contractor on almost all of the construction contracts that we undertake. We complete the majority of our contracts with our own resources, and we typically subcontract only specialized activities, such as traffic control, electrical systems, signage and trucking. As the prime contractor, we are responsible for the performance of the entire contract, including subcontract work. Thus, we are subject to increased costs associated with the failure of one or more subcontractors to perform as anticipated. We manage this risk by reviewing the size of the subcontract, the financial stability of the subcontractor and other factors. Although we generally do not require that our subcontractors furnish a bond or other type of security to guarantee their performance, we require performance and payment bonds on many specialized or large subcontract portions of our contracts. Disadvantaged business enterprise regulations require us to use our best efforts to subcontract a specified portion of contract work performed for governmental entities to certain types of subcontractors, including minority- and women-owned businesses. We have not experienced significant costs associated with subcontractor performance issues.

Insurance and Bonding. All of our buildings and equipment are covered by insurance, at levels which our management believes to be adequate. In addition, we maintain general liability and excess liability insurance, all in amounts consistent with our risk of loss and industry practice. We self-insure our workers' compensation and health plan claims subject to stop-loss insurance coverage.

As a normal part of the construction business, we are generally required to provide various types of surety and payment bonds that provide an additional measure of security for our performance under public sector contracts. Typically, a bidder for a contract must post a bid bond, generally for 5% to 10% of the amount bid, and on winning the bid, must post a performance and payment bond for 100% of the contract amount. Upon completion of a contract, before receiving final payment on the contract, a contractor must post a maintenance bond for generally 1% of the contract amount for one to two years. Our ability to obtain surety bonds depends upon our capitalization, working capital, aggregate contract size, past performance, management expertise and external factors, including the capacity of the overall surety market. Surety companies consider such factors in light of the amount of our backlog that we have currently bonded and their current underwriting standards, which may change from time to time. As is customary, we have agreed to indemnify our bonding company for all losses incurred by it in connection with bonds that are issued, and we have granted our bonding company a security interest in certain assets as collateral for such obligation.

Employees. At February 15, 2009, we had approximately 1,200 employees, including 16 project managers and approximately 50 superintendents who manage over 125 fully-equipped crews in our construction business. Of such employees, approximately 50 were located in our Houston headquarters, with most of the others being field personnel. Of our Nevada employees, 70 are union members represented by three unions.

Our business is dependent upon a readily available supply of management, supervisory and field personnel. Substantially all of our employees who work on our contracts in Texas are a permanent part of our workforce, and we generally do not rely on temporary employees to complete these contracts. In contrast, many of our employees who work on our contracts in Nevada are temporary employees. In the past, we have been able to attract sufficient numbers of personnel to support the growth of our operations.

We conduct extensive safety training programs, which have allowed us to maintain a high safety level at our worksites. All newly-hired employees undergo an initial safety orientation, and for certain types of projects, we conduct specific hazard training programs. Our project foremen and superintendents conduct weekly on-site safety meetings, and our full-time safety inspectors make random site safety inspections and perform assessments and training if infractions are discovered. In addition, all of our superintendents and project managers are required to complete an OSHA-approved safety course.

Item 1A. Risk Factors.

The risks described below are those we believe to be the material risks we face. Any of the risk factors described below could significantly and adversely affect our business, prospects, financial condition, results of operations and cash flows.

Risks Relating to Our Business.

If we are unable to accurately estimate the overall risks or costs when we bid on a contract that is ultimately awarded to us, we may achieve a lower than anticipated profit or incur a loss on the contract.

Substantially all of our revenues and backlog are typically derived from fixed unit price contracts. Fixed unit price contracts require us to perform the contract for a fixed unit price irrespective of our actual costs. As a result, we realize a profit on these contracts only if we successfully estimate our costs and then successfully control actual costs and avoid cost overruns. If our cost estimates for a contract are inaccurate, or if we do not execute the contract within our cost estimates, then cost overruns may cause us to incur losses or cause the contract not to be as profitable as we expected. This, in turn, could negatively affect our cash flow, earnings and financial position.

Table of Contents

The costs incurred and gross profit realized on such contracts can vary, sometimes substantially, from the original projections due to a variety of factors, including, but not limited to:

- onsite conditions that differ from those assumed in the original bid;
- delays caused by weather conditions;
- contract modifications creating unanticipated costs not covered by change orders;
- changes in availability, proximity and costs of materials, including steel, concrete, aggregates and other construction materials (such as stone, gravel, sand and oil for asphalt paving), as well as fuel and lubricants for our equipment;
- inability to predict the costs of accessing and producing aggregates and purchasing oil, required for asphalt paving projects;
- availability and skill level of workers in the geographic location of a project;
- our suppliers' or subcontractors' failure to perform due to various reasons including bankruptcy;
- fraud or theft committed by our employees and management;
- mechanical problems with our machinery or equipment;
- citations issued by any governmental authority, including the Occupational Safety and Health Administration;
- difficulties in obtaining required governmental permits or approvals;
- changes in applicable laws and regulations; and
- claims or demands from third parties alleging damages arising from our work or from the project of which our work is part.

Many of our contracts with public sector customers contain provisions that purport to shift some or all of the above risks from the customer to us, even in cases where the customer is partly at fault. Our experience has often been that public sector customers have been willing to negotiate equitable adjustments in the contract compensation or completion time provisions if unexpected circumstances arise. If public sector customers seek to impose contractual risk-shifting provisions more aggressively, we could face increased risks, which may adversely affect our cash flow, earnings and financial position.

Economic downturns or reductions in government funding of infrastructure projects could reduce our revenues and profits and have a material adverse effect on our results of operations.

Our business is highly dependent on the amount and timing of infrastructure work funded by various governmental entities, which, in turn, depends on the overall condition of the economy, the need for new or replacement infrastructure, the priorities placed on various projects funded by governmental entities and federal, state or local government spending levels. Spending on infrastructure could decline for numerous reasons, including decreased revenues received by state and local governments for spending on such projects, including federal funding. For example, state spending on highway and other projects can be adversely affected by decreases or delays in, or uncertainties regarding, federal highway funding, which could adversely affect us. We are reliant upon contracts with the Texas Department of Transportation, or TXDOT, and the Nevada Department of Transportation, or NDOT, for a significant portion of our revenues. Recent public statements by state officials indicate potential TXDOT and NDOT funding shortfalls and reductions in spending.

Table of Contents

While our business does not include residential and commercial infrastructure work, the severe fall-off in new projects in those markets in Nevada and to a lesser extent in Texas, has caused a softer bidding climate in our infrastructure markets and has caused some residential and commercial infrastructure contractors to bid on public sector transportation and water infrastructure projects, thus increasing competition and creating downward pressure on bid prices in our markets. These and other factors could adversely affect our ability to maintain or increase our backlog through successful bids for new projects and could adversely affect the profitability of new projects that we do obtain through successful bids.

Recent reductions in miles driven in the U.S. and more fuel efficient vehicles are reducing federal and state gasoline taxes and tolls collected. Additionally, the current credit crisis may limit the amount of state and local bonds that can be sold at reasonable terms. Further, the nationwide decline in home sales, increase in foreclosures and a prolonged recession may result in decreases in user fees and property and sales taxes. These and other factors could adversely affect transportation and water infrastructure capital expenditures in our markets.

The cancellation of significant contracts or our disqualification from bidding for new contracts could reduce our revenues and profits and have a material adverse effect on our results of operations.

Contracts that we enter into with governmental entities can usually be canceled at any time by them with payment only for the work already completed. In addition, we could be prohibited from bidding on certain governmental contracts if we fail to maintain qualifications required by those entities. A cancellation of an unfinished contract or our debarment from the bidding process could cause our equipment and work crews to be idled for a significant period of time until other comparable work became available, which could have a material adverse effect on our business and results of operations.

We operate in Texas and Nevada, and any adverse change to the economy or business environment in Texas or Nevada could significantly and adversely affect our operations, which would lead to lower revenues and reduced profitability.

We operate in Texas and Nevada, and our Texas operations are particularly concentrated in the Houston area. Because of this concentration in specific geographic locations, we are susceptible to fluctuations in our business caused by adverse economic or other conditions in these regions, including natural or other disasters. A stagnant or depressed economy in Texas or Nevada could adversely affect our business, results of operations and financial condition.

Our acquisition strategy involves a number of risks.

In addition to organic growth of our construction business, we intend to continue pursuing growth through the acquisition of companies or assets that may enable us to expand our project skill-sets and capabilities, enlarge our geographic markets, add experienced management and increase critical mass to enable us to bid on larger contracts. However, we may be unable to implement this growth strategy if we cannot reach agreements for potential acquisitions on acceptable terms or for other reasons. Moreover, our acquisition strategy involves certain risks, including:

- difficulties in the integration of operations and systems;
- difficulties applying our expertise in one market into another market;
- the key personnel and customers of the acquired company may terminate their relationships with the acquired company;

- we may experience additional financial and accounting challenges and complexities in areas such as tax planning and financial reporting;

- we may assume or be held liable for risks and liabilities (including for environmental-related costs and liabilities) as a result of our acquisitions, some of which we may not discover during our due diligence;

- our ongoing business may be disrupted or receive insufficient management attention; and

- we may not be able to realize cost savings or other financial benefits we anticipated.

Future acquisitions may require us to obtain additional equity or debt financing, as well as additional surety bonding capacity, which may not be available on terms acceptable to us or at all. Moreover, to the extent that any acquisition results in additional goodwill, it will reduce our tangible net worth, which might have an adverse effect on our credit and bonding capacity.

Table of Contents

Our industry is highly competitive, with a variety of larger companies with greater resources competing with us, and our failure to compete effectively could reduce the number of new contracts awarded to us or adversely affect our margins on contracts awarded.

Essentially all of the contracts on which we bid are awarded through a competitive bid process, with awards generally being made to the lowest bidder, but sometimes recognizing other factors, such as shorter contract schedules or prior experience with the customer. Within our markets, we compete with many national, regional and local construction firms. Some of these competitors have achieved greater market penetration than we have in the markets in which we compete, and some have greater financial and other resources than we do. In addition, there are a number of national companies in our industry that are larger than we are and that, if they so desire, could establish a presence in our markets and compete with us for contracts. In some markets where home building projects have slowed, construction companies that lack available work in the home building market have begun on a limited scale bidding on highway and municipal construction contracts. As a result, we may need to accept lower contract margins in order to compete against competitors that have the ability to accept awards at lower prices or have a pre-existing relationship with a customer. If we are unable to compete successfully in our markets, our relative market share and profits could be reduced.

Our dependence on subcontractors and suppliers of materials (including petroleum-based products) could increase our costs and impair our ability to complete contracts on a timely basis or at all, which would adversely affect our profits and cash flow.

We rely on third-party subcontractors to perform some of the work on many of our contracts. We generally do not bid on contracts unless we have the necessary subcontractors committed for the anticipated scope of the contract and at prices that we have included in our bid, except for trucking arrangements needed for our Nevada operations. Therefore, to the extent that we cannot engage subcontractors, our ability to bid for contracts may be impaired. In addition, if a subcontractor is unable to deliver its services according to the negotiated terms for any reason, including the deterioration of its financial condition, we may suffer delays and be required to purchase the services from another source at a higher price. This may reduce the profit to be realized, or result in a loss, on a contract.

We also rely on third-party suppliers to provide most of the materials (including aggregates, asphalt, concrete, steel and pipe) for our contracts, except in Nevada where we source and produce most of our own aggregates. We do not own or operate any quarries in Texas, and there are no naturally occurring sources of aggregates in the Houston metropolitan area. We normally do not bid on contracts unless we have commitments from suppliers for the materials required to complete the contract and at prices that we have included in our bid, except for some aggregates we use in our Nevada construction projects. Thus, to the extent that we cannot obtain commitments from our suppliers for materials, our ability to bid for contracts may be impaired. In addition, if a supplier is unable to deliver materials according to the negotiated terms of a supply agreement for any reason, including the deterioration of its financial condition, we may suffer delays and be required to purchase the materials from another source at a higher price. This may reduce the profit to be realized, or result in a loss, on a contract.

Diesel fuel and other petroleum-based products are utilized to operate the plants and equipment on which we rely to perform our construction contracts. In addition, our asphalt plants and suppliers use oil in combination with aggregates to produce asphalt used in our road and highway construction projects. Decreased supplies of such products relative to demand, unavailability of petroleum supplies due to refinery turnarounds, and other factors can increase the cost of such products. Future increases in the costs of fuel and other petroleum-based products used in our business, particularly if a bid has been submitted for a contract and the costs of such products have been estimated at amounts less than the actual costs thereof, could result in a lower profit, or a loss, on a contract.

We may not accurately assess the quality, and we may not accurately estimate the quantity, availability and cost, of aggregates we plan to produce, particularly for projects in rural areas of Nevada, which could have a material adverse effect on our results of operations.

Particularly for projects in rural areas of Nevada, we typically estimate these factors for anticipated aggregate sources that we have not previously used to produce aggregates, which increases the risk that our estimates may be inaccurate. Inaccuracies in our estimates regarding aggregates could result in significantly higher costs to supply aggregates needed for our projects, as well as potential delays and other inefficiencies. As a result, our failure to accurately assess the quality, quantity, availability and cost of aggregates could cause us to incur losses, which could materially adversely affect our results of operations.

We may not be able to fully realize the revenue anticipated by our reported backlog.

Almost all of the contracts included in backlog are awarded by public sector customers through a competitive bid process, with the award generally being made to the lowest bidder. We add new contracts to our backlog, typically when we are the low bidder on a public sector contract and management determines that there are no apparent impediments to award of the contract. As construction on our contracts progresses, we increase or decrease backlog to take account of changes in estimated quantities under fixed unit price contracts, as well as to reflect changed conditions, change orders and other variations from initially anticipated contract revenues and costs, including completion penalties and bonuses. We subtract from backlog the amounts we bill on contracts.

Most of the contracts with our public sector customers can be terminated at their discretion. If a customer cancels, suspends, delays or reduces a contract, we may be reimbursed for certain costs but typically will not be able to bill the total amount that had been reflected in our backlog. Cancellation of one or more contracts that constitute a large percentage of our backlog, and our inability to find a substitute contract, would have a material adverse effect on our business, results of operations and financial condition.

Table of Contents

If we are unable to attract and retain key personnel and skilled labor, or if we encounter labor difficulties, our ability to bid for and successfully complete contracts may be negatively impacted.

Our ability to attract and retain reliable, qualified personnel is a significant factor that enables us to successfully bid for and profitably complete our work. This includes members of our management, project managers, estimators, supervisors, foremen, equipment operators and laborers. The loss of the services of any of our management could have a material adverse effect on us. Our future success will also depend on our ability to hire and retain, or to attract when needed, highly-skilled personnel. Competition for these employees is intense, and we could experience difficulty hiring and retaining the personnel necessary to support our business. If we do not succeed in retaining our current employees and attracting, developing and retaining new highly-skilled employees, our reputation may be harmed and our future earnings may be negatively impacted.

In Texas, we rely heavily on immigrant labor. Any adverse changes to existing laws and regulations, or changes in enforcement requirements or practices, applicable to employment of immigrants could negatively impact the availability and cost of the skilled personnel and labor we need, particularly in Texas. We may not be able to continue to attract and retain sufficient employees at all levels due to changes in immigration enforcement practices or compliance standards or for other reasons.

In Nevada, a substantial number of our equipment operators and laborers are unionized. Any work stoppage or other labor dispute involving our unionized workforce would have a material adverse effect on our operations and operating results in Nevada.

Our contracts may require us to perform extra or change order work, which can result in disputes and adversely affect our working capital, profits and cash flows.

Our contracts generally require us to perform extra or change order work as directed by the customer even if the customer has not agreed in advance on the scope or price of the extra work to be performed. This process may result in disputes over whether the work performed is beyond the scope of the work included in the original project plans and specifications or, if the customer agrees that the work performed qualifies as extra work, the price that the customer is willing to pay for the extra work. These disputes may not be settled to our satisfaction. Even when the customer agrees to pay for the extra work, we may be required to fund the cost of such work for a lengthy period of time until the change order is approved by the customer and we are paid by the customer.

To the extent that actual recoveries with respect to change orders or amounts subject to contract disputes or claims are less than the estimates used in our financial statements, the amount of any shortfall will reduce our future revenues and profits, and this could have a material adverse effect on our reported working capital and results of operations. In addition, any delay caused by the extra work may adversely impact the timely scheduling of other project work and our ability to meet specified contract milestone dates.

Our failure to meet schedule or performance requirements of our contracts could adversely affect us.

In most cases, our contracts require completion by a scheduled acceptance date. Failure to meet any such schedule could result in additional costs, penalties or liquidated damages being assessed against us, and these could exceed projected profit margins on the contract. Performance problems on existing and future contracts could cause actual results of operations to differ materially from those anticipated by us and could cause us to suffer damage to our reputation within the industry and among our customers.

Unanticipated adverse weather conditions may cause delays, which could slow completion of our contracts and negatively affect our revenues and cash flow.

Because all of our construction projects are built outdoors, work on our contracts is subject to unpredictable weather conditions, which could become more frequent or severe if general climatic changes occur. For example, evacuations in Texas due to Hurricane Rita and Ike resulted in our inability to perform work on all Houston-area contracts for several days. Lengthy periods of wet weather will generally interrupt construction, and this can lead to under-utilization of crews and equipment, resulting in less efficient rates of overhead recovery. For example, during the first nine months of 2007, we experienced an above-average number of days and amount of rainfall across our Texas markets, which impeded our ability to work on construction projects and reduced our gross profit. During the late fall to early spring months of the year, our work on construction projects in Nevada may also be curtailed because of snow and other work-limiting weather. While revenues can be recovered following a period of bad weather, it is generally impossible to recover the inefficiencies, and significant periods of bad weather typically reduce profitability of affected contracts both in the current period and during the future life of affected contracts. Such reductions in contract profitability negatively affect our results of operations in current and future periods until the affected contracts are completed.

Table of Contents

Timing of the award and performance of new contracts could have an adverse effect on our operating results and cash flow.

It is generally very difficult to predict whether and when new contracts will be offered for tender, as these contracts frequently involve a lengthy and complex design and bidding process, which is affected by a number of factors, such as market conditions, financing arrangements and governmental approvals. Because of these factors, our results of operations and cash flows may fluctuate from quarter to quarter and year to year, and the fluctuation may be substantial.

The uncertainty of the timing of contract awards may also present difficulties in matching the size of our equipment fleet and work crews with contract needs. In some cases, we may maintain and bear the cost of more equipment and ready work crews than are currently required, in anticipation of future needs for existing contracts or expected future contracts. If a contract is delayed or an expected contract award is not received, we would incur costs that could have a material adverse effect on our anticipated profit.

In addition, the timing of the revenues, earnings and cash flows from our contracts can be delayed by a number of factors, including adverse weather conditions such as prolonged or intense periods of rain, snow, storms or flooding, delays in receiving material and equipment from suppliers and changes in the scope of work to be performed. Such delays, if they occur, could have adverse effects on our operating results for current and future periods until the affected contracts are completed.

Our dependence on a limited number of customers could adversely affect our business and results of operations.

Due to the size and nature of our construction contracts, one or a few customers have in the past and may in the future represent a substantial portion of our consolidated revenues and gross profits in any one year or over a period of several consecutive years. For example, in 2008, approximately 54.1% of our revenue in Texas was generated from three customers, and approximately 95.3% of our revenue in Nevada was generated from one customer. Similarly, our backlog frequently reflects multiple contracts for individual customers; therefore, one customer may comprise a significant percentage of backlog at a certain point in time. An example of this is TXDOT, with which we had 14 contracts in our backlog at December 31, 2008. The loss of business from any one of such customers could have a material adverse effect on our business or results of operations. Recent public statements by TXDOT and NDOT officials indicate potential funding shortfalls and reductions in spending. Because we do not maintain any reserves for payment defaults, a default or delay in payment on a significant scale could materially adversely affect our business, results of operations and financial condition.

We may incur higher costs to lease, acquire and maintain equipment necessary for our operations, and the market value of our owned equipment may decline.

We have traditionally owned most of the construction equipment used to build our projects. To the extent that we are unable to buy construction equipment necessary for our needs, either due to a lack of available funding or equipment shortages in the marketplace, we may be forced to rent equipment on a short-term basis, which could increase the costs of performing our contracts.

The equipment that we own or lease requires continuous maintenance, for which we maintain our own repair facilities. If we are unable to continue to maintain the equipment in our fleet, we may be forced to obtain third-party repair services, which could increase our costs. In addition, the market value of our equipment may unexpectedly decline at a faster rate than anticipated.

An inability to obtain bonding could limit the aggregate dollar amount of contracts that we are able to pursue.

As is customary in the construction business, we are required to provide surety bonds to secure our performance under construction contracts. Our ability to obtain surety bonds primarily depends upon our capitalization, working capital, past performance, management expertise and reputation and certain external factors, including the overall capacity of the surety market. Surety companies consider such factors in relationship to the amount of our backlog and their underwriting standards, which may change from time to time. Events that affect the insurance and bonding markets generally may result in bonding becoming more difficult to obtain in the future, or being available only at a significantly greater cost. Our inability to obtain adequate bonding, and, as a result, to bid on new contracts, could have a material adverse effect on our future revenues and business prospects.

Table of Contents

Our operations are subject to hazards that may cause personal injury or property damage, thereby subjecting us to liabilities and possible losses, which may not be covered by insurance.

Our workers are subject to the usual hazards associated with providing construction and related services on construction sites, plants and quarries. Operating hazards can cause personal injury and loss of life, damage to or destruction of property, plant and equipment and environmental damage. We self-insure our workers' compensation claims, subject to stop-loss insurance coverage. We also maintain insurance coverage in amounts and against the risks that we believe are consistent with industry practice, but this insurance may not be adequate to cover all losses or liabilities that we may incur in our operations.

Insurance liabilities are difficult to assess and quantify due to unknown factors, including the severity of an injury, the determination of our liability in proportion to other parties, the number of incidents not reported and the effectiveness of our safety program. If we were to experience insurance claims or costs above our estimates, we might also be required to use working capital to satisfy these claims rather than to maintain or expand our operations. To the extent that we experience a material increase in the frequency or severity of accidents or workers' compensation claims, or unfavorable developments on existing claims, our operating results and financial condition could be materially and adversely affected.

Environmental and other regulatory matters could adversely affect our ability to conduct our business and could require expenditures that could have a material adverse effect on our results of operations and financial condition.

Our operations are subject to various environmental laws and regulations relating to the management, disposal and remediation of hazardous substances and the emission and discharge of pollutants into the air and water. We could be held liable for such contamination created not only from our own activities but also from the historical activities of others on our project sites or on properties that we acquire or lease. Our operations are also subject to laws and regulations relating to workplace safety and worker health, which, among other things, regulate employee exposure to hazardous substances. Immigration laws require us to take certain steps intended to confirm the legal status of our immigrant labor force, but we may nonetheless unknowingly employ illegal immigrants. Violations of such laws and regulations could subject us to substantial fines and penalties, cleanup costs, third-party property damage or personal injury claims. In addition, these laws and regulations have become, and enforcement practices and compliance standards are becoming, increasingly stringent. Moreover, we cannot predict the nature, scope or effect of legislation or regulatory requirements that could be imposed, or how existing or future laws or regulations will be administered or interpreted, with respect to products or activities to which they have not been previously applied. Compliance with more stringent laws or regulations, as well as more vigorous enforcement policies of the regulatory agencies, could require us to make substantial expenditures for, among other things, pollution control systems and other equipment that we do not currently possess, or the acquisition or modification of permits applicable to our activities.

Our aggregate quarry lease in Nevada could subject us to costs and liabilities. As lessee and operator of the quarry, we could be held responsible for any contamination or regulatory violations resulting from activities or operations at the quarry. Any such costs and liabilities could be significant and could materially and adversely affect our business, operating results and financial condition.

We may be unable to sustain our historical revenue growth rate.

Our revenue has grown rapidly in recent years. However, we may be unable to sustain these recent revenue growth rates for a variety of reasons, including limits on additional growth in our current markets, reduced spending by our customers, less success in competitive bidding for contracts, limitations on access to necessary working capital and investment capital to sustain growth, limitations on access to bonding to support increased contracts and operations, inability to hire and retain essential personnel and to acquire equipment to support growth, and inability to identify acquisition candidates and successfully acquire and integrate them into our business. A decline in our revenue growth could have a material adverse effect on our financial condition and results of operations if we are unable to reduce the growth of our operating expenses at the same rate.

Our growth has been funded in part by our utilization of net operating loss carry-forwards, or NOLs, to reduce the amounts that we have paid for income taxes, and we expect our NOLs to be fully utilized in our 2008 federal income tax return. Paying taxes will reduce cash flows from operations compared to prior periods, as we will be required to fund the payment of taxes in 2008 and future periods. To the extent that cash flow from operations is insufficient to fund future investments, make acquisitions or provide needed additional working capital, we may require additional financing from other sources of funds.

Terrorist attacks have impacted, and could continue to negatively impact, the U.S. economy and the markets in which we operate.

Terrorist attacks, like those that occurred on September 11, 2001, have contributed to economic instability in the United States, and further acts of terrorism, violence or war could affect the markets in which we operate, our business and our expectations. Armed hostilities may increase, or terrorist attacks, or responses from the United States, may lead to further acts of terrorism and civil disturbances in the United States or elsewhere, which may further contribute to economic instability in the United States. These attacks or armed conflicts may affect our operations or those of our customers or suppliers and could impact our revenues, our production capability and our ability to complete contracts in a timely manner.

Table of Contents

Risks Related to Our Financial Results and Financing Plans

Actual results could differ from the estimates and assumptions that we use to prepare our financial statements.

To prepare financial statements in conformity with GAAP, management is required to make estimates and assumptions, as of the date of the financial statements, which affect the reported values of assets and liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. Areas requiring significant estimates by our management include: contract costs and profits and application of percentage-of-completion accounting and revenue recognition of contract change order claims; provisions for uncollectible receivables and customer claims and recoveries of costs from subcontractors, suppliers and others; valuation of assets acquired and liabilities assumed in connection with business combinations; and accruals for estimated liabilities, including litigation and insurance reserves. Our actual results could differ from, and could require adjustments to, those estimates.

In particular, as is more fully discussed in Item 7 - “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies,” we recognize contract revenue using the percentage-of-completion method. Under this method, estimated contract revenue is recognized by applying the percentage of completion of the contract for the period to the total estimated revenue for the contract. Estimated contract losses are recognized in full when determined. Contract revenue and total cost estimates are reviewed and revised on a continuous basis as the work progresses and as change orders are initiated or approved, and adjustments based upon the percentage of completion are reflected in contract revenue in the accounting period when these estimates are revised. To the extent that these adjustments result in an increase, a reduction or an elimination of previously reported contract profit, we recognize a credit or a charge against current earnings, which could be material.

We may need to raise additional capital in the future for working capital, capital expenditures and/or acquisitions, and we may not be able to do so on favorable terms or at all, which would impair our ability to operate our business or achieve our growth objectives.

Our ability to obtain additional financing in the future will depend in part upon prevailing credit and equity market conditions, as well as conditions in our business and our operating results; such factors may adversely affect our efforts to arrange additional financing on terms satisfactory to us. We have pledged the proceeds and other rights under our construction contracts to our bond surety, and we have pledged substantially all of our other assets as collateral in connection with our credit facility and mortgage debt. As a result, we may have difficulty in obtaining additional financing in the future if such financing requires us to pledge assets as collateral. In addition, under our credit facility, we must obtain the consent of our lenders to incur any amount of additional debt from other sources (subject to certain exceptions). If future financing is obtained by the issuance of additional shares of common stock, our stockholders may suffer dilution. If adequate funds are not available, or are not available on acceptable terms, we may not be able to make future investments, take advantage of acquisitions or other opportunities, or respond to competitive challenges.

We are subject to financial and other covenants under our credit facility that could limit our flexibility in managing our business.

We have a credit facility that restricts us from engaging in certain activities, including restrictions on our ability (subject to certain exceptions) to:

- make distributions, pay dividends and buy back shares;
- incur liens or encumbrances;

- incur indebtedness;
- guarantee obligations;
- dispose of a material portion of assets or otherwise engage in a merger with a third party;
- make acquisitions; and
- incur losses for two consecutive quarters.

Table of Contents

Our credit facility contains financial covenants that require us to maintain specified fixed charge coverage ratios, asset ratios and leverage ratios, and to maintain specified levels of tangible net worth. Our ability to borrow funds for any purpose will depend on our satisfying these tests. If we are unable to meet the terms of the financial covenants or fail to comply with any of the other restrictions contained in our credit facility, an event of default could occur. An event of default, if not waived by our lenders, could result in the acceleration of any outstanding indebtedness, causing such debt to become immediately due and payable. If such an acceleration occurs, we may not be able to repay such indebtedness on a timely basis. Acceleration of our credit facility could result in foreclosure on and loss of our operating assets. In the event of such foreclosure, we would be unable to conduct our business and forced to discontinue operations.

Item 1B. Unresolved Staff Comments.

None

Item 2. Properties.

We own our 25,304 square-foot headquarters office building in Houston, Texas, which is located on a seven-acre parcel of land on which our Texas equipment repair center is also located. We also own land in Dallas and San Antonio on which we plan to construct regional offices and repair facilities. Pending completion of these regional offices, we lease office facilities in these locations. In order to complete most contracts in Texas, we lease small parcels of real estate near the site of a contract job site to store materials, locate equipment, conduct concrete crushing and pugging operations, and provide offices for the contracting customer, its representatives and our employees.

For our Nevada operations, we lease office space in Reno, Nevada, and we have an office and repair facilities located on a forty-five acre parcel of land in Lovelock, Nevada. We also lease the right to mine stone and sand at a quarry in Carson City, Nevada. Unlike in Texas where we acquire aggregates from third-party suppliers, in Nevada, we generally source and produce our own aggregates, either from the Carson City quarry or from other sources near job sites where we enter into short-term leases to acquire the aggregates necessary for the job. In order to complete most contracts in Nevada, we also lease small parcels of real estate near the site of a contract job site to store materials, locate equipment, and provide offices for the contracting customer, its representatives and our employees.

Item 3. Legal Proceedings.

We are and may in the future be involved as a party to various legal proceedings that are incidental to the ordinary course of business. We regularly analyze current information about these proceedings and, as necessary, provide accruals for probable liabilities on the eventual disposition of these matters.

In the opinion of management, after consultation with legal counsel, there are currently no threatened or pending legal matters that would reasonably be expected to have a material adverse impact on our consolidated results of operations, financial position or cash flows.

Item 4. Submission of Matters to a Vote of Security Holders.

None

Table of Contents

PART II

Item 5. Market for the Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities..

The Company's common stock is traded on the NASDAQ Global Select Market ("NGS"). The table below shows the market high and low closing sales prices of the common stock for 2007 and 2008 by quarter and for the period from January 1, through February 28, 2009.

	High	Low
Year Ended December 31, 2007		
First Quarter	$22.74	$17.42
Second Quarter	$23.86	$18.90
Third Quarter	$23.97	$18.64
Fourth Quarter	$26.60	$20.45
Year Ended December 31, 2008		
First Quarter	$21.84	$16.37
Second Quarter	$21.02	$18.70
Third Quarter	$20.80	$16.16
Fourth Quarter	$19.30	$9.40
January 1 through February 28, 2009	$19.69	$15.32

On February 28, 2009, there were approximately 1,181 holders of record of our common stock.

Dividend Policy. We have never paid any cash dividends on our common stock. For the foreseeable future, we intend to retain any earnings in our business, and we do not anticipate paying any cash dividends. Whether or not we declare any dividends will be at the discretion of the Board of Directors considering then-existing conditions, including the Company's financial condition and results of operations, capital requirements, bonding prospects, contractual restrictions (including those under the Company's Credit Facility) business prospects and other factors that our Board of Directors considers relevant.

Equity Compensation Plan Information. Certain information about the Company's equity compensation plans is set forth in Item 12. — Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

Performance Graph. The following graph compares the percentage change in the Company's cumulative total stockholder return on its common stock for the last five years with the Dow Jones US Index, a broad market index, and the Dow Jones US Heavy Construction Index, a group of companies whose marketing strategy is focused on a limited product line, such as civil construction. Both indices are published in The Wall Street Journal.

The returns are calculated assuming that an investment with a value of $100 was made in the Company's common stock and in each index at the end of 2003 and that all dividends were reinvested in additional shares of common stock; however, the Company has paid no dividends during the periods shown. The graph lines merely connect the measuring dates and do not reflect fluctuations between those dates. The stock performance shown on the graph is not intended to be indicative of future stock performance.

Table of Contents

	December 2003	December 2004	December 2005	December 2006	December 2007	December 2008
Sterling Construction Company, Inc	100.00	114.57	371.52	480.35	481.68	409.05
Dow Jones US	100.00	112.01	119.10	137.64	145.91	91.69
Dow Jones US Heavy Construction	100.00	121.26	175.23	218.58	415.21	186.34

Table of Contents

Item 6. Selected Financial Data.

The following table sets forth selected financial and other data of the Company and its subsidiaries and should be read in conjunction with both Item 7. —Management's Discussion and Analysis of Financial Condition and Results of Operations, which follows, and Item 8. — Financial Statements and Supplementary Data.

	Year Ended December 31				
	2008	2007	2006	2005	2004
	(Amounts in thousands except per-share data)				
Operating Results:					
Revenues	$ 415,074	$ 306,220	$ 249,348	$ 219,439	$ 132,478
Income from continuing operations before income taxes andminority interest	28,999	22,396	19,204	13,329	4,109
Income tax (expense)/benefit	(10,025)	(7,890)	(6,566)	(2,788)	2,134
Minority interest	(908)	(62)	--	--	(962)
Income from continuing operations	18,066	14,444	12,638	10,541	5,281
Income (loss) from discontinued operations, including gain on sale in 2006			682	559	372
Net income	$ 18,066	$ 14,444	$ 13,320	$ 11,100	$ 5,653
Basic and diluted per share amounts:					
Basic earnings per share from -					
Continuing operations	$ 1.38	$ 1.31	$ 1.19	$ 1.36	$ 0.99
Discontinued operations	--	--	$ 0.06	$ 0.07	$ 0.07
Basic earnings per share	$ 1.38	$ 1.31	$ 1.25	$ 1.43	$ 1.06
Basic weighted average shares outstanding	13,120	11,044	10,583	7,775	5,343
Diluted earnings per share from -					
Continuing operations	$ 1.32	$ 1.22	$ 1.08	$ 1.11	$ 0.75
Discontinued operations	--	--	$ 0.06	$ 0.05	$ 0.05
Diluted earnings per share	$ 1.32	$ 1.22	$ 1.14	$ 1.16	$ 0.80
Diluted weighted average shares outstanding	13,702	11,836	11,714	9,538	7,028
Cash dividends declared	—	—	—	—	—
Balance Sheet:					
Total assets	$ 289,615	$ 274,515	$ 167,772	$ 118,455	$ 89,544
Long-term debt	55,483	65,556	30,659	14,570	21,979
Equity	159,116	138,612	90,991	48,612	35,208
Book value per share of outstanding common stock	$ 12.07	$ 10.66	$ 8.37	$ 5.95	$ 4.77
Shares outstanding	13,185	13,007	10,875	8,165	7,379

Table of Contents

In January 2006 the Company completed a public offering of approximately 2.0 million shares of its common stock at $15.00 per share. The Company received proceeds, net of underwriting commissions, of approximately $28.0 million ($13.95 per share) and paid approximately $907,000 in related offering expenses. In addition, the Company received approximately $484,000 from the exercise of warrants and options to purchase 321,758 shares in December 2005. These shares were sold by the option and warrant holders in the offering. From the proceeds of the offering, the Company repaid its outstanding promissory notes and related interest aggregating approximately $5.5 million to the executive management, directors and former directors.

During 2006, the Company utilized part of the offering proceeds to purchase additional capital equipment for the construction business and to replenish funds that had been used for the 2006 acquisition of a drill shaft business.

In December 2007, the Company completed an additional public offering of 1.84 million shares of its common stock at $20.00 per share. The Company received proceeds, net of underwriting commissions, of approximately $35.0 million ($19.00 per share) and paid approximately $0.5 million in related offering expenses. Between the purchase date of RHB and the 2007 public offering of stock, the Company used the proceeds from the sale of its investments in short-term securities and cash provided by operations to reduce the Credit Facility borrowings used to purchase RHB by $22.4 million. The proceeds of the public stock offering were used to replenish the investment in short-term securities.

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operation.

Overview

For an overview of the Company's business and its associated risks, see Item 1. Business and Item 1A. Risk Factors.

Critical Accounting Policies

Our significant accounting policies are described in Note 1 of Notes to Consolidated Financial Statements for the year ended December 31, 2008.

Use of Estimates.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Our business involves making significant estimates and assumptions in the normal course of business relating to our contracts due to, among other things, different project scopes and specifications, the long-term duration of our contract cycle and the type of contract utilized. Therefore, management believes that “Revenue Recognition” is the most important and critical accounting policy. The most significant estimates with regard to these financial statements relate to the estimating of total forecasted construction contract revenues, costs and profits in accordance with accounting for long-term contracts. Actual results could differ from these estimates and such differences could be material.

Our estimates of contract revenue and cost are highly detailed. We believe, based on our experience, that our current systems of management and accounting controls allow management to produce reliable estimates of total contract revenue and cost during any accounting period. However, many factors can and do change during a contract performance period, which can result in a change to contract profitability from one financial reporting period to another. Some of the factors that can adversely change the estimate of total contract revenue, cost and profit include differing site conditions (to the extent that contract remedies are unavailable), the failure of major material suppliers to deliver on time, the failure of subcontractors to perform as agreed, unusual weather conditions, our failure to achieve expected productivity and efficient use of labor and equipment and the inaccuracies of our original bid estimate. Because we have a large number of contracts in process at any given time, these changes in estimates can sometimes offset each other without affecting overall profitability. However, significant changes in cost estimates on larger, more complex projects can have a material impact on our financial statements and are reflected in our results of operations when they become known.

When recording revenue from change orders on contracts that have been approved as to scope but not price, we include in revenue an amount equal to the amount that we currently expect to recover from customers in relation to costs incurred by us for changes in contract specifications or designs, or other unanticipated additional costs. Revenue relating to change order claims is recognized only if it is probable that the revenue will be realized. When determining the likelihood of eventual recovery, we consider such factors as evaluation of entitlement, settlements reached to date and our experience with the customer. When new facts become known, an adjustment to the estimated recovery is made and reflected in the current period results.

Table of Contents

Revenue Recognition.

The majority of our contracts with our customers are “fixed unit price.” Under such contracts, we are committed to providing materials or services required by a contract at fixed unit prices (for example, dollars per cubic yard of concrete poured or per cubic yard of earth excavated). To minimize increases in the material prices and subcontracting costs used in submitting bids, we obtain firm quotations from our suppliers and subcontractors. After we are advised that our bid is the winning bid, we enter into firm contracts with most of our materials suppliers and sub-contractors, thereby mitigating the risk of future price variations affecting those contract costs. Such quotations do not include any quantity guarantees, and we therefore have no obligation for materials or subcontract services beyond those required to complete the respective contracts that we are awarded for which quotations have been provided. As a result, we have rarely been exposed to material price or availability risk on contracts in our contract backlog. Assuming performance by our suppliers and subcontractors, the principal remaining risks under our fixed price contracts relate to labor and equipment costs and productivity levels. Most of our state and municipal contracts provide for termination of the contract for the convenience of the owner, with provisions to pay us only for work performed through the date of termination.

We use the percentage of completion accounting method for construction contracts in accordance with the American Institute of Certified Public Accountants Statement of Position 81-1, “Accounting for Performance of Construction-Type and Certain Production-Type Contracts.” Revenue and earnings on construction contracts are recognized on the percentage of completion method in the ratio of costs incurred to estimated final costs. Revenue is recognized as costs are incurred in an amount equal to cost plus the related expected profit. Contract cost consists of direct costs on contracts, including labor and materials, amounts payable to subcontractors and equipment expense (primarily depreciation, fuel, maintenance and repairs). Depreciation is computed using the straight-line method for construction equipment. Contract cost is recorded as incurred, and revisions in contract revenue and cost estimates are reflected in the accounting period when known.

The accuracy of our revenue and profit recognition in a given period is dependent on the accuracy of our estimates of the cost to finish uncompleted contracts. Our cost estimates for all of our significant contracts use a highly detailed “bottom up” approach, and we believe our experience allows us to produce reliable estimates. However, our contracts can be highly complex, and in almost every case, the profit margin estimates for a contract will either increase or decrease to some extent from the amount that was originally estimated at the time of bid. Because we have a large number of contracts of varying levels of size and complexity in process at any given time, these changes in estimates can sometimes offset each other without materially impacting our overall profitability. However, large changes in revenue or cost estimates can have a significant effect on profitability.

There are a number of factors that can contribute to changes in estimates of contract cost and profitability. The most significant of these include the completeness and accuracy of the original bid, recognition of costs associated with scope changes, extended overhead due to customer-related and weather-related delays, subcontractor and supplier performance issues, site conditions that differ from those assumed in the original bid (to the extent contract remedies are unavailable), the availability and skill level of workers in the geographic location of the contract and changes in the availability and proximity of materials. The foregoing factors, as well as the stage of completion of contracts in process and the mix of contracts at different margins, may cause fluctuations in gross profit between periods, and these fluctuations may be significant.

Valuation of Long-Term Assets.

Long-lived assets, which include property, equipment and acquired identifiable intangible assets, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment evaluations involve management estimates of useful asset lives and future cash flows. Actual useful lives and cash flows could be different from those estimated by management, and this could have a material effect on operating results and financial position. In addition, we had goodwill with a carrying amount of approximately $57 million at December 31, 2008, which must be reviewed for impairment at least annually in accordance with Statement of Financial Accounting Standards No. 142, or SFAS 142. The impairment testing required by SFAS 142 requires considerable judgment, and an impairment charge may be required in the future. We completed our annual impairment review for goodwill during the fourth quarter of 2008, and it did not result in an impairment.

Income Taxes.

Deferred tax assets and liabilities are recognized based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. We regularly review our deferred tax assets for recoverability and, where necessary, establish a valuation allowance. Reflecting management's assessment of expected future operating profitability and expectation that the Company would utilize all remaining net operating loss carry forwards ("NOLs"), we eliminated our valuation allowance in 2005. We are subject to the alternative minimum tax (AMT). When we utilize our NOLs to offset taxable income, payment of AMT results in a reduction of our deferred tax liability.

Our deferred tax assets related to our NOLs for financial statement purposes were fully utilized during 2007. In addition to the utilization of those NOLs, we had available to us the excess tax benefit resulting from exercise of a significant number of non-qualified in-the-money options amounting to $1.2 million, which we expect to utilize in the preparation of our 2008 federal income tax return. Accordingly, because we will no longer have the significant offsets provided by the NOLs, a comparison of our future cash flows to our historic cash flows may not be meaningful.

On January 1, 2007, we adopted the provisions of FASB Interpretation No. 48, (FIN 48) which establishes the criteria that an individual tax position must meet for some or all of the benefits of that position to be recorded. Adoption of FIN 48 did not have a material impact on our consolidated financial statements.

Discontinued Operations.

In August 2005, our board of directors authorized management to sell our distribution business. In accordance with the provisions of SFAS 144, we determined in the third quarter of 2005 that the distribution business became a long-lived asset held for sale and a discontinued operation. In October 2006, we sold the distribution business to an industry-related buyer for gross proceeds of approximately $5.4 million. We recognized a pre-tax gain on the sale in 2006 of approximately $249,000, equal to $121,000 after taxes.

Table of Contents

Results of Operations

Fiscal Year Ended December 31, 2008 (2008) Compared with Fiscal Year Ended December 31, 2007 (2007).

	2008	2007	% Change
	(Dollar amounts in thousands)		
Revenues	$ 415,074	$ 306,220	35.5%
Gross profit	41,972	33,686	24.6
Gross margin	10.1%	11.0%	(8.2)
General and administrative expenses, net	(13,763)	(13,231)	4.0
Other income (loss)	(81)	549	(114.8)
Operating income	28,128	21,004	33.9
Operating margin	6.8%	6.9%	(1.5)
Interest income	1,070	1,669	(35.9)
Interest expense	(199)	(277)	28.2
Income before taxes	28,999	22,396	29.5
Income taxes	(10,025)	(7,890)	27.1
Minority interest in subsidiary	(908)	(62)	(1,364.5)
Net income	$ 18,066	$ 14,444	25.1
Contract backlog, end of year	$ 448,000	$ 450,000	(0.4)

Revenues. Revenues increased $109 million, or 35.5%, from 2007 to 2008. A majority of the increase was due to the revenues earned by our Nevada operations, acquired on October 31, 2007, which were included in the consolidated results of operations for the full year of 2008 versus only two months in 2007. The remainder of the increase in revenues is the result of an increase in work performed by our Texas operations as a result of better weather throughout 2008 than 2007. Management estimates that revenues would have been $10 to $12 million greater had our Houston operations not been interrupted by Hurricane Ike and its after effects in September, 2008. Additionally, one of our oil suppliers in Nevada filed for bankruptcy in July 2008 and failed to furnish contracted oil for our production of asphalt on two of our jobs-in-progress, which delayed job performance and deferred approximately $25.0 million of revenue into 2009. The Company has negotiated with NDOT and does not anticipate the profitability on these contracts will be materially impacted by this matter.

Contract receivables are directly related to revenues and include both amounts currently due and retainage. The increase of $6.2 million in contracts receivable to $60.6 million at December 31, 2008 versus 2007 is due to the increase in revenue for the year 2008. The days revenue in contract receivables is approximately 53 days and 65 days at December 31, 2008 and 2007, respectively. The days revenue in contract receivables would have been similar for the two years if the revenues of our Nevada operations had been included in our revenues for a full year in 2007.

Revenue in the fourth quarter of 2008 increased $21 million to $109 million versus 2007 for the same reasons as discussed above for the full year. See note 17 to the consolidated financial statements for unaudited quarterly financial information.

Table of Contents

Gross profit

Gross profit increased $8.3 million in 2008 over 2007. This was due to the contribution of our Nevada operations in 2008 and better weather in Texas during most of 2008 than during 2007 (other than for the period during Hurricane Ike), which allowed our crews and equipment to be more productive. While Hurricane Ike affected our work in 2008, a hurricane usually does not adversely affect our profitability as much as the consistent rainy periods we had in 2007. Our gross margin decreased in 2008 from 2007 because of operating inefficiencies on certain contracts in Texas, higher fuel costs and lower profit margins on certain contracts started in the last half of 2008. We expect the trend of lower profit margins on contracts awards to continue at least in the first half of 2009.

Gross profit in the fourth quarter of 2008 decreased $2.5 million or 21% from the same quarter in 2007. Gross profit was 13.7% of revenues in the 2007 fourth quarter versus 8.7% in the fourth quarter of 2008 as a result of some unusually profitable municipal projects being performed primarily in the 2007 fourth quarter. Without those projects, the gross margins for the 2007 fourth quarter would have been more in line with normal margins, although still somewhat better than that of the fourth quarter of 2008.

Contract Backlog

At December 31, 2008, our backlog of construction projects was $448 million, as compared to $450 million at December 31, 2007. We were awarded approximately $413 million of new projects and change orders and recognized $415 million of earned revenue in 2008. Approximately $69 million of the backlog at December 31, 2008 is expected to be completed after 2009. The decrease in backlog from 2007 was due to increased competition and economic conditions in certain of our markets.

While our business does not include residential and commercial infrastructure work, the severe fall-off in new projects in those markets in Nevada and to a lesser extent in Texas, has caused a softer bidding climate in our infrastructure markets and has caused some residential and commercial infrastructure contractors to bid on public sector transportation and water infrastructure projects, thus increasing competition and creating downward pressure on bid prices in our markets. These and other factors could adversely affect our ability to maintain or increase our backlog through successful bids for new projects and could adversely affect the profitability of new projects that we do obtain through successful bids.

Recent reductions in miles driven in the U.S. and more fuel efficient vehicles are reducing federal and state gasoline taxes and tolls collected. Additionally, the current credit crisis may limit the amount of state and local bonds that can be sold at reasonable terms. Further, the nationwide decline in home sales, the increase in foreclosures and a prolonged recession may result in decreases in user fees and property and sales taxes. These and other factors could adversely affect transportation and water infrastructure capital expenditures in our markets.

General and administrative expenses, and other income

General and administrative expenses, net, increased by $0.5 million in 2008 from 2007 primarily due to a full year of G&A at our Nevada operations offset by lower stock compensation expense.

Despite the increase in absolute G&A expenses, the percentage of G&A to revenue decreased to 3.3% in 2008 from 4.3% in 2007 as the Nevada operations' G&A is not as large a percentage of revenues as Sterling's G&A which includes corporate overhead and expenses associated with being a public company.

Other income decreased $0.6 million and consists of gains and losses on disposal of equipment which depends on, among other things, age and condition of equipment disposed of, insurance recoveries and the market for used equipment.

Operating income

Operating income increased $7.1 million due to the factors discussed above regarding gross profit and general and administrative expenses and other income.

Table of Contents

Interest income and expense

Net interest income was $0.5 million less for 2008 than 2007 due to a decrease in interest rates on cash and short-term investments combined with the imputed interest expense of $0.2 million on the put option related to the minority interest in RHB.

Income taxes

Our effective income tax rate for the year ended December 31, 2008 was 34.6% compared to 35.2% for 2007. The difference between the effective tax rate and the statutory tax rate is due to the portion of earnings of a subsidiary taxed to the minority interest owner partially offset by the revised Texas franchise tax which became effective July 1, 2007.

Minority interest in subsidiary

The increase of $0.8 million is due to the minority interest's share of the results of RHB included in the consolidated results of operations for a full year in 2008 versus two months in 2007.

Fiscal Year Ended December 31, 2007 (2007) Compared with Fiscal Year Ended December 31, 2006 (2006).

	2007		2006		% Change
	(Dollar amounts in thousands)				
Revenues	$	306,220	$	249,348	22.8%
Gross profit		33,686		28,547	18.0%
Gross margin		11.0%		11.4%	(3.5)%
General and administrative expenses, net		(13,231)		(10,825)	22.0%
Other income		549		276	98.9%
Operating income		21,004		17,998	16.8%
Operating margin		6.9%		7.2%	(4.2)%
Interest income		1,669		1,426	17.0%
Interest expense		(277)		(220)	26.5%
Income from continuing operations before taxes		22,396		19,204	16.4%
Income taxes		(7,890)		6,566	20.2%
Minority interest in subsidiary		(62)		--	100.0%
Net income from continuing operations		14,444		12,638	14.5%
Net income (loss) from discontinued operations, including gain on sale		--		682	(100.0)%
Net income	$	14,444	$	13,320	8.4%
Contract backlog, end of year	$	450,000	$	395,000	13.9%

Revenues. Revenues increased $57 million, or 23%, from 2006 to 2007 reflecting the effect of continued expansion of our construction fleet, addition of a concrete plant and addition of crews. Our workforce grew by 18% year-over-year, and we purchased over $36 million in property, plant and equipment, including that acquired in the purchase of RHB, within the twelve month period ending December 31, 2007.

The increased revenue came strictly from the state market resulting from the Company being the successful low bidder in the state market which was assisted by an improved bidding climate in 2006 due to a large state highway program and increased total funding in the Dallas and Houston areas. The improvement in the weather in the fourth quarter 2007 offset much of the lower than expected revenue of the first three quarters of 2007 due to heavy rainfall during those months. Due to seasonality of the Nevada market, the contracts of RHB had only a modest effect on revenues for the two months they were included in 2007 revenues.

Table of Contents

Contract receivables are directly related to revenues and include both amounts currently due and retainage. The increase of $11.6 million in contracts receivable to $54.4 million at December 31, 2007 versus 2006 is due to the increase in revenue for the year 2007. The days revenue in contract receivables is approximately 65 days and 62 days at December 31, 2007 and 2006, respectively. The increase in days revenue in contract receivables is primarily the result of the Nevada operations receivables at December 31, 2007.

Gross Profit. The improvement in gross profits in 2007 was due principally to the increase in revenues. The slight margin reduction was attributable to a decrease of margin in backlog due to poor weather for the first three quarters of the year, and an increase in sales from the state contracts which have historically had lower gross than municipal contracts.

State highway contracts generally allow us to achieve greater revenue and gross profit production from our equipment and work crews, although on average the gross margins on this work tend to be slightly lower than on our water infrastructure contracts in the municipal markets. The lower margins reflect proportionally larger material inputs in the state contracts as we typically receive lower margins on materials than on labor. Partially offsetting the margin reduction was our ability to continue to redesign some jobs, achieve incentive awards and maintain good execution levels during dry weather. Due to the large number of contracts in different stages of completion and in different locations, it is not practical to quantify the impact of each of these matters on revenues and gross profit.

Contract Backlog. The increase in contract backlog is related to the Nevada acquisition in 2007. There was $16 million included in our 2007 year-end backlog on which we were the apparent low bidder and have subsequently been officially awarded these contracts. Historically, subsequent non-awards of such low bids have not materially affected our backlog or financial condition.

General and Administrative Expenses, Net of Other Income and Expense. The increase in general and administrative expenses, or G&A, in 2007 was principally due to higher employee expenses, including an increase in staff, and higher professional fees. Despite these increases in G&A expenses in support of our growing business, our ratio of G&A expenses to revenue remained essentially unchanged from 2006 to 2007, at 4%.

Operating Income. The 2007 increase in operating income resulted principally from the higher revenues and gross profits as discussed above.

Interest Income and Expense. The interest income net of interest expense remained virtually unchanged from 2006 to 2007 given the high cash and short term investments maintained throughout the year and the offering completed in December 2007. A total of $53,000 of interest expense was capitalized as part of our office and shop expansion.

Income Taxes. Income taxes increased due to increased income, the Texas margin tax and an increase in the statutory tax rate.

Minority Interest. As discussed in Part I, Item 1. Business, on October 31, 2007, the Company acquired a 91.67% interest in RHB. The minority interest's share of RHB's income before income taxes was $62,000 for the two months ended December 31, 2007 that was included in the consolidated results of operations.

Net Income from Continuing Operations. The 2007 increase in net income from continuing operations was the result of the various factors discussed above.

Discontinued Operations, Net of Tax. Discontinued operations for 2006 represents the results of operations of our distribution business, which was operated by Steel City Products, LLC.

The distribution business was sold on October 27, 2006. The Company recorded proceeds from the sale of approximately $5.4 million and recorded a pre-tax gain on the sale of approximately $249,000 and recorded $128,000 in income tax expense related to that gain in 2006.

Table of Contents

Historical Cash Flows

The following table sets forth information about our cash flows for the years ended December 31, 2008, 2007 and 2006.

	Year Ended December 31,		
	2008	2007	2006
	(Amounts in thousands)		
Cash and cash equivalents (at end of period)	$ 55,305	$ 80,649	$ 28,466
Net cash provided by (used in)			
Continuing operations:			
Operating activities	26,721	29,542	23,089
Investing activities	(42,923)	(47,935)	(52,358)
Financing activities	(9,142)	70,576	35,468
Discontinued operations			
Operating activities	--	--	495
Investing activities	--	--	4,739
Financing activities	--	--	(5,357)
Supplementary information:			
Capital expenditures	19,896	26,319	24,849
Working capital (at end of period)	95,123	82,063	62,874

Operating Activities

Significant non-cash items included in operating activities are:

- depreciation and amortization, which for 2008 totaled $13.2 million, an increase of $3.6 million from 2007 and $6.2 million from 2006, as a result of the continued increase in the size of our construction fleet in recent years and a full year's depreciation on equipment purchased in the RHB acquisition on October 31, 2007;
- deferred tax expense was $8.9 million, $6.6 million and $6.3 million in 2008, 2007 and 2006, respectively, mainly attributable to accelerated depreciation methods used on equipment for tax purposes and amortization for tax return purposes of goodwill arising in the acquisition of RHB.

Besides net income of $18.1 million and the non-cash items discussed above, other significant components of cash flows from operations are as follows:

- contracts receivable increased by $6.2 million in the current year due to the increase in revenues of $109 million, including those of the Nevada operations, as compared to an increase of $6.6 million in 2007 which was also due to an increase in revenue and a higher level of customer retentions;
- the increase in cost and estimated earnings in excess of billings on uncompleted contracts of $3.8 million as of December 31, 2008, versus a decrease of $0.6 million as of December 31, 2007, which was due to an increase in the volume of materials purchased for certain projects at December 31, 2008, but not billed to the customer until 2009 and timing of other billings.
- accounts payable decreased by $1.1 million in 2008 and increased $6.1 million in 2007 as a result of changes in the volume of materials and sub-contractor services purchased in later months of each period.

Table of Contents

Investing activities

Expenditures for the replacement of certain equipment and to expand our construction fleet and office and shop facilities totaled $19.9 million in 2008, compared with a total of $26.3 million of property and equipment purchases in 2007. Capital equipment is acquired as needed to support work crews required by increased backlog and to replace retiring equipment. The decrease in capital expenditures in 2008 was principally due to management's cautious view regarding certain of the Company's markets in 2009 and current economic uncertainties. Unless such factors change, management expects capital expenditures in 2009 to be equal to or less than in 2008.

During the twelve months ended December 31, 2008, the Company had purchases of short-term securities of $24.3 million versus a net reduction of $26.1 million in 2007 primarily due to the longer term of the securities purchased.

In October 2007, we purchased a 91.67% equity interest in RHB which we acquired for a net cash purchase price of $49.3 million in order to expand our construction operations to Nevada.

Financing activities

Financing activities in 2008 primarily reflect a reduction of $10.0 million in borrowings under our $75.0 million Credit Facility as compared to an increase of $35.0 million of borrowings in 2007. The amount of borrowings under the Credit Facility is based on the Company's expectations of working capital requirements.

Additionally, the Company sold common stock in 2007 and 2006 for net proceeds of $34.5 million and $27.0 million, respectively.

Liquidity

The level of working capital required for our construction business varies due to fluctuations in:

- customer receivables and contract retentions;
- costs and estimated earnings in excess of billings;
- billings in excess of costs and estimated earnings;
- the size and status of contract mobilization payments and progress billings;
- the amounts owed to suppliers and subcontractors.

Some of these fluctuations can be significant.

As of December 31, 2008, we had working capital of $95.1 million, an increase of $13.1 million over December 31, 2007. Increasing working capital is an important element in expanding our bonding capacity, which enables us to bid on larger and longer-lived projects. The increase in working capital was mainly the result of net income plus depreciation and deferred tax expense totaling $40.2 million reduced by purchases of property and equipment of $19.9 million and net repayment of debt of $10 million.

The Company believes that it has sufficient liquid financial resources, including the unused portion of its Credit Facility, to fund its requirements for the next twelve months of operations, including its bonding requirements, and expects no other material changes in its liquidity.

Sources of Capital

In addition to our available cash and cash equivalents, short term investments balances and cash provided by operations, we use borrowings under our Credit Facility with Comerica Bank to finance our capital expenditures and working capital needs.

The financial markets have recently experienced substantial volatility as a result of disruptions in the credit markets. However, to date we have not experienced any difficulty in borrowing under our Credit Facility or any change in its terms.

Table of Contents

We have a $75.0 million Credit Facility with a bank syndicate for which Comerica Bank is a participant and agent. The Credit Facility entered into on October 31, 2007 replaced a similar $35.0 million revolver that had been renewed in April 2006. The Credit Facility has a maturity date of October 31, 2012, and is secured by all assets of the Company, other than proceeds and other rights under our construction contracts which are pledged to our bond surety. Borrowings under the Credit Facility were used to finance the RHB acquisition, repay indebtedness outstanding under the Revolver, and finance working capital. At December 31, 2008, the aggregate borrowings outstanding under the Credit Facility were $55.0 million, and the aggregate amount of letters of credit outstanding under the Credit Facility was $1.8 million, which reduces availability under the Credit Facility. Availability under the Credit Facility was, therefore, $18.2 million.

The Credit Facility is subject to our compliance with certain covenants, including financial covenants relating to fixed charges, leverage, tangible net worth, asset coverage and consolidated net losses.

The Credit Facility contains restrictions on our ability to:

- Make distributions and dividends;
- Incur liens and encumbrances;
- Incur further indebtedness;
- Guarantee obligations;
- Dispose of a material portion of assets or merge with a third party;
- Incur negative income for two consecutive quarters.

The Company was in compliance with all covenants under the Credit Facility as of December 31, 2008.

The unpaid principal balance of each prime-based loan will bear interest at a variable rate equal to Comerica's prime rate plus an amount ranging from 0% to 0.50% depending on the pricing leverage ratio that we achieve. If we achieve a pricing leverage ratio of (a) less than 1.00 to 1.00; (b) equal to or greater than 1.00 to 1.00 but less than 1.75 to 1.00; or (c) greater than or equal to 1.75 to 1.00, then the applicable prime margins will be 0.0%, 0.25% or 0.50%, respectively. The interest rate on funds borrowed under this revolver during the year ended December 31, 2008 ranged from 3.5% to 7.5%.

Management believes that the new Credit Facility will provide adequate funding for the Company's working capital, debt service and capital expenditure requirements, including seasonal fluctuations at least through December 31, 2009.

At our election, the loans under the new Credit Facility bear interest at either a LIBOR-based interest rate or a prime-based interest rate. The unpaid principal balance of each LIBOR-based loan bears interest at a variable rate equal to LIBOR plus an amount ranging from 1.25% to 2.25% depending on the pricing leverage ratio that we achieve. The "pricing leverage ratio" is determined by the ratio of our average total debt, less cash and cash equivalents, to earnings before interest, taxes, depreciation and amortization ("EBITDA") that we achieve on a rolling four-quarter basis. The pricing leverage ratio is measured quarterly. If we achieve a pricing leverage ratio of (a) less than 1.00 to 1.00; (b) equal to or greater than 1.00 to 1.00 but less than 1.75 to 1.00; or (c) greater than or equal to 1.75 to 1.00, then the applicable LIBOR margins will be 1.25%, 1.75% or 2.25%, respectively. Interest on LIBOR-based loans is payable at the end of the relevant LIBOR interest period, which must be one, two, three or six months. The new Credit Facility is subject to our compliance with certain covenants, including financial covenants relating to fixed charges, leverage, tangible net worth, asset coverage and consolidated net losses.

Table of Contents

Mortgages

In 2001 we completed the construction of a new headquarters building on land owned by us adjacent to our equipment repair facility in Houston. The building was financed principally through an additional mortgage of $1.1 million on the land and facilities at a floating interest rate which at December 31, 2008 was 3.5% per annum, repayable over 15 years.

Uses of Capital

Contractual Obligations.

The following table sets forth our fixed, non-cancelable obligations at December 31, 2008.

	Payments due by Period				
	Total	Less Than One Year	1—3 Years	4—5 Years	More Than 5 Years
			(Amounts in thousands)		
Credit Facility	$ 55,000	$ —	$ —	$ 55,000	$ —
Operating leases	2,146	721	1,425	--	—
Mortgages	556	73	220	147	116
	$ 57,702	$ 794	$ 1,645	$ 55,147	$ 116

Our obligations for interest are not included in the table above as these amounts vary according to the levels of debt outstanding at any time. Interest on our Credit Facility is paid monthly and fluctuates with the balances outstanding during the year, as well as with fluctuations in interest rates. In 2008 interest on the Credit Facility was approximately $91,000. The mortgages are expected to have future annual interest expense payments of approximately $18,000 in less than one year, $40,000 in one to three years, $14,000 in four to five years and $3,000 for all years thereafter.

To manage risks of changes in the material prices and subcontracting costs used in submitting bids for construction contracts, we generally obtain firm quotations from our suppliers and subcontractors before submitting a bid. These quotations do not include any quantity guarantees, and we have no obligation for materials or subcontract services beyond those required to complete the contracts that we are awarded for which quotations have been provided.

As is customary in the construction business, we are required to provide surety bonds to secure our performance under construction contracts. Our ability to obtain surety bonds primarily depends upon our capitalization, working capital, past performance, management expertise and reputation and certain external factors, including the overall capacity of the surety market. Surety companies consider such factors in relationship to the amount of our backlog and their underwriting standards, which may change from time to time. Events that affect the insurance and bonding markets generally may result in bonding becoming more difficult to obtain in the future, or being available only at a significantly greater cost. We have pledged all proceeds and other rights under our construction contracts to our bond surety to the surety company.

Capital Expenditures.

Our capital expenditures during 2008 were $19.9 million, and during 2007 were $36.0 million including property, plant and equipment acquired with the purchase of RHB. In 2009 we expect that our capital expenditure spending will be equal to or less than the 2008 level due to management's cautious view regarding certain of the Company's markets and current economic uncertainties.

Table of Contents

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

New Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board (FASB) revised Statement of Financial Accounting Standards No. 141, "Business Combinations" (SFAS 141(R)). This Statement establishes principles and requirements for how the acquirer: (a) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree; (b) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase and (c) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. Also, under SFAS 141(R), all direct costs of the business combination must be charged to expense on the financial statements of the acquirer as incurred. SFAS 141(R) revises previous guidance as to the recording of post-combination restructuring plan costs by requiring the acquirer to record such costs separately from the business combination. This statement is effective for acquisitions occurring on or after January 1, 2009, with early adoption not permitted. Unless the Company enters into another business combination, there will be no effect on future financial statements of SFAS 141(R) when adopted.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" (SFAS 157) which establishes a framework for measuring fair value and requires expanded disclosure about the information used to measure fair value. The statement applies whenever other statements require or permit assets or liabilities to be measured at fair value, and does not expand the use of fair value accounting in any new circumstances. In February 2008, the FASB delayed the effective date by which companies must adopt the provisions of SFAS 157 for nonfinancial assets and liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The new effective date of SFAS 157 deferred implementation to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years. The adoption of this standard is not anticipated to have a material impact on our financial position, results of operations, or cash flows.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment to FASB Statement No. 115" ("SFAS No. 159"). This statement allows a company to irrevocably elect fair value as a measurement attribute for certain financial assets and financial liabilities with changes in fair value recognized in the results of operations. SFAS No. 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. Adoption of this pronouncement did not have a material impact on the Company's results of operations and financial position.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, "Non-controlling Interests in Consolidated Financial Statements" (SFAS 160). SFAS 160 clarifies previous guidance on how consolidated entities should account for and report non-controlling interests in consolidated subsidiaries. The statement standardizes the presentation of non-controlling ("minority interests") for both the consolidated balance sheet and income statement. This Statement is effective for the Company for fiscal years beginning on or after January 1, 2009, and all interim periods within that fiscal year, with early adoption not permitted. When this Statement is adopted, the minority interest in any subsequent acquisitions that does not contain a put will be reported as a separate component of stockholders' equity instead of a liability and net income will be segregated between net income attributable to common stockholders and non-controlling interests.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk.

Changes in interest rates are one of our sources of market risks. At December 31, 2008, $55 million of our outstanding indebtedness was at floating interest rates. Based on our average debt outstanding during 2008, we estimate that an increase of 1.0% in the interest rate would have resulted in an increase in our interest expense of approximately $15,000 in 2008.

To manage risks of changes in material prices and subcontracting costs used in tendering bids for construction contracts, we obtain firm price quotations from our suppliers, except for fuel, and subcontractors before submitting a bid. These quotations do not include any quantity guarantees, and we have no obligation for materials or subcontract services beyond those required to complete the respective contracts that we are awarded for which quotations have been provided.

During 2009, we have started a process of investing in certain securities, the assets of which are a crude oil commodity pool. We believe that the gains and losses on these securities will tend to offset increases and decreases in the price we pay for diesel and gasoline fuel and reduce the volatility of such fuel costs in our operations. There can, however, be no assurance that this process will be successful.

Table of Contents

ItemFinancial Statements and Supplementary Data.
8.

Financial statements start on page F-1.

ItemChanges in and Disagreements with Accountants on Accounting and Financial Disclosure.
9.

None

ItemControls and Procedures.
9A.

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to the issuer's management, including the principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

The Company's principal executive officer and principal financial officer reviewed and evaluated the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on that evaluation, the Company's principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures were effective at December 31, 2008 to ensure that the information required to be disclosed by the Company in this Annual Report on Form 10-K is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and is accumulated and communicated to the Company's management including the principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

Management's Report on Internal Control over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f)) under the Securities Exchange Act of 1934). Under the supervision and with the participation of the Company's management, including the principal executive officer and principal financial officer, the Company conducted an evaluation of the effectiveness of internal control over financial reporting at December 31, 2008. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework. The Company's management has concluded that, at December 31, 2008, the Company's internal control over financial reporting is effective based on these criteria.

Our internal control over financial reporting has been audited by Grant Thornton LLP, an independent registered public accounting firm, as stated in their report included herein.

Changes in Internal Control over Financial Reporting

We maintain a system of internal control over financial reporting that is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States. Based on the most recent evaluation, we have concluded that no significant changes in our internal control over financial reporting occurred during the last fiscal quarter that have materially affected or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Internal control over financial reporting may not prevent or detect all errors and all fraud. Also, projections of any evaluation of effectiveness of internal control to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

ItemOther Information.
9B.

None

Table of Contents

PART III

Item 10. Directors and Executive Officers of the Registrant.

Directors. The following table sets forth the name and age of each of the Company's current directors and the positions each held on February 16, 2009.

Name	Position	Age	Director Since	Year Term of Office Expires
Patrick T. Manning	Chairman of the Board of Directors & Chief Executive Officer	63	2001	2011
Joseph P. Harper, Sr.	President, Treasurer & Chief Operating Officer, Director	63	2001	2011
John D. Abernathy	Director	71	1994	2009
Robert W. Frickel	Director	65	2001	2009
Donald P. Fusilli, Jr.	Director	57	2007	2010
Maarten D. Hemsley	Director	59	1998	2010
Christopher H. B. Mills	Director	56	2001	2010
Milton L. Scott	Director	52	2005	2009
David R. A. Steadman	Director	71	2005	2009

Patrick T. Manning. Mr. Manning joined the predecessor of Texas Sterling Construction Co., the Company's Texas construction subsidiary, which along with its predecessors is referred to as TSC, in 1971 and led its move from Detroit, Michigan into the Houston market in 1978. He has been TSC's President and Chief Executive Officer since 1998 and Chairman of the Board of Directors and Chief Executive Officer of the Company since July 2001. Mr. Manning has served on a variety of construction industry committees, including the Gulf Coast Trenchless Association and the Houston Contractors' Association, where he served as a member of the board of directors and as President from 1987 to 1993. He attended Michigan State University from 1969 to 1972.

Joseph P. Harper, Sr. Mr. Harper has been employed by TSC since 1972. He was Chief Financial Officer of TSC for approximately 25 years until August 2004, when he became Treasurer of TSC. In addition to his financial responsibilities, Mr. Harper has performed both estimating and project management functions. Mr. Harper has been a director and the Company's President and Chief Operating Officer since July 2001, and in May 2006 was elected Treasurer. Mr. Harper is a certified public accountant.

John D. Abernathy. Mr. Abernathy was Chief Operating Officer of Patton Boggs LLP, a Washington D.C. law firm, from January 1995 through May 2004 when he retired. He is also a director of Par Pharmaceutical Companies, Inc., a New York Stock Exchange-listed company that manufactures generic and specialty drugs, and Neuro-Hitech, Inc., a company that manufactures generic drugs, the shares of which are traded on the over-the-counter market. Mr. Abernathy is a certified public accountant. In December 2005, Mr. Abernathy was first elected Lead Director by the independent members of the Board of Directors.

Robert W. Frickel. Mr. Frickel is the founder and President of R.W. Frickel Company, P.C., a public accounting firm that provides audit, tax and consulting services primarily to companies in the construction industry. Prior to the founding of R.W. Frickel Company in 1974, Mr. Frickel was employed by Ernst & Ernst. Mr. Frickel is a certified public accountant.

Donald P. Fusilli, Jr. Mr. Fusilli is presently the principal of the Telum Group, a professional consulting firm. From January 2008 to January 2009, he was the Chief Executive Officer of a marine services subsidiary of David Evans and Associates, Inc., a company that provides underwater mapping and analysis services. From May 1973 until September 2006, Mr. Fusilli served in a variety of capacities at Michael Baker Corporation, a public company listed on the American Stock Exchange that provides a variety of professional engineering services spanning the complete life cycle of infrastructure and managed asset projects. Mr. Fusilli joined Michael Baker Corporation as an engineer and over the course of his career rose to president and chief executive officer in April 2001. From September 2006 to January 2008, Mr. Fusilli was an independent consultant providing strategic planning, marketing development and operations management services. Mr. Fusilli is a director of RTI International Metals, Inc., a New York Stock Exchange-listed company that is a leading U.S. producer of titanium mill products and fabricated metal components. He holds a Civil Engineering degree from Villanova University, a Juris Doctor degree from Duquesne University School of Law and attended the Advanced Management Program at the Harvard Business School.

Maarten D. Hemsley. Mr. Hemsley served as the Company's President and Chief Operating Officer from 1988 until 2001, and as Chief Financial Officer from 1998 until August 2007. From January 2001 to May 2002, Mr. Hemsley was also a consultant to, and thereafter has been an employee of, JO Hambro Capital Management Limited, which is part of JO Hambro Capital Management Group Limited, or JOHCMG, an investment management company based in the United Kingdom. Mr. Hemsley has served since 2001 as Fund Manager of JOHCMG's Leisure & Media Venture Capital Trust, plc, and since February 2005, as Senior Fund Manager of its Trident Private Equity II LLP investment fund. Mr. Hemsley is a director of Tech/Ops Sevcon, Inc., a U.S. public company that manufactures electronic controls for electric vehicles and other equipment, and of a number of privately-held companies in the United Kingdom. Mr. Hemsley is a Fellow of the Institute of Chartered Accountants in England and Wales.

Christopher H. B. Mills. Mr. Mills is a director of JOHCMG. Prior to founding JOHCMG in 1993, Mr. Mills was employed by Montagu Investment Management and its successor company, Invesco MIM, as an investment manager and director, from 1975 to 1993. He is the Chief Executive of North Atlantic Smaller Companies Investment Trust plc, which is a part of JOHCMG and a 3.82% holder of the Company's common stock. Mr. Mills is a director of two U.S. public companies, W-H Energy Services, Inc., a New York Stock Exchange-listed company that is in the oilfield services industry, and SunLink Healthcare Systems, Inc., a publicly-traded, non-urban community healthcare provider for seven hospitals and related businesses in four states in the Southwest and Midwest. Mr. Mills also serves as a director of a number of public and private companies outside of the U.S. in which JOHCMG funds have investments.

Milton L. Scott. Mr. Scott is Chairman and Chief Executive Officer of the Tagos Group, a strategic advisory and services company in supply chain management, transportation and logistics, and integrated supply. He was previously associated with Complete Energy Holdings, LLC, a company of which he was Managing Director until January 2006 and which he co-founded in January 2004 to acquire, own and operate power generation assets in the United States. From March 2003 to January 2004, Mr. Scott was a Managing Director of The StoneCap Group, an entity formed to acquire, own and operate power generation assets. From October 1999 to November 2002, Mr. Scott served as Executive Vice President and Chief Administrative Officer at Dynegy Inc., a public company that was a market leader in power distribution, marketing and trading of gas, power and other commodities, midstream services and electric distribution. From July 1977 to October 1999, Mr. Scott was with the Houston office of Arthur Andersen LLP, a public accounting firm, where he served as partner in charge of the Southwest Region Technology and Communications practice.

David R. A. Steadman. Mr. Steadman is President of Atlantic Management Associates, Inc., a management services and investment group. An engineer by profession, Mr. Steadman served as Vice President of the Raytheon Company from 1980 until 1987 where he was responsible for commercial telecommunications and data systems businesses in addition to setting up a corporate venture capital portfolio. Subsequent to that and until 1989, Mr. Steadman was Chairman and Chief Executive Officer of GCA Corporation, a manufacturer of semiconductor production equipment. Mr. Steadman serves as a director of Aavid Thermal Technologies, Inc., a provider of thermal management solutions for the electronics industry, a privately-held company. Mr. Steadman also serves as Chairman of Tech/Ops Sevcon, Inc., a public company that manufactures electronic controls for electric vehicles and other equipment. Mr. Steadman is a Visiting Lecturer in Business Administration at the Darden School of the University of Virginia.

Executive Officers. In addition to Messrs. Manning and Harper, whose backgrounds are described above, the following are the Company's other executive officers:

James H. Allen, Jr. Mr. Allen became the Company's Senior Vice President & Chief Financial Officer in August 2007. He spent approximately 30 years with Arthur Andersen & Co., including 19 years as an audit and business advisory partner and as head of the firm's Houston office construction industry practice. After being retired for several years, he became chief financial officer of a process chemical manufacturer and served in that position for over three years prior to joining the Company. Mr. Allen is a certified public accountant.

Roger M. Barzun. Mr. Barzun has been the Company's Vice President, Secretary and General Counsel since August 1991. He was elected a Senior Vice President from May 1994 until July 2001 and again in March 2006. Mr. Barzun has been a lawyer since 1968 and is a member of the bar of both New York and Massachusetts. Mr. Barzun also serves as general counsel to other corporations from time to time on a part-time basis.

Section 16(a) Beneficial Ownership Reporting Compliance. Section 16(a) of the Exchange Act requires the Company's officers and directors, and persons who own more than 10% of the Company's equity securities, or insiders, to file with the Securities and Exchange Commission (SEC) reports of beneficial ownership of those securities and certain changes in beneficial ownership on Forms 3, 4 and 5, and to give the Company a copy of those reports.

Based solely upon a review of Forms 3 and 4 and amendments to them furnished to the Company during 2008, any Forms 5 and amendments to them furnished to the Company relating to 2008, and any written representations that no Form 5 is required, all Section 16(a) filing requirements applicable to the Company's insiders were satisfied except as follows:

In December 2008, Mr. Mills shared voting and investment power over 400,000 shares of the Company's common stock with North Atlantic Smaller Companies Investment Trust plc, or NASCIT, of which he is chief executive officer. Mr. Mills failed to timely file a Form 4 covering sales by NASCIT on December 5, 2008 of 39,400 shares. A Form 4 reporting that sale was filed with the SEC on December 12, 2008.

Table of Contents

Code of Ethics. The Company has adopted a Code of Business Conduct & Ethics that complies with SEC rules. The Code applies to all the officers and in-house counsel of the Company and its subsidiaries, and is posted on the Company's website at www.sterlingconstructionco.com.

The Audit Committee. The Company has a standing audit committee as defined in Section 3(a)(58)(A) of the Securities Exchange Act of 1934. The members of the Audit Committee are John D. Abernathy, Chairman, Donald P. Fusilli, Jr., and Milton L. Scott.

Each of the members of the Audit Committee is an independent director under the independence standards of both Nasdaq and the SEC. The Board of Directors has determined that each of Messrs. Abernathy and Scott is an audit committee financial expert. The independent members of the Board have appointed Mr. Abernathy Lead Director.

Item 11. Executive Compensation

Introduction

This Item 11 has two main parts. The first contains information about the compensation of the executive officers of the Company and the second contains information about the compensation of directors who are not also executive officers.

The Company is required under applicable rules and regulations to furnish information about the compensation of four of its top executive officers. Because these executive officers are named in the Summary Compensation Table for 2008 in this Item 11, they are sometimes referred to as the named executive officers. The named executive officers are as follows:

Patrick T. Manning	Chairman & Chief Executive Officer
Joseph P. Harper, Sr.	President, Treasurer & Chief Operating Officer
James H. Allen, Jr.	Senior Vice President & Chief Financial Officer
Roger M. Barzun	Senior Vice President, Secretary & General Counsel

The compensation of these executives, which is based on employment agreements between the Company and the executives, is described and discussed in the subsections listed below:

- The Compensation Discussion and Analysis, which covers how and why executive compensation was determined.
- The Employment Agreements of Named Executive Officers, which describes the important terms of the executives' employment agreements.
- The Potential Payments upon Termination or Change-in-Control, which as its name indicates, describes particular provisions of the executives' employment agreements relating to the termination of their employment and a change in control of the Company.
- The Summary Compensation Table for 2008, which shows the cash and equity compensation the Company paid to the named executive officers for 2008.
- The table of Grants of Plan-Based Awards for 2008, which shows details of any equity and non-equity awards made to the named executive officers for 2008 and describes the plans under which the Company made those awards.

- The table of Option Exercises and Stock Vested for 2008, which shows the number of shares the named executive officers purchased under their stock options in 2008 and the dollar value of the difference between the market value of the shares purchased on the date of purchase and the option exercise price.

- The table of Outstanding Equity Awards at December 31, 2008, which as its name indicates, shows the stock options held by the named executive officers at year's end and gives other details of their option awards.

Table of Contents

Compensation Discussion and Analysis

Introduction. This discussion and analysis of executive compensation is designed to show how and why the compensation of the named executive officers was determined. Their compensation is determined by the Compensation Committee of the Board of Directors, or the Committee, whose members are three independent directors of the Company.

Compensation Objectives. The Committee's compensation objectives for each of the named executive officers as well as for other management employees is to provide the employee with a rate of pay for the work he does that is appropriate in comparison to similar companies in the industry and that is considered fair by the executive and the Company; to give the executive a significant incentive to make the Company financially successful; and to give him an incentive to remain with the Company.

Employment Agreements. The Company believes that compensating an executive under an employment agreement has the benefit of assuring the executive of continuity, both as to his employment and the amounts and elements of his compensation. At the same time, an employment agreement gives the Company some assurance that the executive will remain with the Company for the duration of the agreement and enables the Company to budget salary costs over the term of the agreement. All elements of the compensation of the named executive officers are paid according to the terms of their employment agreements.

How the Terms of the Employment Agreements Were Determined. The agreements under which the Company compensated the executives in 2008 became effective as of July 2007, when the prior employment agreements of Messrs. Manning and Harper expired and when Mr. Allen was first employed by the Company. The Committee's starting point was a written salary and cash incentive bonus proposal made by Messrs. Manning and Harper for themselves and for the five senior managers of TSC. Mr. Allen had not then joined the Company. In connection with the proposal, Messrs. Manning and Harper stressed their belief in the importance of a team approach to compensation, an approach that is designed to avoid the disruptive effects of variations in compensation levels between managers of equal responsibility and importance to the Company. The Committee discussed the proposal in the course of several meetings. No member of senior management to be covered by the employment agreements, including Messrs Manning and Harper, was present at any of the Committee's deliberations and discussions.

Compensation Principles and Policies. In the course of their discussions, members of the Committee came to a consensus on the following general compensation principles as a guide for their further discussion of the compensation of Messrs. Manning, Harper and Allen as well as of the five senior managers of TSC:

- Compensation should consist of two main elements, base salary and cash incentive bonus to achieve all of the compensation objectives discussed above.

- Equity compensation should not be an element of compensation for executives who already hold a substantial number of shares of the Company's common stock or who already hold options to purchase a substantial number of shares of common stock, or both.

- The cash incentive bonus element of compensation should be divided into two parts: one part, 60%, of the incentive bonus should be based on the achievement by the Company, on a consolidated basis, of financial goals. The other part, 40%, should be based on the achievement by the executive of personal goals to be established annually in advance by the Committee in consultation with the executive.

- Perquisites such as car allowances, reimbursement of club dues and the like should not be an element of compensation because salaries are designed to be sufficient for the executive to pay these items personally.

- The Committee should determine at the end of each year the extent to which each of Messrs. Manning, Harper and Allen has achieved his personal goals, as provided in the Committee's charter.

- In determining individual compensation levels, the Committee should take into account, among other things, the following:

- The elimination of stock options as an element of compensation (except for Mr. Allen, who was a new employee in 2007.)

- The executives' existing salaries.

- Salaries of comparable executives in the industry.

Table of Contents

- Wage inflation from 2004 through 2007, to the extent applicable.
- The Company's growth since July 2004 when the prior employment agreements of Messrs. Manning and Harper became effective and the resulting increase in senior management responsibilities.
- The total amount that is appropriate for the Company to allocate to the compensation of the Company's senior management given the Company's size and industry.
- The elimination of perquisites.

Compensation Consultant. To assist them in evaluating management's proposed salary and bonus structure, in May 2007, the Committee authorized its Chairman to retain the services of Hay Group, a large firm that performs a number of consulting services, including the benchmarking of executive compensation. The Committee's Chairman instructed Hay Group to prepare an analysis of the levels of compensation payable under the July 2004 employment agreements to Messrs. Manning, Harper and the five senior managers of TSC, and to compare them to a representative group of similar companies. Mr. Allen joined the Company in July 2007 just before Hay Group's report was finished and as a result, its analysis did not cover his compensation.

The peer group was selected by Hay Group in consultation with the Chairman of the Committee and Messrs. Manning and Harper. The peer group consisted of eight engineering and construction companies with 2006 revenues of between $85 million and $651 million. The following is a list of companies in the peer group:

- Devcon International Corp.
- Furmanite Corporation
- Modtech Holdings Inc.
- Meadow Valley Corporation
- SPARTA, Inc. (Delaware)
- Great Lakes Dredge & Dock Company
- Insituform Technologies Inc.
- Michael Baker Corporation

The Committee determined that although these companies are in different areas of the construction and engineering industry, they present an appropriate range in size and types of construction-related businesses to which to compare the Company.

After distributing its report to members of the Committee, two representatives of Hay Group reviewed its findings in detail at a meeting of the Committee held at the end of July 2007. Hay Group performed no other services for the Committee. Because of the work Hay Group did for the Committee, the Board's Corporate Governance & Nominating Committee retained Hay Group to do a similar analysis and report relating to the compensation of the Company's non-employee directors.

Table of Contents

The following is a summary of the Hay Group's Executive Compensation Report, which was delivered to Committee members in mid 2007 and was based on financial information for calendar year 2006, the then most recently completed full fiscal year:

- Except for net income, the Company was at or about the median of the peer group in sales, assets, market capitalization and number of employees. In total shareholder return, growth in income before interest and taxes, and return on investment, the Company was ahead of the peer group.
- The Company's 2006 net income was above the peer group and its stockholders' equity was 135% of the peer-group median.
- Using the peer group, the base salaries of Messrs. Manning and Harper under their July 2004 agreements were 64% and 81%, of the median, respectively; the sum of their base salaries and annual incentive awards were 130% and 150% of the median, respectively; and their total direct compensation (which includes equity compensation) was 86% and 93% of the median, respectively.
- Using Hay Group's so called national general industry database updated to July 2007, the base salaries of Messrs. Manning and Harper under the July 2004 agreements were below the median, 91% and 81% respectively, but their total cash compensation was above the median, 144% and 132%, respectively.

The Committee concluded from these numbers that it is the financial success of the Company and the resulting incentive bonuses that results in the total compensation of Messrs. Manning and Harper to be above the median.

Compensation Levels. It was the consensus of the Committee that both the salary and cash incentive bonus levels of Messrs. Manning and Harper should be significantly above the peer-group median to reflect the following:

- The Company's excellent, above-median performance in net income and stockholders' equity;
- The growth of the Company since 2004 and the resulting increase in the complexity of the business; and
- The elimination of equity as an element of compensation.

To account for the elimination of long-standing perquisites, the Committee added $25,000 to the proposed base salaries of both executives. In addition, the Committee took into account the fact that under the accounting rules of FAS 123R, the elimination of equity compensation causes the proposed $3.41 million of total compensation for the seven-person management group consisting of Messrs. Manning, Harper and the five TSC senior managers, to be below the total of prior years.

Because of management's expressed desire for a team concept of compensation, the Committee agreed with the proposal of Messrs. Manning and Harper that their own salaries and cash incentive bonuses be the same, reflecting their belief that each has different but equal levels of responsibility and expertise.

The Committee determined that performance-based compensation, including deferred salary as described below, should be approximately equal to base salary. In the case of Mr. Allen, his performance-based compensation when combined with his equity compensation is approximately 60% of his base salary.

As noted above, Mr. Allen's compensation was not a subject of Hay Group's report because he joined the Company just before the report was presented. The Committee established his salary based on a number of factors, including Mr. Allen's thirty years of experience in Houston with a major public accounting firm, nineteen of those years consisting of concentration in the construction industry; his financial and business experience; the compensation package requested by Mr. Allen; and Committee members' own judgment of what is a reasonable level of compensation. The Committee granted him the stock option described below so that like other members of senior management, he would have a long-term equity interest in the Company. The Committee determined that Mr. Allen would be compensated under the same form of employment agreement as the one agreed upon with Messrs. Manning and Harper.

Table of Contents

Deferred Salary. The Committee's first inclination was to have cash incentive bonuses tied solely to a financial measurement found in the Company's annual audited financial statements. Mr. Harper advised the Committee that EBITDA was used in the past as a measure of financial performance because it was the number on which management believes that its performance has the most direct effect. Mr. Harper also noted that the threshold for bonus achievement was 75% instead of 100% of budgeted EBITDA because in the past, base salaries had been set at a relatively low level, a fact supported by the Hay Group report. The relatively easily achieved cash incentive bonus together with base salary was intended to yield fair base compensation, but was also intended to conserve cash by keeping salaries low in years in which the Company had especially poor financial performance and did not even achieve 75% of budgeted EBITDA.

The Committee agreed to maintain this concept, but determined that it would be better structured by revising the base salary arrangements. The Committee divided base salary into two parts; the larger part to be paid in periodic installments through the payroll system, or base payroll salary, and the balance to be deferred, or base deferred salary, to be paid in a lump sum after year end only if 75% of budgeted EBITDA is achieved. EBITDA is defined in the agreements as annual net income determined in accordance with generally accepted accounting principles —

Plus Interest expense for the period;

Plus Depreciation and amortization expense for the period;

Plus Federal and state income tax expense incurred for the period;

Plus Extraordinary items (to the extent negative) if any, for the period;

Minus Extraordinary items (to the extent positive) if any

Minus Interest income for the period; and

Minus Any fees paid to non-employee directors.

Cash Incentive Bonus. In keeping with its principle of basing cash incentive bonuses on the achievement of a financial measurement that can be determined by direct reference to the Company's audited annual financial statements, the Committee decided to base 60% of the bonus on achieving budgeted fully-diluted earnings per share in the belief that it is a measure that most directly affects a stockholder's investment in the Company, and 40% on the achievement of personal goals by the executives.

Termination Events. The obligations of the Company under the employment agreements in the event of the termination of the employment of the named executive officers or a change in control of the Company are described in detail in the section entitled Potential Payments Upon Termination or Change-in-Control, below.

The Committee's principle in setting termination provisions was based on the belief that absent a termination for cause, an employee should at least receive the base deferred salary and cash incentive bonus that he would have earned had his employment not terminated, but prorated for the portion of the year that he was an employee. The Committee made an exception to this in the event the executive voluntarily resigns, in which case the Committee determined that payment of any cash incentive bonus is not warranted because incentive bonuses are designed in part to encourage the employee to remain in the Company's employ.

In accordance with a sense of basic fairness, the Committee determined that in the event that termination is by the Company without cause or because of an uncured breach by the Company of the employment agreement, the executive should also receive the benefit of his base salary for the balance of the term of the agreement, but at least for twelve months.

The Committee did not believe that any special payments should be made to executives in the event of a change in control of the Company because the protections afforded by their employment agreements against termination without cause would be unaffected by a change in control. The executives' outstanding stock options by their terms vest in full in the event of a change in control. The acceleration of vesting is based on the assumption that a change in control often results in a change in senior management. Absent accelerated vesting, a termination without cause after a change in control could unfairly reduce or eliminate the benefit of a stock option depending on when the change occurs. If the executive is terminated for cause, all of the executives' stock options immediately terminate.

Deferred Salary and Incentive Awards for 2008. In 2008, the Company exceeded the 75% of budgeted EBITDA goal, but did not achieve the budgeted, fully-diluted earnings-per-share goal. In February 2009, the Committee reviewed the personal goals of each of Messrs. Manning, Harper and Allen and determined that they had substantially completed all of them to the satisfaction of the Committee. Therefore, the Committee approved the payment to each of Messrs. Manning, Harper and Allen of his base deferred salary and 40% of his cash incentive bonus.

Table of Contents

The Committee, in the exercise of its discretion and based on the personal judgment of the Committee members, awarded Mr. Barzun a cash incentive bonus of $30,000 and increased his annual salary to $80,000.

All base deferred salary payments and cash incentive bonuses for 2008, are more fully described in the following sections:

Employment Agreements of Named Executive Officers

Summary Compensation Table for 2008

Grants of Plan-Based Awards for 2008

Employment Agreements of Named Executive Officers

During 2008, Messrs. Manning, Harper and Allen were compensated under similar employment agreements that became effective in July of 2007 and that expire on December 31, 2010. The following table describes the material financial features of each of the employment agreements.

	Mr. Manning	Mr. Harper	Mr. Allen
Base Salary	$365,000	$365,000	$250,000
Base Deferred Salary	$162,500	$162,500	$75,000
Maximum Incentive Bonus	$162,500	$162,500	$75,000
Equity Compensation	None	None	13,707-share stock option award (1)
Vacation	Discretionary (2)	Discretionary (2)	5 weeks
Benefits Paid by the Company	None	None	None(3)

(1) Information about this stock option, which was granted in August 2007, is set forth below in the section entitled Outstanding Equity Awards at December 31, 2008.

(2) The executive is entitled to take as many days vacation per year as he believes is appropriate in light of the needs of the business.

(3) At Mr. Allen's request when he joined the Company, the Company agreed that he would continue his then current health plan rather than participate in the Company's health plan and that he would be reimbursed for up to $1,000 of the monthly premiums of his plan. This arrangement is less expensive for the Company than if Mr. Allen had joined the Company's health plan.

Mr. Barzun's Employment Agreement. Mr. Barzun's employment agreement became effective in March 2006 and continues until terminated by the Company or by Mr. Barzun. His base salary in 2008 under the terms of his employment agreement was $75,000, and is subject to merit increases. He is also eligible to receive an annual cash incentive bonus in the discretion of the Committee. Because he is a part-time employee, there is no provision in his agreement for paid vacation time.

All of the foregoing agreements provide for the election of the executive to his current positions with the Company. The employment agreements of Messrs. Manning, Harper and Allen provide that they may not compete with the Company after termination of employment for a period of twelve months or for the period, if any, during which the Company is obligated to continue to pay him his base payroll salary, whichever period is longer

43

Table of Contents

Potential Payments upon Termination or Change-in-Control

The following table describes the payment and other obligations of the Company and the named executive officers under their employment agreements in the event of a termination of employment or a change in control of the Company. The table also shows the estimated cost to the Company had the executive's employment been terminated on December 31, 2008.

Patrick T. Manning, Joseph P. Harper, Sr. & James H. Allen, Jr.

Event	Payment and/or Other Obligations *
1.Termination by the Company without cause	The Company must — · Continue to pay the executive his base salary for the balance of the term of his employment agreement or for one year, whichever period is longer; · Continue to cover him under its medical and dental plans provided the executive reimburses the Company the COBRA cost thereof, in which event the Company must reimburse the amount of the COBRA payments to the executive; and · Pay him a portion of any base deferred salary and cash incentive bonus that he would have earned had he remained an employee of the Company through the end of the calendar year in which his employment is terminated, based on the number of days during the year that he was an employee of the Company.
Estimated December 31, 2008 termination payments: Messrs. Manning & Harper (each)	$730,000 plus COBRA payment reimbursement, which currently would be approximately $32,219 for Mr. Manning and $20,885 for Mr. Harper for the two-year period.
Mr. Allen	$500,000 plus $24,000 in health insurance reimbursements.
2.Termination by reason of the executive's death	The Company is obligated to pay the executive a portion of any base deferred salary and of any cash incentive bonus that he would have earned had he remained an employee of the Company through the end of the calendar year in which his employment terminated, based on the number of days during the year that he was an employee of the Company.
Estimated December 31, 2008 termination payments:	None
3.Termination by the Company for cause(1)	The Company is required to pay the executive any accrued but unpaid base payroll salary through the date of termination and any other legally-required payments through that date. All of the executive's stock options terminate.
Estimated December 31, 2008 termination payments:	None
4.Involuntary resignation of the executive (2)	An involuntary resignation, also known as a constructive termination, is treated under the agreement as a termination by the Company without cause. See Event #1, above.

Estimated December 31, 2008 termination payments:	
5.Voluntary resignation by the executive	The Company is obligated to pay the executive a portion of any base deferred salary that he would have earned had he remained an employee of the Company through the end of the calendar year in which he resigned, based on the number of days during the year that he was an employee of the Company.
Estimated December 31, 2008 termination payments:	None
6.A change in control of the Company.	All the executives' un-exercisable but in-the-money stock options become exercisable in full. At December 31, 2008, those options had the following values based on the difference between the market value of a share of the Company's common stock at that date and each option's per-share exercise price: Mr. Manning $11,851 Mr. Harper $1,050 Mr. Allen -0-

* The base payroll salaries, base deferred salaries and cash incentive bonus eligibility of the executives are set forth above under the heading Employment Agreements of Named Executive Officers.

(1) The term "cause" is defined in the employment agreements and means what is commonly referred to as cause in employment matters, such as gross negligence, dishonesty, insubordination, inadequate performance of responsibilities after notice and the like. A termination without cause is a termination for any reason other than for cause, death or voluntary resignation.

(2) The executive is entitled to "involuntarily" resign in the event that the Company commits a material breach of a material provision of his employment agreement and fails to cure the breach within thirty days, or, if the nature of the breach is one that cannot practicably be cured in thirty days, if the Company fails to diligently and in good faith commence a cure of the breach within the thirty-day period.

Table of Contents

Roger M. Barzun. In the event that Mr. Barzun's employment is terminated for cause, the Company is only obligated to pay him his salary through the date of termination, and his outstanding options terminate on that date. In the event that his employment is terminated without cause, or by reason of his death or permanent disability, the Company is obligated to pay him his salary then in effect for a period of six months, which at December 31, 2008 would be $37,500, and to pay him within thirty days of his termination a portion of any cash incentive bonus to which he would otherwise have been entitled had his employment not been terminated, based on the number of days during the year that he was an employee of the Company. For purposes of determining the amount of the cash incentive bonus to which he would have been entitled, the Company is required to make such reasonable assumptions as it determines in good faith. In the event of a change in control of the Company, all of Mr. Barzun's options become exercisable in full. At December 31, 2008, his only un-exercisable, in-the-money option had a value of $700 based upon the difference between the market value of a share of the Company's common stock at that date and the option's per-share exercise price.

Summary Compensation Table for 2008

The following table sets forth for calendar years 2006, 2007 and 2008 all compensation awarded to, earned by, or paid to, Patrick T. Manning, the Company's principal executive officer, and James H. Allen, Jr., its principal financial officer, who joined the Company in July 2007.

The table also shows the same compensation information of Joseph P. Harper, Sr., the Company's President, Treasurer & Chief Operating Officer, and Roger M. Barzun, its Senior Vice President, Secretary & General Counsel, who are the only other executive officers whose compensation for 2008 exceeded $100,000.

The Company pays compensation to these executive officers according to the terms of their employment agreements. The Company does not pay Messrs. Manning or Harper additional compensation for service on the Board of Directors. The amounts include any compensation that was deferred by the executive through contributions to his defined contribution plan account under Section 401(k) of the Internal Revenue Code. All amounts are rounded to the nearest dollar.

Name and Principal Position	Year	Salary ($)	Option Awards(1) ($)	Non-Equity Incentive Plan Compensation(2) ($)	All Other Compensation ($)(3)	Total ($)
Patrick T. Manning Chairman of the Board & Chief Executive Officer (principal executive officer)	2006	240,000	82,883	341,000	38,950	702,833
	2007	296,500	—	325,000	31,258	652,758
	2008	365,000	—	227,500	6,900	599,400
Joseph P. Harper, Sr. President, Treasurer & Chief Operating Officer	2006	235,800*	82,883	318,500	21,150	658,333
	2007	282,500	—	325,000	14,396	621,896
	2008	365,000	—	227,500	7,300	599,800
James H. Allen, Jr. Senior Vice President & Chief	2007	115,500	14,553	100,000	865	230,918
	2008	250,000	—	105,000	7,500	362,500

Financial Officer (principal financial officer)						
Roger M. Barzun	2007	62,500	—	75,000	—	137,500
Senior Vice President & General Counsel, Secretary	2008	76,800	—	30,000	—	106,800

* This includes $20,800 paid to Mr. Harper for foregoing approximately five weeks of the vacation he was entitled to in 2006 under his prior employment agreement, which expired in July 2007.

(1) The value of these stock option awards is the total dollar cost of the award recognized by the Company in the year of grant for financial reporting purposes in accordance with FAS 123R. No amounts earned by the executive officers have been capitalized on the balance sheet for 2008. The cost does not reflect any estimates made for financial statement reporting purposes of forfeitures by the executive officers related to service-based vesting conditions.

The valuation of these options was made on the equity valuation assumptions described in Note 8 of Notes to Consolidated Financial Statements. None of the awards has been forfeited. The following section, entitled Grants of Plan-Based Awards for 2008, contains a description of the basis on which these stock options were awarded and their full grant date fair market value.

(2) Cash incentive bonuses were calculated and approved by the Committee in February 2009. The bonuses for 2006 were determined in part by the application of a formula found in the prior employment agreement of each executive officer and in part by the Committee exercising its discretion as to the amount of additional cash incentive bonus within the range provided for in his employment agreements. Footnotes (1) and (2) to the table in the following section, entitled Grants of Plan-Based Awards for 2008, contain a description of the formula and its application.

(3) The following table shows a breakdown of the amounts shown above in the column entitled All Other Compensation. The dollar amounts are the costs of the items to the Company.

Table of Contents

Type of Other Compensation	Year	Mr. Manning	Mr. Harper	Mr. Allen
Car allowance	2006	$8,400	$8,400	—
	2007	$5,000	$5,000	—
	2008	—	—	
Expenses of commuting to work	2006	$2,500	$1,800	—
	2007	$2,400	$1,750	—
	2008	—	—	
Country club dues	2006	$25,000	$4,500	—
	2007	$15,000	$3,420	—
	2008	—	—	
Company contribution to 401(k) Plan account	2006	$3,050	$6,450	—
	2007	$8,858	$4,226	$865
	2008	$6,900	$7,300	$7,500

Grants of Plan-Based Awards for 2008

The following table shows each grant of an award for 2008 to a named executive officer under a Company plan. The Company did not award any SAR's, stock, restricted stock, restricted stock units, or similar instruments to any of the named executive officers in 2008.

	Grant Date	Estimated Possible Payouts Under Non-Equity Incentive Plan Awards (1) ($)			All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards ($/share)	Grant Date Fair Value of Option Awards ($)
		Threshold	Target	Maximum			
Patrick T. Manning	N/A	162,500	260,000	325,000	—	N/A	N/A
Joseph P. Harper, Sr.	N/A	162,500	260,000	325,000	—	N/A	N/A
James H. Allen, Jr.	N/A	75,000	120,000	150,000	—	N/A	N/A
Roger M. Barzun	N/A	—	$75,000	—	—	N/A	N/A

Table of Contents

(1) Non-Equity Incentive Plan Awards. In the table above, "possible" payouts mean the payouts that were available to be earned by the executive for calendar year 2008.

Messrs. Manning, Harper and Allen. As more fully described above under the heading Employment Agreements of Named Executive Officers, the employment agreements of Messrs. Manning, Harper and Allen provide each executive annually with the ability to earn compensation in addition to his base salary. The additional compensation is divided into three parts, each based on the achievement of an annual goal, as follows:

- The achievement by the Company of 75% of budgeted EBITDA.
- The achievement by the Company of budgeted fully-diluted earnings per share.
- The achievement by the executive of personal goals approved by the Committee at the beginning of the year.

As a result, in any given year, the executive may earn all, some or none of the additional compensation. In the table above —

- The Threshold is the amount that the executive will earn if the Company achieves the 75% of budgeted EBITDA goal. It is designated the threshold because, as described above in the section entitled Compensation Discussion and Analysis, this amount is considered by the Committee to be salary that is deferred pending the achievement by the Company of a relatively modest financial goal. In 2008 the goal was more than met by achieving 92% of budgeted EBITDA.
- The Target is the amount that the executive will earn if both the EBITDA and the earnings-per-share goals are achieved. In 2008, the Company did not achieve the earnings-per-share goal.
- The Maximum is the sum of the Target amount and the amount the executive will earn if, in addition to the financial goals, he achieves all of his personal goals for the year. In 2008 the Committee determined that each executive completed substantially all of his personal goals.

Mr. Barzun. Mr. Barzun's cash incentive bonus for a given year is entirely in the discretion of the Committee and is based on the Company's consolidated financial results for the year, the number of non-routine legal transactions to which he devoted substantial time during the year, and such other matters as the Committee deems relevant. Accordingly, because Mr. Barzun's possible payout for 2008 cannot be estimated at the beginning of the year, the Target amount included in the table is the bonus paid to him for 2007.

For the actual amounts paid to the executives for 2008, see the Summary Compensation Table for 2008, above.

Table of Contents

Option Exercises and Stock Vested for 2008

The following table contains information on an aggregated basis about each exercise of a stock option during 2008 by each of the named executive officers.

	Option Awards	
Name	Number of Shares Acquired on Exercise (#)	Value Realized Upon Exercise(1) ($)
Patrick T. Manning	17,200	$221,380
Joseph P. Harper, Sr.	—	—
James H. Allen, Jr.	—	—
Roger M. Barzun	1,190	$24,722

(1) SEC regulations define the "Value Realized Upon Exercise" as the difference between the market price of the shares on the date of the purchase, and the option exercise price of the shares, whether or not the shares are sold, or if they are sold, whether or not the sale occurred on the date of the exercise.

Outstanding Equity Awards at December 31, 2008

The following table shows certain information concerning un-exercised stock options and stock options that have not vested that were outstanding on December 31, 2008 for each named executive officer. No other equity awards have been made to the named executive officers.

	Option Awards					
Name	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price/Share ($)	Option Grant Date	Option Expiration Date	Vesting Date Footnotes
Patrick T. Manning	400	600	$25.21	8/08/2006	9/08/2011	(1)
	10,000	—	$24.96	7/18/2006	7/18/2011	(2)
	300	600	$16.78	8/12/2005	9/12/2010	(1)
	10,000	—	$9.69	7/18/2005	7/18/2010	(2)
	2,800	700	$3.10	8/12/2004	8/12/2014	(1)
	—	—	$3.10	8/12/2004	8/12/2009	(2)
	3500	—	$3.05	8/20/2003	8/20/2013	(1)
Joseph P. Harper, Sr.	400	600	$25.21	8/08/2006	9/08/2011	(1)
	10,000	—	$24.96	7/18/2006	7/18/2011	(2)
	900	600	$16.78	8/12/2005	9/12/2010	(1)
	10,000	—	$9.69	7/18/2005	7/18/2010	(2)
	3,500	—	$3.10	8/12/2004	8/12/2014	(3)
	10,000	—	$3.10	8/12/2004	8/12/2009	(2)
	3,500	—	$3.05	8/20/2003	8/20/2013	(3)

	3,500	—	$1.725	7/24/2002	7/24/2012	(3)
	3,700	—	$1.50	7/23/2001	7/23/2011	(1)
James H. Allen, Jr.	13,707	9,138	$18.99	8/7/2007	8/7/2012	(3)
Roger M. Barzun	240	360	$25.21	8/8/2006	9/8/2011	(1)
	600	400	$16.78	8/12/2005	9/12/2010	(1)
	2,000	—	$3.10	8/12/2004	8/12/2014	(4)

Table of Contents

Vesting of Stock Options. If there is a change in control of the Company, all the stock options then held by a named executive officer become exercisable in full. Absent a change in control of the Company, the options listed above vest as described in the following footnotes:

(1) This option vests in equal installments on the first five anniversaries of its grant date.

(2) This option vested in a single installment on July 18, 2007.

(3) This option vests in equal installments on the first three anniversaries of its grant date.

(4) This option vested in a single installment on its grant date.

Director Compensation for 2008

The Company does not pay additional compensation for serving on the Board of Directors to directors who are employees of the Company, namely Messrs. Manning and Harper. The following table contains information concerning the compensation paid for 2008 to non-employee directors. All dollar numbers are rounded to the nearest dollar.

Name	Fees Earned or Paid in Cash ($)	Stock Awards (1)(3) ($)	Total(2) ($)
John D. Abernathy (Lead director) Chairman of the Audit Committee Member of the Compensation and Corporate Governance & Nominating Committees	39,184	50,000	89,184
Robert W. Frickel Chairman of the Compensation Committee Member of the Corporate Governance & Nominating Committee	29,884	50,000	79,884
Donald P. Fusilli, Jr. Member of the Audit Committee Member of the Compensation Committee	26,956	50,000	76,956
Maarten D. Hemsley	21,406	50,000	71,406
Christopher H. B. Mills	18,756	50,000	68,756
Milton L. Scott Chairman of the Corporate Governance & Nominating Committee Member of the Audit Committee	30,998	50,000	80,998
David R. A. Steadman Member of the Corporate Governance & Nominating Committee	25,542	50,000	75,542

(1) The aggregate value of these restricted stock awards was $350,000, including $220,833 recognized in 2008 for financial reporting purposes in accordance with FAS 123R. No amounts earned by a director have been capitalized on the balance sheet for 2008. The cost does not reflect any estimates made for financial statement reporting purposes of future forfeitures related to service-based vesting conditions. The valuation of the awards was made on the equity valuation assumptions described in Note 8 of Notes to Consolidated Financial Statements. None of

the awards has been forfeited to date.

(2) During 2008, none of the non-employee directors received any other compensation for any service provided to the Company. All directors are reimbursed for their reasonable out-of-pocket expenses incurred in attending meetings of the Board and Board committees. Directors living outside of North America, currently only Mr. Mills, have the option of attending regularly-scheduled in-person meetings by telephone, and if they choose to do so, they are paid an attendance fee as if they had attended in person.

(3) The following table shows for each non-employee director the grant date fair value of each stock award that has been expensed, the aggregate number of shares of stock awarded, and the number of shares underlying stock options that were outstanding on December 31, 2008.

Table of Contents

Name	Grant Date	Securities Underlying Option Awards Outstanding at December 31, 2008 (#)	Aggregate Stock Awards Outstanding at December 31, 2008 (#)	Grant Date Fair Value of Stock and Option Awards ($)
John D. Abernathy	5/19/2005	5,000		27,950
	5/8/2008		2,564	50,000
Total		5,000	2,564	77,950
Robert W. Frickel	7/23/2001	12,000		57,600
	5/19/2005	5,000		27,950
	5/8/2008		2,564	50,000
Total		17,000	2,564	135,550
Donald P. Fusilli, Jr.	5/8/2008	—	2,564	50,000
Maarten D. Hemsley	7/18/2007	2,800		27,640
	7/18/2006	2,800		45,917
	7/18/2005	2,800		17,534
	5/8/2008		2,564	50,000
Total		8,400	2,564	141,091
Christopher H. B. Mills	5/19/2005	5,000		27,950
	5/8/2008		2,564	50,000
Total		5,000	2,564	77,950
Milton L. Scott	5/8/2008		2,564	50,000
David R. A. Steadman	5/8/2008		2,564	50,000

Standard Director Compensation Arrangements. The following table shows the standard compensation arrangements for non-employee directors that were adopted by the Board on May 8, 2008.

Annual Fees		
Annual Fees	Each Non-Employee Director	
	$17,500	
	An award (on the date of each Annual Meeting of Stockholders) of restricted stock that has an accounting income charge under FAS 123R of $50,000 per grant.*	
Additional Annual Fees for Committee Chairmen		
Chairman of the Audit Committee		$12,500
Chairman of the Compensation Committee		$7,500
Chairman of the Corporate Governance & Nominating Committee		$7,500
Meeting Fees		
In-Person Meetings		Per Director Per Meeting
Board Meetings		$1,500
Committee Meetings		
Audit Committee Meetings in connection with a Board meeting		$1,000

not in connection with a Board meeting	$1,500
Other Committee Meetings	
in connection with a Board meeting	$500
not in connection with a Board meeting	$750
Telephonic Meetings (Board & committee meetings)	
One hour or longer	$1,000
Less than one hour	$300

* The shares awarded are considered restricted because they may not be sold, assigned, transferred, pledged or otherwise disposed of until the restrictions expire. The restrictions for the award made on May 8, 2008 expire on May 5, 2009, the day before the 2009 Annual Meeting of Stockholders, but earlier if the director dies or becomes disabled or if there is a change in control of the Company. The shares are forfeited if before the restrictions expire, the director ceases to be a director other than because of his death or disability.

Table of Contents

Compensation Committee Interlocks and Insider Participation

During 2008, Robert W. Frickel (Chairman), John D. Abernathy and Donald P. Fusilli, Jr. served on the Compensation Committee. None of these Compensation Committee members is or has been an officer or employee of the Company. Mr. Frickel is President of R.W. Frickel Company, P.C., an accounting firm that performs certain accounting and tax services for the Company. In 2008, the Company paid or accrued for payment to R.W. Frickel Company approximately $39,700 in fees. The Company estimates that during 2009, the fees of R.W. Frickel Company will be approximately the same as in 2008.

None of the Company's executive officers served as a director or member of the compensation committee, or any other committee serving an equivalent function, of any other entity that has an executive officer who is serving or during 2008 served as a director or member of the Compensation Committee of the Company.

Compensation Committee Report

The Compensation Committee of the Board of Directors has reviewed and discussed with management the Compensation Discussion and Analysis set forth above in this Item 11. Based on that review and those discussions, the Compensation Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this Annual Report on Form 10-K.

Submitted by the members of the Compensation Committee on March 16, 2009

Robert W. Frickel, Chairman
John D. Abernathy
Donald P. Fusilli, Jr.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

Equity Compensation Plan Information. The following table contains information at December 31, 2008 about compensation plans (including individual compensation arrangements) under which the Company has authorized the issuance of equity securities.

Plan Category(1)	Number of Securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans, excluding securities reflected in column (a)
	(a)	(b)	(c)
Equity compensation plans approved by security holders:	411,000	$9.753	397,690

(1) There is no outstanding compensation plan (including individual compensation arrangements) under which the Company has authorized the issuance of equity securities that has not been approved by stockholders.

Security Ownership of Certain Beneficial Owners and Management. The following table sets forth certain information at February 16, 2009 about the beneficial ownership of shares of the Company's common stock by each person or entity known to the Company to own beneficially more than 5% of the outstanding shares of common stock; by each director; by each executive officer named above in Item 11. — Executive Compensation, under the heading Summary Compensation Table for 2008; and by all directors and executive officers as a group. The Company has no other class of equity securities outstanding.

Table of Contents

Based on information furnished by the beneficial owners, the Company believes that those owners have sole investment and voting power over the shares of common stock shown as beneficially owned by them, except as stated otherwise in the footnotes to the table.

Rule 13d-3(d)(1) of the Securities Exchange Act of 1934 requires that the percentages listed in the following table assume for each person or group the acquisition of all shares that the person or group can acquire within sixty days of February 16, 2009, for instance by the exercise of a stock option, but not the acquisition of the shares that can be acquired in that period by any other person or group listed.

Except for Mr. Mills and the entities listed below, the address of each person is the address of the Company.

Name and Address of Beneficial Owner	Number of Outstanding Shares of Common StockOwned	Shares Subject to Purchase*	Total Beneficial Ownership	Percent of Class
Wellington Management Company, LLP 75 State Street Boston, Massachusetts 02109 (2)	1,646,870(1)	—	1,646,870	12.49%
T. Rowe Price Associates, Inc. 100 E. Pratt Street Baltimore, Maryland 21201 (1)	1,086,413(2)	—	1,086,413	8.24%
John D. Abernathy	54,531(3)	5,000	59,531	†
Robert W. Frickel	67,369(3)	17,000	84,369	†
Donald P. Fusilli, Jr.	4,162(3)	—	4,162	†
Joseph P. Harper, Sr.	520,444(4)	173,074	693,518	5.19%
Maarten D. Hemsley	184,238 (3)(5)	8,400	192,638	1.46%
Patrick T. Manning	100,295(6)	27,600	127,895	