

STERLING CONSTRUCTION CO INC  
Form 10-K  
March 05, 2019

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

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: December 31, 2018

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_ to \_\_\_

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.)

1800 Hughes Landing Blvd.

The Woodlands, Texas

77380

(Address of principal executive office)

(Zip Code)

Registrant's telephone number, including area code (281) 214-0800

Securities registered pursuant to Section 12(b) of the Act: Name of each exchange on which registered  
Title of each class The NASDAQ Stock Market LLC

Common Stock, \$0.01 par value per share  
(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 whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).  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

Edgar Filing: STERLING CONSTRUCTION CO INC - 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 the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company   
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Act

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, 2018:  
\$341,407,747.

At March 1, 2019, the registrant had 26,639,715 shares of common stock outstanding.

#### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company's definitive Proxy Statement to be filed with the Securities and Exchange Commission and delivered to stockholders in connection with the Annual Meeting of Stockholders to be held on May 8, 2019 are incorporated by reference into Part III of this Form 10-K.

---

Sterling Construction Company, Inc.

Annual Report on Form 10-K

Table of Contents

<u>PART I</u>	<u>3</u>
<u>Item 1. Business</u>	<u>5</u>
<u>Item 1A. Risk Factors</u>	<u>10</u>
<u>Item 1B. Unresolved Staff Comments</u>	<u>21</u>
<u>Item 2. Properties</u>	<u>21</u>
<u>Item 3. Legal Proceedings</u>	<u>21</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>22</u>
<u>Executive Officers of the Registrant</u>	<u>23</u>
<u>PART II</u>	<u>24</u>
<u>Item 5. Market for the Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>24</u>
<u>Item 6. Selected Financial Data</u>	<u>27</u>
<u>Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>28</u>
<u>Item 7A. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>44</u>
<u>Item 8. Financial Statements and Supplementary Data</u>	<u>44</u>
<u>Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure</u>	<u>44</u>
<u>Item 9A. Controls and Procedures</u>	<u>44</u>
<u>Item 9B. Other Information</u>	<u>45</u>
<u>PART III</u>	<u>46</u>
<u>Item 10. Directors, Executive Officers and Corporate Governance</u>	<u>46</u>
<u>Item 11. Executive Compensation</u>	<u>46</u>
<u>Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>46</u>
<u>Item 13. Certain Relationships and Related Transactions, and Director Independence</u>	<u>46</u>
<u>Item 14. Principal Accounting Fees and Services</u>	<u>46</u>
<u>PART IV</u>	<u>47</u>
<u>Item 15. Exhibits, and Financial Statement Schedules</u>	<u>47</u>
<u>Financial Statement Schedules</u>	<u>47</u>
<u>Exhibits</u>	<u>47</u>
<u>Item 16. Form 10-K Summary</u>	<u>50</u>
<u>SIGNATURES</u>	<u>51</u>

## PART I

### Cautionary Statement

This annual report on Form 10-K, including the documents incorporated herein by reference, contains statements that are, or may be considered to be, “forward-looking statements” regarding the Company which represent our expectations and beliefs concerning future events. These forward-looking statements are intended to be covered by the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995 as set forth in Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. The forward-looking statements included herein or incorporated herein by reference relate to matters that are predictive in nature, 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, and may use or contain words such as “anticipate,” “assume,” “believe,” “budget,” “continue,” “could,” “estimate,” “expect,” “forecast,” “future,” “intend,” “may,” “predict,” “project,” “should,” “will,” “would” and similar terms and phrases.

Forward-looking statements reflect our current expectations as of the date of this annual report on Form 10-K 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 those anticipated, projected or assumed in the forward-looking statements due to a variety of factors. Although it is not possible to identify all of these factors, they include, among others, the following:

factors that affect the accuracy of estimates inherent in our bidding for contracts, estimates of backlog, recognition of revenue and earnings from construction contracts over time, including onsite conditions that differ materially from those assumed in our original bid, contract modifications, or mechanical problems with our machinery or equipment; actions of suppliers, subcontractors, design engineers, joint venture partners, customers, competitors, banks, surety companies and others which are beyond our control, including suppliers’, subcontractors’ and joint venture partners’ failure to perform;

cost escalations associated with our contracts, including changes in availability, proximity and cost of materials such as steel, cement, concrete, aggregates, oil, fuel and other construction materials, including changes in U.S. trade policies and retaliatory responses from other countries, and cost escalations associated with subcontractors and labor;

change in cost to lease, acquire or maintain our equipment;

our dependence on a limited number of significant customers;

the presence of competitors with greater financial resources or lower margin requirements than ours, and the impact of competitive bidders on our ability to obtain new backlog at reasonable margins acceptable to us;

a shutdown of the federal government;

our ability to qualify as an eligible bidder under government contract criteria;

changes in general economic conditions, including recessions, reductions in federal, state and local government funding for infrastructure services, changes in those governments’ budgets, practices, laws and regulations and adverse economic conditions in our geographic markets;

delays or difficulties related to the completion of our projects, including additional costs, reductions in revenues or the payment of liquidated damages, or delays or difficulties related to obtaining required governmental permits and approvals;

design/build contracts which subject us to the risk of design errors and omissions;

- our ability to obtain bonding or post letter of credit;
- our ability to raise additional capital on favorable terms;
- our ability to attract and retain key personnel;
- increased unionization of our workforce or labor costs and any work stoppages or slowdowns;
- adverse weather conditions;
- our ability to successfully identify, finance, complete and integrate acquisitions;
- citations issued by any governmental authority, including the Occupational Safety and Health Administration;
- federal, state and local environmental laws and regulations where non-compliance can result in penalties and/or termination of contracts as well as civil and criminal liability; and
- the other factors discussed in more detail in “Item 1A. Risk Factors.”

In reading this annual report on Form 10-K, 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. Investors are cautioned that many of the assumptions upon which our forward-looking statements are based are likely to change after the forward-looking statements are made. Further, we may make changes to our business plans that could affect our results. Although we believe that our plans, intentions and expectations reflected in, or suggested by, the forward-looking statements that we make in this annual report on Form 10-K are reasonable, we can provide no assurance that they will be achieved.

The forward-looking statements included herein are made only as of the date hereof, and we undertake no obligation to update any information contained herein 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 annual report on Form 10-K.

4

---

## Item 1. Business

### Overview of the Company's Business

Sterling Construction Company, Inc., ("Sterling" or "the Company") was founded in 1991 as a Delaware corporation. Our principal executive offices are located at 1800 Hughes Landing Boulevard, Suite 250, The Woodlands, Texas 77380 and our telephone number at this address is (281) 214-0800. Our construction business was founded in 1955 by a predecessor company in Michigan and is now conducted through our subsidiaries which primarily include: J. Banicki Construction, Inc., an Arizona corporation, or "JBC"; Myers & Sons Construction, L.P., a California limited partnership, or "Myers"; Myers & Sons Construction, LLC, a California limited liability company and wholly-owned subsidiary of Myers; Ralph L. Wadsworth Construction Company, LLC, a Utah limited liability company, or "RLW"; Road and Highway Builders, LLC, a Nevada limited liability company, or "RHB"; Tealstone Commercial, Inc., a Texas corporation, or "TCI"; Tealstone Residential Concrete, Inc., a Texas corporation, or "TRC"; and Texas Sterling Construction Co., a Delaware corporation, or "TSC". TCI and TRC combined are referred to as "Tealstone." 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 or a particular subsidiary.

The Company is a construction company that specializes in heavy civil infrastructure construction and infrastructure rehabilitation as well as residential construction projects. We operate primarily in Arizona, California, Colorado, Hawaii, Nevada, Texas and Utah, as well as other states in which there are feasible construction opportunities. Heavy civil construction projects include highways, roads, bridges, airfields, ports, light rail, water, wastewater and storm drainage systems, foundations for multi-family homes, commercial concrete projects and parking structures. Residential construction projects include concrete foundations for single-family homes.

Sterling has grown its service profile and geographic reach both organically and through acquisitions. RHB was acquired in 2007, which expanded the footprint into Nevada and Hawaii. Expansions into Utah, Arizona and California were achieved with the 2009 acquisition of RLW and the 2011 acquisitions of JBC and Myers, respectively. Expansion into single family home residential concrete foundation projects was achieved with the 2017 acquisition of Tealstone.

### Recent Developments

In 2018, the Company's revenues increased to \$1,037.7 million, from \$958.0 million in 2017. Our 2018 operating income totaled \$42.6 million and net income attributable to Sterling common stockholders was \$25.2 million compared to an operating income of \$26.2 million and a net income of \$11.6 million in 2017. Our gross margins have increased to 10.6% in 2018 from 9.3% in 2017. In addition, the Company generated \$39.5 million of cash from operations, repaid \$10.4 million of debt and repurchased \$4.7 million of common stock in 2018.

The Company's financial improvements reflect progress in delivering our multi-year strategy to solidify the base, grow high margin products and expand into adjacent markets. Our strategic element to solidify the base of the heavy civil construction business focuses on cost reductions, remaining disciplined at the bid table, monitoring pricing at the time of bid, and executing the projects to expectations. The strategy element to grow high margin products is reflected in the increasing percentage of backlog of non-heavy highway projects. Finally, expansion of the residential business, as well as other acquisition opportunities, will lead to further expansion into adjacent markets. Overall, the execution of our strategy led to improved operating income of \$42.6 million in 2018 compared to an operating income of \$26.2 million in 2017.





Sterling's heavy civil construction business is primarily driven by federal, state and municipal funding. Federal funds, on average, provide 50% of annual State Department of Transportation (DOT) capital outlays for highway and bridge projects. Several of the states in Sterling's key markets have instituted actions to further increase annual spending. In November 2018, various state and local transportation measures were passed securing funding of \$1.57 billion in California, \$1.27 billion in Texas, \$528.5 million in Arizona, \$128.2 million in Colorado and \$87 million in Utah. In October 2018, the Federal Aviation Administration reauthorized \$3.35 billion annually for the next five years. This reauthorization also includes more than \$1 billion a year for airport infrastructure grants and about \$1.7 billion for disaster relief. In Texas, two constitutional amendments were passed in 2015, which will increase the annual funds allocated to transportation projects from \$4.0 billion to \$4.5 billion per year. Texas also has locally approved bonds estimated at \$1.3 billion that were approved in November 2017. In Utah, a 20% gas tax increase to support infrastructure projects was put into effect January 2016, which is the first state gas tax increase in 18 years. The State of Utah also approved, in 2017, a \$1 billion bond package for infrastructure improvements. A 1-cent sales tax increase was approved in Los Angeles, California in 2016 that will provide \$3 billion per year for local road, bridge and transit projects. In addition, California approved a 10 year \$52 billion bill that provides an annual \$5 billion in incremental funding for use on highway transit repair projects. In addition to the state locally funded actions, Sterling is in year four of the 2015 federally funded five-year \$305 billion surface transportation bill that increased the annual federal highway investment by 15.1% over the five-year period from 2016 to 2020.

#### Initiation of a 2 Million Share Stock Repurchase Program

On November 2, 2018, the Board of Directors approved the repurchase of up to 2 million shares of its outstanding common stock through June 30, 2020. The repurchase program permits shares to be repurchased in the open market or in private transactions and pursuant to any trading plan that may be adopted in accordance with all applicable securities laws and regulations. Repurchases will be made at management's discretion at prices that management considers to be attractive and in the best interests of both Sterling and its stockholders. The timing and amount of shares repurchased will depend on a variety of factors, including the availability of stock, general market conditions, the trading price of the stock, alternative uses for capital and Sterling's financial performance. The repurchase program may be suspended, terminated or modified at any time for any reason, including market conditions, the cost of repurchasing shares, the availability of alternative investment opportunities, liquidity, and other factors deemed appropriate. The repurchase program does not obligate Sterling to purchase any particular number of shares.

#### Tealstone Acquisition

On April 3, 2017, the Company consummated the acquisition (the "Tealstone Acquisition") of 100% of the outstanding stock of Tealstone from the stockholders thereof (the "Sellers") for consideration totaling \$84 million and up to an aggregate of \$15.0 million in earn-out payments if specified financial performance levels are achieved. Tealstone focuses on concrete construction of residential foundations, parking structures, elevated slabs and other concrete work for leading homebuilders, multi-family developers and general contractors in both residential and commercial markets. This acquisition enables expansion into adjacent markets and diversification of revenue streams and customer base with higher margin work.

In conjunction with the Tealstone Acquisition, on April 3, 2017, the Company, as borrower, and certain of its subsidiaries, as guarantors, entered into a Loan and Security Agreement with Wilmington Trust, National Association, as agent, and the lenders party thereto (the "Oaktree Facility"), providing for a term loan of \$85.0 million (the "Loan") with a maturity date of April 4, 2022, which replaced the then existing debt facility. The Loan is secured by substantially all of the assets of the Company and its subsidiaries.

#### Our Markets and Customers

Our operations are performed under our heavy civil construction and residential construction segments within the United States (“U.S.”). See Note 18 - Segment Information for additional details (references to “Note” or “Notes” refer to the Notes to the consolidated financial statements for the year ended December 31, 2018, included in this annual report on Form 10-K).

#### Heavy Civil Construction

Our heavy civil construction segment relies heavily on federal and state infrastructure spending. In our heavy civil construction segment, our principal markets are Arizona, California, Colorado, Hawaii, Nevada, Texas and Utah. Within our principal markets, our core customers are the departments of transportation in various states DOTs, regional transit authorities, airport authorities, port authorities, water authorities, railroads and commercial construction customers.

Currently, our largest customers are Utah, Texas and California DOTs. The Utah DOT contributed more than 10% of our consolidated revenues in 2018. We routinely construct projects for these customers. If we lost any of these customers, it could have a material adverse effect on our financial results. Refer to Item 1A "Risk Factors" and Note 16 - Concentration of Risk and Enterprise Wide Disclosures for the Company's major customers that represent a concentration of risk due to their significant revenue contributions.

### Residential Construction

Our residential construction segment's principal market is Texas, specifically the Dallas-Fort Worth area and the surrounding communities. The core customer base for residential construction segment is primarily made up of leading national home builders as well as regional and custom home builders. Our largest customers are Pulte Group, Inc., D.R. Horton, Inc., Lennar and HISTORYMAKER Homes.

### Competition

Our competition for both segments ranges from small local contractors to large international construction companies. We traditionally try to position ourselves to bid on work that is too large for the small local contractors yet too small for the large national and international construction companies. However, if market conditions became less favorable, we would tend to see migration from both the small local contractors and large international players into that geographical market. This, in return, could increase competitive bidding pressure and reduce both revenue growth and margins. See the section below entitled, Item 1A. "Risk Factors."

### Seasonality

Our operations for both segments are typically affected by weather conditions primarily during the first and fourth quarters of our fiscal year, which may alter construction schedules and can create variability in our revenues, profitability and the required number of employees.

### Source and Availability of Raw Materials

We purchase raw materials for both segments, including but not limited to, cement, aggregate, concrete, liquid asphalt, steel, diesel and gasoline fuel, natural gas and propane from numerous sources. The price and availability of raw materials may vary from year to year due to fluctuations in market conditions and production capacities. We do not foresee a lack of availability of any necessary raw materials over the next twelve months.

### Heavy Civil Construction Backlog

Components of our heavy civil construction Combined Backlog are as follows:

- "Backlog" is the unearned revenue we expect to earn in future periods on our executed heavy civil construction contracts. Backlog was \$851 million and \$744 million as of December 31, 2018 and 2017, respectively. As the construction on our projects progress, we increase or decrease Backlog to take into account signed contracts, revenue earned during the period and our estimates of the effects of changes in estimated quantities, changed conditions, change orders and other variations from previously anticipated contract revenues, including completion penalties and incentives. We anticipate that approximately 75% of our Backlog will be recognized as revenues during 2019.

• We exclude from "Backlog" contracts in which we are the apparent low bidder for projects ("Unsigned Low-bid Awards") until the contract is executed by our customer. Unsigned Low-bid Awards were \$293 million at

December 31, 2018 and \$250 million at the end of 2017. We expect substantially all of the Unsigned Low-bid Awards at December 31, 2018 to be signed and included in Backlog in the first half of 2019.

The combination of our Backlog and Unsigned Low-bid Awards, which we refer to as "Combined Backlog," totaled \$1.1 billion and \$995 million as of December 31, 2018 and 2017, respectively.

7

---

## Types of Contracts

Our contracts are awarded on a competitively bid basis or negotiated bid basis using a range of contracting options, including cost-reimbursable, lump sum and fixed-unit price. Each contract is designed to optimize the balance between risk and reward. At December 31, 2018, approximately 80% of our backlog was contracted on a fixed-unit price or lump sum basis. See Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion of our types of risk and how we mitigate cancellation and credit risk.

## Insurance and Bonding

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, workers' compensation insurance and auto insurance all in amounts consistent with our risk of loss and industry practice.

As a normal part of the heavy civil 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 the contract. Typically, a bidder for a contract must post a bid bond, generally for 5% to 10% of the bid amount, and on being awarded the bid, must post a performance and payment bond for 100% of the costs to construct. Usually, upon posting of the performance bond, a contractor must also 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, including accounts receivable, as collateral for such obligation.

## Government and Environmental Regulations

Our operations are subject to compliance with numerous regulatory requirements of federal, state and local agencies and authorities, including regulations concerning safety, wage and hour, and other labor issues, immigration controls, vehicle and equipment operations and other aspects of our business. For example, our construction operations are subject to the requirements of the Occupational Safety and Health Act ("OSHA") and comparable state laws directed toward the protection of employees. In addition, most of our construction contracts are entered into with public authorities, and these contracts frequently impose additional governmental requirements, including requirements regarding labor relations and subcontracting with designated classes of disadvantaged businesses.

All of our operations are also subject to federal, state and local laws and regulations relating to the environment, including those relating to discharges into air, water and land, climate change, the handling and disposal of solid and hazardous waste, the handling of underground storage tanks and the cleanup of properties affected by hazardous substances. For example, we must apply water or chemicals to reduce dust on road construction projects and to contain contaminants in storm run-off water at construction sites. In certain circumstances, we may also be required to hire subcontractors to dispose of hazardous wastes encountered on a project in accordance with a plan approved in advance by the customer. Certain environmental laws impose substantial penalties for non-compliance and others, such as the federal Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, impose strict and retroactive joint and several liability upon persons responsible for releases of hazardous substances.

CERCLA and comparable state laws impose liability, without regard to fault or the legality of the original conduct, on certain classes of persons that contributed to the release of a "hazardous substance" into the environment. These persons include the owner or operator of the site where the release occurred and companies that disposed or arranged for the

disposal of the hazardous substances found at the site. Under CERCLA, these persons may be subject to joint and several liability for the costs of cleaning up the hazardous substances that have been released into the environment, for damages to natural resources and for the costs of certain health studies. CERCLA also authorizes the Federal Environmental Protection Agency, or EPA, and, in some instances, third parties, to act in response to threats to the public health or the environment and to seek to recover from the responsible classes of persons the costs they incur.

Solid wastes, which may include hazardous wastes, are subject to the requirements of the Federal Solid Waste Disposal Act, the Federal Resource Conservation and Recovery Act, referred to as RCRA, and comparable state statutes. Although we do not generate solid waste, we occasionally dispose of solid waste on behalf of customers. From time to time, the EPA considers the adoption of stricter disposal standards for non-hazardous wastes. Moreover, it is possible that additional wastes will in the future be designated as “hazardous wastes.” Hazardous wastes are subject to more rigorous and costly disposal requirements than are non-hazardous wastes.

We continually evaluate whether we must take additional steps at our locations to ensure compliance with environmental laws. While compliance with applicable regulatory requirements has not materially adversely affected our operations in the past, there can be no assurance that these requirements will not change and that compliance will not adversely affect our operations in the future. In addition, tighter regulation for the protection of the environment and other factors may make it more difficult to obtain new permits and renewal of existing permits may be subject to more restrictive conditions than currently exist.

### Employees

As of December 31, 2018, the Company had approximately 1,935 employees, including 1,637 field personnel in our heavy civil construction division. Of the 1,637 heavy civil construction field employees, 311 were union members covered by collective bargaining agreements primarily in Arizona, California, Hawaii and Nevada. Our residential construction segment had approximately 56 employees, including 41 field personnel. None of the residential construction employees are union members.

Our business is dependent upon a readily available supply of management, supervisory and field personnel. Substantially all of our employees are hired on a full-time basis; however, as is typical in the construction industry, we experience a high degree of turnover as construction projects are completed. In the past, we have been able to attract sufficient numbers of personnel to support the growth of our operations. However, we continue to face competition for experienced workers in all our markets.

We focus on our safety processes which have allowed us to maintain a high level of safety at our work sites. All employees receive hazard specific training and our newly-hired employees undergo an initial safety orientation and receive follow-up trainings during their first 90 days of employment. Our project managers and superintendents work closely with the safety department to ensure safety is planned into all of our operations before they begin. Daily, our project foremen are required to conduct safety briefings with employees. Regular safety walkthroughs are conducted by our managers, supervisors and safety staff to evaluate project conditions and observe employee safety behavior.

### Access to Company’s Filings

The Company maintains a website at [www.strlco.com](http://www.strlco.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; some directly on the website and others through a link to the Securities and Exchange Commission’s (“SEC”) website ([www.sec.gov](http://www.sec.gov)) where those reports are filed. Our website also has recent press releases, the Company’s code of business conduct, the charters of the audit committee, compensation and talent development committee, and corporate governance and nominating committee of the Board of Directors and information on the Company’s “whistleblower” 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 annual report on Form 10-K by this reference to it.





## Item 1A. Risk Factors

The following discussion of risk factors contains forward-looking statements. These risk factors may be important to understanding other statements in this annual report on Form 10-K. The following information should be read in conjunction with Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes in Part II, Item 8, "Financial Statements and Supplementary Data" of this annual report on Form 10-K.

Our business, financial condition and operating results can be affected by a number of factors, whether currently known or unknown, including but not limited to those described below; any one or more of which could, directly or indirectly, cause our actual financial condition and operating results to vary materially from past, or from anticipated future, financial condition and operating results. Any of these factors, in whole or in part, could materially and adversely affect our business, prospects, financial condition, results of operations, stock price and cash flows. These could also be affected by additional factors that apply to all companies generally which are not specifically mentioned below.

Because of the following factors, as well as other factors affecting our financial condition and operating results, our past financial performance should not be considered to be a reliable indicator of our future performance, and investors should not use historical trends to anticipate results or trends in future periods.

### Risks Relating to Our Business

If we do not accurately estimate the overall risks, requirements or costs related to a heavy civil project when we bid on or negotiate a contract that is ultimately awarded to us, we may achieve a lower than anticipated profit or incur a loss on the contract.

The majority of our revenues and backlog are derived from fixed unit price contracts and from lump sum contracts. Fixed unit price contracts require us to provide materials and services at a fixed unit price based on agreed quantities irrespective of our actual per unit costs. Lump sum contracts require the contract work to be completed for a single price irrespective of our actual costs incurred. Given that our revenues per contract are fixed, our ability to achieve contract profitability is dependent upon our ability to avoid cost overruns by accurately estimating our costs and then successfully controlling our actual costs. If our cost estimates for a contract are inaccurate, or if we do not perform 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. As a result, these types of contracts could negatively affect our cash flow, earnings and financial position.

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

- onsite conditions that differ from those assumed in the original bid or contract;
- failure to include required materials or work in a bid, or the failure to estimate properly the quantities or costs needed to complete a lump sum contract;
- delays caused by weather conditions;
- contract or project modifications creating unanticipated costs not covered by change orders or contract price adjustments;
- 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;
- higher than anticipated costs to lease, acquire and maintain 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;
- rapidly increasing labor costs;
- failure by our suppliers, subcontractors, designers, engineers, joint venture partners or customers to perform their obligations;
- fraud, theft or other improper activities by our suppliers, subcontractors, designers, engineers, joint venture partners, customers or our own personnel;
- mechanical problems with our machinery or equipment;
- citations issued by any governmental authority, including OSHA;
- difficulties in obtaining required governmental permits or approvals;
- changes in applicable laws and regulations;
- delays in quickly identifying and taking measures to address issues which arise during execution of a project; and
- claims or demands from third parties for alleged damages arising from the design, construction or use and operation of a project of which our work is apart.

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. Public sector customers may seek to impose contractual risk-shifting provisions more aggressively, which could increase risks and adversely affect our cash flow, earnings and financial position.

Substantially all of the contracts in our Backlog contain "termination for convenience" clauses which allow the customer to cancel the contract at their election but require that the Company be remunerated for work performed through the date of termination; we have not been materially adversely affected by contract cancellations or modifications in the past. See the section below entitled, "Heavy Civil Construction Contracts — Contract Management Process."

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.

We rely on third-party subcontractors to perform some of the work on many of our projects and third party suppliers to provide most of the materials (including aggregates, cement, asphalt, concrete, steel, oil and fuel) for our contracts. We generally do not bid on contracts unless we have the key subcontractors committed for the anticipated scope of the contract and commitments from suppliers for the significant materials required to complete the contract, and at prices that we have included in our bid. Therefore, to the extent that we cannot engage subcontractors or obtain commitments from our suppliers for materials, our ability to bid for contracts may be impaired. In addition, if a subcontractor or supplier is unable to deliver its services or materials, 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 or materials from another source at a higher price or incur other unanticipated costs. 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, higher prices charged for petroleum-based products 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.

Recent and potential changes in U.S. trade policies and retaliatory responses from other countries may significantly increase the costs or limit supplies of materials and products used in our heavy civil and residential concrete construction projects.

The federal government recently imposed new or increased tariffs or duties on an array of imported materials and goods that are used in connection with our construction business, including steel, raising our costs for these items (or products made with them), and has threatened to impose further tariffs, duties and/or trade restrictions on imports. Foreign governments, including China and Canada, and trading blocs, such as the European Union, have responded by imposing or increasing tariffs, duties and/or trade restrictions on U.S. goods, and are reportedly considering other measures. These trading conflicts and related escalating governmental actions that result in additional tariffs, duties and/or trade restrictions could increase our construction costs further, cause disruptions or shortages in our supply chains and/or negatively impact the U.S., regional or local economies, and, individually or in the aggregate, materially and adversely affect our business and result of operations.

We may not accurately assess the quality, and we may not accurately estimate the quantity, availability and cost, of aggregates we need to complete a project, particularly for projects in rural areas.

Particularly for projects in rural areas, we may estimate the quality, quantity, availability and cost for aggregates (such as sand, gravel, crushed stone, slag and recycled concrete) from sources that we have not previously used to supply 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. If we fail to accurately assess the quality, quantity, availability and cost of aggregates, it could cause us to incur losses, which could materially adversely affect our results of operations.

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 service a significant portion of our contracts with our own construction equipment rather than leased or rented equipment. 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 utilize our own facilities to maintain the equipment in our fleet, we may be forced to obtain third-party repair services, which could increase our costs.

We are dependent on a limited number of heavy civil construction customers.

Due to the size and nature of our heavy civil 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. Similarly, our backlog frequently reflects multiple contracts for certain customers; therefore, one customer may comprise a significant percentage of backlog at a certain point in time. Our significant heavy civil customers, those greater than 10% of our consolidated revenues, accounted for approximately 15% of our revenue in 2018, 25% of our revenue in 2017 and 37% of our revenue in 2016. The loss of business from any one of such customers could have a material adverse effect on our business or results of operations. Also, a default or delay in payment on a significant scale by a customer could materially adversely affect our business, results of operations, cash flows and financial condition. See Note 16 - Concentration of Risk and Enterprise Wide Disclosures.

The heavy civil construction industry is highly competitive, with a variety of companies competing against 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.

In the past, a majority of the heavy civil construction contracts on which we bid were 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. For our design-build, CM/GC and other alternative methods of delivering projects, reputation, marketing efforts, quality of design and minimizing public inconvenience are also significant factors considered in awarding heavy civil construction contracts, in addition to cost. Within our geographic markets, we compete with many international, national, regional and local construction firms. Some of these competitors have achieved greater geographic market penetration than we have in the geographic markets in which we compete, and several of our competitors have greater financial and other resources than we do. In addition, a number of international and national companies in our industry that are larger than we are and that currently do not have a significant presence in our geographic markets, if they so desire, could establish a presence in our geographic markets and compete with us for contracts.

In addition, if the use of design-build, CM/GC and other alternative project delivery methods continues to increase and we are not able to further develop our capabilities and reputation in connection with these alternative delivery methods, we will be at a competitive disadvantage, which may have a material adverse effect on our financial position, results of operations, cash flows and prospects. If we are unable to compete successfully in our markets, our relative market share and profits could also be reduced.

A prolonged government shutdown may adversely affect our business.

We derive a significant portion of our heavy civil construction revenue from governmental agencies and programs. A prolonged government shutdown could impact inspections, regulatory review and certifications, grants, approvals, or cause other situations that could result in our incurring substantial labor or other costs without reimbursement under government contracts, or the delay or cancellation of key government programs in which we are involved, all of which could have a material adverse effect on our business and results of operations.

Our heavy civil construction business relies on highly competitive and highly regulated government contracts.

Government funding for public works projects is limited, thus creating a highly competitive environment for the limited number of public projects available. In addition, government contracts are subject to specific procurement regulations, contract provisions and a variety of regulatory requirements relating to their formation, administration, performance and accounting. Many of these contracts include express or implied certifications of compliance with applicable laws and contract provisions. As a result, any violations of these regulations could bring about litigation, including the possibility of qui tam (“Whistleblower”) litigation brought by private individuals on behalf of the government under the Federal Civil False Claims Act, and could cause termination of other existing government contracts and result in the loss of future government contracts. Due to the significant competition in the marketplace and the level of regulations on government contracts, we could suffer reductions in new projects and see lower revenues and profit margins on those projects, which could have a material adverse effect on the business, operating results and financial condition.

Our heavy civil construction business depends on our ability to qualify as an eligible bidder under government contract criteria and to compete successfully against other qualified bidders in order to obtain government contracts within our heavy civil business.

The U.S. government and various state and local government agencies conduct rigorous competitive processes for awarding many contracts. Some contracts include multiple award task order contracts in which several contractors are selected as eligible bidders for future work. We will face strong competition and pricing pressures for any additional heavy civil construction contract awards from the U.S. government and other government agencies, and we may be required to qualify or continue to qualify under various multiple award task order contract criteria. Our inability to qualify as an eligible bidder under government contract criteria could preclude us from competing for certain government contract awards. In addition, our inability to qualify as an eligible bidder, or to compete successfully when bidding for certain government contracts and to win those heavy civil construction contracts, could materially adversely affect our business, operations, revenues and profits.

Our heavy civil construction business is susceptible to economic downturns and reductions in government funding of infrastructure projects.

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. 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 since we are reliant upon contracts with state transportation departments for a significant portion of our revenues.

Refer to our “Business - Our Markets and Customers” section above for a more detailed discussion of our geographic markets.

Most of our significant heavy civil construction contracts can be canceled on short notice.

Our governmental contracts generally have clauses that permit the government to cancel the heavy civil construction contract unilaterally and at any time as long as the government pays for the work already completed. A cancellation of an unfinished contract could cause our equipment and work crews to be idle for a significant period of time until other comparable work becomes available, which could have a material adverse effect on our business and results of

operations.

The homebuilding industry is cyclical and susceptible to downward changes in general economic or other business conditions which could adversely affect our residential construction projects, including foundations for single-family and multi-family homes.

The residential homebuilding industry is sensitive to changes in economic conditions and other factors, such as the level of employment, consumer confidence, consumer income, availability of financing, and interest rate levels. Adverse changes in any of these conditions generally, or in the markets where we operate, could decrease demand and pricing for new homes in these areas or result in customer cancellations of pending contracts, which could adversely affect the number of concrete projects we construct or reduce the prices we can charge for these projects, either of which could result in a decrease in our revenues and earnings that could materially adversely affect our results of operations.

13

---



Although the U.S. housing market continues to recover, especially in the markets currently served by us, we cannot predict with certainty the overall trajectory of these markets or the duration of this trend due to changes in conditions that are beyond our control, including, but not limited to:

- Rising interest rates;
- Shortage of lots available for development;
- Changes in demographics and population migration that impair the demand for new housing;
- Labor shortages, especially craft labor, and rising costs of labor; and
- Changes in the tax laws that reduce the benefits of home ownership.

Our participation in heavy civil construction joint ventures exposes us to liability and/or harm to our reputation for failures of our partners.

As part of our business, we are a party to joint venture arrangements, pursuant to which we typically jointly bid on and execute particular projects with other companies in the construction industry. Success on these joint projects depends in part on whether our joint venture partners satisfy their contractual obligations.

We and our joint venture partners are generally jointly and severally liable for all liabilities and obligations of our joint ventures. If a joint venture partner fails to perform or is financially unable to bear its portion of required capital contributions or other obligations, including liabilities stemming from lawsuits, we could be required to make additional investments, provide additional services or pay more than our proportionate share of a liability to make up for our partner's shortfall. Furthermore, if we are unable to adequately address our partner's performance issues, the customer may terminate the project, which could result in legal liability to us, harm to our reputation and reduce our profit on a project.

In connection with acquisitions, certain counterparties to joint venture arrangements, which may include our historical direct competitors, may not desire to continue such arrangements with us and may terminate the joint venture arrangements or not enter into new arrangements. Any termination of a joint venture arrangement could cause us to reduce our backlog and could materially and adversely affect our business, results of operations and financial condition.

We may not be able to recover on claims or change orders against clients for payment or on claims against subcontractors for performance.

We occasionally present claims or change orders to our clients for additional costs exceeding a contract price or for costs not included in the original contract price. Change orders are modifications of an original contract that effectively change the provisions of the contract without adding new provisions. They generally include changes in specifications or design, facilities, equipment, materials, sites and periods for completion of work. Claims are amounts in excess of the agreed contract price (or amounts not included in the original contract price) that we seek to collect for customer-caused delays, errors in specifications and designs, contract terminations or other causes of unanticipated additional costs. These costs may or may not be recovered until the claim is resolved. In addition, we may have claims against subcontractors for performance or non-performance related issues which resulted in additional costs on a project. In some instances, these claims can be the subject of lengthy legal proceedings, and it is difficult to accurately predict when they will be fully resolved. A failure to promptly document and negotiate a recovery for change orders and claims could have a negative impact on our cash flows and overall ability to recover change orders and claims, which would have a negative impact on our financial condition, results of operations and cash flows.

We may fail to meet schedule or performance requirements of our heavy civil contracts.

In most cases, our heavy civil construction contracts require completion by a scheduled acceptance date. Failure to timely complete a project could result in additional costs, penalties or liquidated damages being assessed against us, and these could exceed projected profit margins on the contract.

The design-build project delivery method subjects us to the risk of design errors and omissions.

In the event of a design error or omission causing damages with respect to one of our design-build projects, we could be liable. Although by contract we pass design responsibility on to the engineering firms that we engage to perform design services on our behalf for these projects, in the event of a design error or omission causing damages, there is risk that the engineering firm, its professional liability insurance, and the errors and omissions insurance that they and we purchase will not fully protect us from costs or liabilities. Any liabilities resulting from an asserted design defect with respect to our heavy civil construction projects may have a material adverse effect on our financial position, results of operations and cash flows. Performance problems on existing and future heavy civil construction 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.

An inability to obtain bonding or post letters of credit could limit the aggregate dollar amount of heavy civil contracts that we are able to pursue.

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

Timing of the award and performance of new heavy civil contracts may fluctuate.

It is generally very difficult to predict whether and when new contracts will be offered for tender, as our heavy civil construction contracts frequently involve a lengthy and complex design and bidding process, which is affected by a number of factors, such as market conditions, funding 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 heavy civil construction 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.

We may be unable to attract and retain project managers, skilled labor and other key personnel.

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 for each of our subsidiaries management, project managers, estimators, supervisors, foremen, equipment operators and laborers. The loss of the services of any of our subsidiaries' management-level personnel 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. If competition for these employees is intense, 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 operations and future earnings may be negatively impacted.

We may be subject to unionization, work stoppages, slowdowns or increased labor costs.

In Arizona, California, Hawaii and Nevada a substantial number of our equipment operators and laborers are unionized. Additional groups of our employees may also unionize in the future. If at any time, a significant amount of our employees unionized, it could limit the flexibility of the workforce and could result in demands that might increase our operating expenses and adversely affect our profitability. Each of our different employee groups could unionize at any time and would require separate collective bargaining agreements. If any group of our employees were to unionize and we were unable to agree on the terms of their collective bargaining agreement or we were to experience widespread employee dissatisfaction, we could be subject to work slowdowns or stoppages. In addition, we may be subject to disruptions by organized labor groups protesting our non-union status. Any of these events would be disruptive to our operations and could have a material adverse effect on the business, operating results and financial condition.

15

---

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 as well as negative reputational impacts relating to health and safety matters.

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 maintain general liability and excess liability insurance, workers' compensation insurance, auto insurance and other types of insurance all in amounts consistent with our risk of loss and industry practice, but this insurance may not be adequate to cover all losses or liabilities that we may incur in our operations. In addition, if our safety record were to substantially deteriorate over time or were to suffer substantial penalties or criminal prosecution for violation of health and safety regulations, our customers could cancel our contracts or not award us future business.

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 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 and health claims, or unfavorable developments on existing claims, our operating results and financial condition could be materially and adversely affected.

If we are unable to comply with applicable immigration laws, our ability to successfully complete contracts may be negatively impacted.

We rely heavily on immigrant labor. We have taken steps that we believe are sufficient and appropriate to ensure compliance with immigration laws. However, we cannot provide assurance that we have identified, or will identify in the future, all undocumented immigrants who work for us. Our failure to identify undocumented immigrants who work for us may result in fines or other penalties being imposed upon us, which could have a material adverse effect on our operations, results of operations and financial condition.

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

Adverse weather conditions may cause delays, which could slow completion of our construction activity.

Because all of our construction projects are performed 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, in 2017 Hurricane Harvey caused damage and disruption that resulted in our inability to perform work on all Houston-area contracts for several days or weeks. Future evacuations in Texas due to hurricanes along the U.S. Gulf of Mexico coastal areas can delay our performance of work on contracts for several days or weeks or longer. Lengthy periods of wet or cold winter weather will generally interrupt construction, and this can lead to under-utilization of crews and equipment, resulting in less efficient rates of overhead recovery.

16

---

Extreme heat can prevent us from performing certain types of operations. During the late fall to the early spring months of each year, our work on construction projects in Nevada and Utah 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 cost of 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.

We rely on information technology systems to conduct our business, which are subject to disruption, failure or security breaches.

We rely on information technology (“IT”) systems in order to achieve our business objectives. We also rely upon industry accepted security measures and technology to securely maintain confidential information on our IT systems. However, our portfolio of hardware and software products, solutions and services and our enterprise IT systems may be vulnerable to damage or disruption caused by circumstances beyond our control such as catastrophic events, power outages, natural disasters, computer system or network failures, computer viruses, cyber-attacks or other malicious software programs. The failure or disruption of our IT systems to perform as anticipated for any reason could disrupt our business and result in decreased performance, significant remediation costs, transaction errors, loss of data, processing inefficiencies, downtime, litigation and the loss of suppliers or customers. A significant disruption or failure could have a material adverse effect on our business operations, financial performance and financial condition.

We are dependent on a small number of significant customers in our residential construction business.

Our customers are leading residential homebuilders. Several of these customers individually account for a significant portion of our residential construction business's sales in a normal year. In our residential construction business, D.R. Horton Inc., Pulte Homes Inc., HISTORYMAKER Homes, and Lennar, including their respective affiliates, accounted for approximately 72% and 67% of our revenue for the years ended December 31, 2018 and 2017, respectively. In addition, homebuilders are reliant upon growth in the housing market and the continued ability to purchase and develop land, which ultimately impact customers' demand for our residential construction services. The loss of any one or more of our significant customers could have a material adverse effect on our results of operations.

#### Risks Related to Our Financial Results, Financing and Liquidity

Our use of over time recognition (formally known as percentage-of-completion method) accounting related to our heavy civil construction projects could result in a reduction or elimination of previously reported revenue and profits.

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 heavy civil contract revenue over time. This method is used because management considers the cost-to-cost measure of progress to be the best measure of progress on these contracts.

Under this method, estimated contract revenue is recognized by applying the cost-to-cost measure of progress for the period (based on the ratio of costs incurred to total estimated costs of a contract) to the total estimated revenue for the contract. Contract estimates are based on various assumptions to project the outcome of future events that often span several years. These assumptions include labor productivity and availability, the complexity of the work to be performed, the cost and availability of materials and the performance of subcontractors. Changes in job performance, job conditions and estimated profitability, including those changes arising from contract penalty provisions and final contract settlements may result in revisions to costs and income and are recognized in the period in which the revisions are determined. These adjustments could result in both increases and decreases in profit margins or losses.

Actual results could differ from estimated amounts and could result in a reduction or elimination of previously recognized earnings. In certain circumstances, it is possible that such adjustments could be significant and could have an adverse effect on our business. 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 not be able to fully realize the revenue value reported in our Backlog.

Backlog as of December 31, 2018 totaled \$851 million in our heavy civil construction segment. Backlog develops as a result of new awards, which represent the potential revenue value realizable pursuant to new project commitments received by us during a given period.



Backlog is measured and defined differently by companies within our industry. We refer to “Backlog” as the unearned revenue we expect to earn in future periods on our executed heavy civil construction contracts. As the construction on our projects progresses, we increase or decrease Backlog to take into account signed contracts, revenue earned during the period and our estimates of the effects of changes in estimated quantities, changed conditions, change orders and other variations from previously anticipated contract revenues, including completion penalties and incentives. We cannot guarantee that the revenue projected in our Backlog will be realized, or if realized, will result in earnings. Most contracts may be terminated by our customers on short notice. In the event of a project cancellation, we may be reimbursed for certain costs but typically have no contractual right to recover the total revenue reflected in our Backlog. In addition to being unable to recover certain direct costs, canceled projects may also result in additional unrecoverable costs due to the resulting under-utilization of our assets or labor force. Backlog may not be realized or may not result in revenues or profits.

Given these factors, our Backlog at any point in time may not accurately represent the revenue that we expect to realize during any period, and our Backlog as of the end of a fiscal year may not be indicative of the revenue we expect to earn in the following fiscal year. Inability to realize revenue from our Backlog could have an adverse effect on our business.

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 and makes us more vulnerable to adverse economic and competitive conditions.

We have pledged the proceeds and other rights under our heavy civil construction contracts to our bond surety, and we have pledged substantially all of our other assets as collateral in connection with our Oaktree Facility. 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 Oaktree Facility, we must obtain the consent of our lenders to incur additional debt from other sources (subject to certain limited exceptions). In April 2017, we amended our certificate of incorporation to increase our authorized shares of common stock from 28 million shares to 38 million shares. 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 certain covenants under our Oaktree Facility that could limit our flexibility in managing our business and our ability to raise capital.

Our Oaktree Facility restricts us from engaging in certain activities, including our and certain of our subsidiaries' ability (subject to certain exceptions) to:

- create, incur, assume or permit to exist liens or encumbrances;
- incur additional indebtedness;
- dispose of a material portion of assets or merge or consolidate with a third party;
- sell assets;
- make loans;
- enter into acquisitions;
- incur capital expenditures;

make investments; and  
pay dividends.

18

---

Additionally, our Oaktree Facility also requires that we maintain certain financial covenants and prepay outstanding loans (in certain cases with a prepayment premium) with proceeds from the issuance of debt or equity, transfers, events of loss and extraordinary receipts. These requirements could limit our cash flow or impair our ability to conduct business and pursue business strategies. Further, our level of indebtedness could have important other consequences to our business, including the following:

- limiting our flexibility in planning for, or reacting to, changes in the industry in which we operate;
- increasing our vulnerability to general adverse economic and industry conditions;
- limiting our ability to fund future working capital and capital expenditures because of the need to dedicate a substantial portion of our cash flows from operations to payments on our debt service;
- placing us at a competitive disadvantage compared to our competitors that have less debt;
- limiting our ability to borrow additional funds or refinance existing debt; or
- requiring that we pledge substantial collateral, which may limit flexibility in operating our business and restrict our ability to sell assets.

These restrictions may interfere with our ability to obtain financings or engage in other business activities, which could have a material adverse effect on our results of operations, cash flows or financial condition.

Any failure to comply with the financial and other covenants in our Oaktree Facility may result in an event of default that could allow the creditors to accelerate maturities under the Oaktree Facility, which in turn may trigger cross-acceleration or cross-default provisions in other debt or bonding agreements. Our available cash and liquidity would not be sufficient to fully repay borrowings under all of our debt instruments that could be accelerated upon an event of default.

Our Oaktree Facility bears interest at an annual rate of the one-, two-, three- or six-month London Interbank Offered Rate, or LIBOR, plus 8.75%, subject to adjustment under certain circumstances. Accordingly, increases in interest rates could have a material adverse effect on our business operations, financial performance and financial condition.

The financial industry is currently transitioning away from LIBOR as a benchmark for the interbank lending market. While an orderly transition to a new benchmark is expected, a universal approach has not been adopted. It is uncertain as to the nature of any replacement rate and whether it will gain widespread market acceptance. Because our Oaktree Facility bears interest calculated by reference to LIBOR, we may be impacted by this transition, including by:

- the effect of uncertainty regarding the interest rate calculation before replacement benchmark is published regularly and gains widespread market acceptance;
- the risk that differences in the administration or determination methodology of the replacement benchmark may affect the amount of interest payments; or
- the potential need to amend our credit facility to specify a replacement reference rate via a consent solicitation, and whether necessary consent may be obtained at an acceptable cost or at all.

Our strategy of growing through strategic acquisitions may not be successful.

We may pursue growth through the acquisition of companies or assets that will enable us to broaden the types of projects we execute and also expand into new markets. We have completed several acquisitions and plan to consider strategic acquisitions in the future. We may be unable to implement this growth strategy if we cannot identify suitable companies or assets or reach agreement on potential strategic acquisitions on acceptable terms. Moreover, an acquisition involves certain risks, including:

- difficulties in the integration of operations, systems, policies and procedures;

enhancements in our controls and procedures including those necessary for a public company may make it more difficult to integrate operations and systems;

failure to implement proper overall business controls, including those required to support our growth, resulting in inconsistent operating and financial practices at companies we acquire or have acquired;

termination of relationships with the key personnel and customers of an acquired company;

additional financial and accounting challenges and complexities in areas such as tax planning, treasury management, financial reporting and internal controls;

the incurrence of environmental and other liabilities, including liabilities arising from the operation of an acquired business or asset prior to our acquisition for which we are not indemnified or for which the indemnity is inadequate;

disruption of or receipt of insufficient management attention to our ongoing business; and

inability to realize the cost savings or other financial benefits that we anticipate.

To service our indebtedness and to fund working capital, we will require a significant amount of cash. Our ability to generate cash depends on many factors that are beyond our control, including the fact that adverse capital and credit market conditions may affect our ability to meet liquidity needs, access to capital and cost of capital.

We do not have a revolving credit facility or letter of credit facility so our ability to meet our liquidity requirements, including to make payments on our indebtedness and to fund working capital requirements, will depend on our ability to generate cash in the future. This is subject to our operational performance, as well as general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control. We may be unable to expand our credit capacity, which could adversely affect our operations and business. Earnings from our operations and our working capital requirements can vary from period to period based primarily on the mix of our projects underway and the percentage of project work completed during the period. Capital expenditures may also vary significantly from period to period. We cannot provide assurance that our business will generate sufficient cash flow from operations or asset sales or that we can obtain future borrowing capacity in an amount sufficient to enable us to pay our indebtedness or to fund our other liquidity needs. Without sufficient liquidity, we will be forced to curtail our operations, and our business will suffer.

In the event these resources do not satisfy our liquidity needs, we may have to seek additional financing. The availability of additional financing will depend on a variety of factors such as market conditions, the general availability of credit, the volume of trading activities, our credit ratings and credit capacity, as well as the possibility that customers or lenders could develop a negative perception of our long- or short-term financial prospects if the level of our business activity decreased due to a market downturn. The domestic and worldwide capital and credit markets may experience significant volatility, disruptions and dislocations with respect to price and credit availability. Should we need additional funds or to refinance our existing indebtedness, we may not be able to obtain such additional funds. If internal sources of liquidity prove to be insufficient, we may not be able to successfully obtain additional financing on favorable terms, or at all.

We may need to refinance all or a portion of our indebtedness on or before maturity. We cannot provide assurance that we will be able to refinance any of our indebtedness on commercially reasonable terms or at all. Our inability to refinance our debt on commercially reasonable terms also could have a material adverse effect on our business. If we experience operational difficulties, we may need to increase our available borrowing capacity or seek amendments to the terms of our Oaktree Facility. There can be no assurance that we will be able to secure any additional capacity or amendment to our Oaktree Facility or to do so on terms that are acceptable to us, in which case, our costs of borrowing could rise and our business and results of operations could be materially adversely affected.

We must manage our liquidity carefully to fund our working capital.

The need for working capital for our business varies due to fluctuations in the following amounts, among other factors:

- 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; and
- the amounts owed to suppliers and subcontractors.

We may have limited cash on hand and the timing of payments on our contract receivables is difficult to predict. If the timing of payments on our receivables is delayed or the amount of such payments is less than expected, our liquidity and ability to fund working capital could be materially and adversely affected.



We may be required to write down all or part of our goodwill and intangibles.

We had \$85 million of goodwill and \$42 million of intangibles recorded on our consolidated balance sheet at December 31, 2018. Goodwill represents the excess of cost over the fair value of net assets acquired in business combinations reduced by any impairments recorded subsequent to the date of acquisition. Intangible assets are recognized as an asset apart from goodwill if it arises from contractual or other legal rights or if it is separable, that is, it is capable of being separated or divided from the acquired business and sold, transferred, licensed, rented or exchanged (whether there is intent to do so). A shortfall in our revenues or net income or changes in various other factors from that expected by securities analysts and investors could significantly reduce the market price of our common stock. If our market capitalization drops significantly below the amount of net equity recorded on our balance sheet, it might indicate a decline in our fair value and would require us to further evaluate whether our goodwill or intangible assets have been impaired. We perform an annual test of our goodwill and periodic assessments of intangible assets to determine if they have become impaired. On an interim basis, we also review the factors that have or may affect our operations or market capitalization for events that may trigger impairment testing. Write downs of goodwill and intangible assets may be substantial. If we were required to write down all or a significant part of our goodwill and/or intangible assets in future periods, our net earnings and equity could be materially adversely affected.

#### Item 1B. Unresolved Staff Comments

None.

#### Item 2. Properties

Our corporate headquarters are located in The Woodlands, Texas, in leased office space with a seven year term ending in 2021. Our executive, finance and accounting offices are located at this facility. We also lease an office located in Lafayette, Colorado for our information technology professionals.

##### Heavy Civil Construction

Our Texas operations owns an office building and land in Houston and San Antonio, Texas, and we lease office space and an equipment yard in Dallas, which houses it's management, project management and administrative functions.

Our Utah operations lease office space in Draper, Utah, and also repair facilities in West Jordan City, Utah from entities owned by our Chief Operations Officer and his family members. Refer to Note 17 - Related Party Transactions.

Our Nevada operations lease office space in Sparks, Nevada, and we own our office and repair facilities located in Lovelock, Nevada. In Nevada, we also own property that was previously used to source and produce our own aggregates.

Our Arizona, California and Hawaii operations lease office space in Phoenix, Sacramento and Honolulu, respectively. We also own a repair facility in Sacramento, California.

In order to complete most contracts, 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.

##### Residential Construction

Our Tealstone operations leases a combined office, construction and repair facility in Denton, Texas, which houses Tealstone's executive management, project management and administrative functions. The facility is leased from entities owned primarily by certain officers of Tealstone. Refer to Note 17 - Related Party Transactions.

All of our assets are encumbered, see Note 9 for further discussion on debt and the Oaktree facility.

### 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 in the future to have a material adverse impact on our consolidated results of operations, financial position or cash flows.

Item 4. Mine Safety Disclosures

Not applicable.

---

## Executive Officers of the Registrant

(At March 5, 2019)

The following is a list of the Company's executive officers, their ages, positions, offices and the year they became executive officers together with a brief description of their business experience.

Name	Age	Position/Offices	Executive Officer Since
Joseph A. Cutillo	53	Chief Executive Officer & Director	2017
Con L. Wadsworth	58	Executive Vice President & Chief Operating Officer	2016
Ronald A. Ballschmiede	63	Executive Vice President & Chief Financial Officer, Chief Accounting Officer & Treasurer	2015
Richard E. Chandler, Jr.	62	Executive Vice President, General Counsel & Secretary	2017

Each executive officer is appointed by the Board of Directors and, subject to the terms of any employment agreement he may have with the Company, holds office for such term as the Board of Directors may prescribe, or until his death, disqualification, resignation or removal. On December 12, 2018 the Company entered into employment agreements with Mr. Cutillo, Mr. Ballschmiede and Mr. Chandler.

Mr. Cutillo joined the Company in October 2015. In May 2017, he was appointed to the position of Chief Executive Officer and as a member of the Board of Directors. He was appointed President in February 2017. In May 2016, he was promoted to Executive Vice President & Chief Business Development Officer from Vice President - Strategy and Business Development. Prior to joining the Company, from August 2008 to October 2015, Mr. Cutillo was President and Chief Executive Officer of Inland Pipe Rehabilitation LLC, a private equity-backed trenchless pipe rehabilitation company, over which time he grew the business from a start-up acquisition to the second largest trenchless rehabilitation pipe business in the U.S.

Mr. Wadsworth joined RLW in 1976 serving in various capacities, including President of RLW. In March 2016 he was appointed as Executive Vice President & Chief Operating Officer of the Company.

Mr. Ballschmiede has been our Executive Vice President & Chief Financial Officer, Chief Accounting Officer & Treasurer since joining the Company in November 2015. From June 2006 until his retirement in March 2015, Mr. Ballschmiede was Executive Vice President & Chief Financial Officer of Chicago Bridge & Iron Company N.V. (CB&I), a leading engineering, procurement and construction contractor.

Mr. Chandler has been our Executive Vice President, General Counsel & Secretary since joining the Company in October 2017. Mr. Chandler served as Executive Vice President, Chief Legal Officer & Secretary of CB&I, a leading engineering, procurement and construction contractor from February 2011 to December 2016. He is a member of the State Bar of Texas.

## 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.

On February 28, 2019, there were 762 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. Additionally, our Oaktree Facility restricts the payout of 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 Oaktree 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 incorporated into Item 12. "Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters" from the Company's proxy statement for its 2019 Annual Meeting of Stockholders. Additionally, information related to the Company's Stock buyback plan is incorporated subsequently in "Issuer Purchases of Equity Securities".

#### 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 Total Return 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 2013 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.

\*\$100 invested on December 31, 2013 in stock or index, including reinvestment of dividends.  
Fiscal year ending December 31.

Copyright© 2019 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved.

	December 2013 (\$)	December 2014 (\$)	December 2015 (\$)	December 2016 (\$)	December 2017 (\$)	December 2018 (\$)
Sterling Construction Company, Inc.	100.00	54.48	51.83	72.12	138.79	92.84
Dow Jones US Total Return Index	100.00	112.95	113.66	127.59	155.01	147.30
Dow Jones US Heavy Construction Index	100.00	74.48	65.89	81.29	85.65	63.28

25

---

## Issuer Purchases of Equity Securities

The following table shows, by month, the number of shares of the Company's common stock that the Company repurchased from employees in the quarter ended December 31, 2018. These shares were repurchased from employees holding shares of the Company's common stock that had been awarded to them by the Company and that were released from Company-imposed transfer restrictions. The repurchase was to enable the employees to satisfy the Company's tax withholding obligations occasioned by the release of the restrictions. The repurchase was made at the election of the employees pursuant to a procedure adopted by the Compensation and Talent Development Committee of the Board of Directors.

Period	Total Number of Shares Purchased	Average Price Paid per Share
October 1 – October 31, 2018	3,279	\$ 11.53
November 1 – November 30, 2018	1,100	\$ 12.87
December 1 – December 31, 2018	—	\$ —

On November 2, 2018, the Board of Directors approved a plan that authorized stock repurchases of up to 2.0 million shares of the Company's common stock. Under the plan, the Company may repurchase its common stock in the open market or through privately negotiated transactions at such times and at such prices as determined to be in the Company's best interest. The amount and timing of any purchases will depend on a number of factors, including the Company's liquidity position and trading price, trading volume and general market conditions. No assurance can be given that any particular amount of common stock will be repurchased. This repurchase program expires on June 30, 2020 and may be modified, extended or terminated by the Board at any time. The table below sets forth the Company's share repurchase during the last fiscal quarter.

Period	Total Number of Shares Purchased	Average Price Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Program	Maximum Number (or Appropriate Dollar Value) of Shares that May Yet be Purchased Under the Plans or Programs
October 1 – October 31, 2018	—	\$ —	—	—
November 1 – November 30, 2018	—	—	—	—
December 1 – December 31, 2018	466,519	10.27	466,519	1,533,481
Total 2018	466,519	\$ 10.27	466,519	1,533,481

## 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.” Amounts are in thousands, except per share data:

	2018	2017	2016	2015	2014
Revenues	\$1,037,667	\$957,958	\$690,123	\$623,595	\$672,230
Income (loss) income before income taxes and earnings attributable to noncontrolling interests	\$31,278	\$15,935	\$(7,324)	\$(17,179)	\$(4,593)
Income tax expense	(1,738)	(118)	(88)	(7)	(632)
Net income (loss)	29,540	15,817	(7,412)	(17,186)	(5,225)
Noncontrolling owners’ interests in earnings of subsidiaries and joint ventures	(4,353)	(4,200)	(1,826)	(3,216)	(4,556)
Net income (loss) attributable to Sterling common stockholders before noncontrolling interest revaluation	25,187	11,617	(9,238)	(20,402)	(9,781)
Revaluation of noncontrolling interest due to a new agreement or a put/call liability reflected in additional paid-in capital or retained earnings, net of tax	—	—	—	(18,774)	—
Net income (loss) attributable to Sterling common stockholders	\$25,187	\$11,617	\$(9,238)	\$(39,176)	\$(9,781)
Net income (loss) per share attributable to Sterling common stockholders:					
Basic	\$0.94	\$0.44	\$(0.40)	\$(2.02)	\$(0.54)
Diluted	0.93	0.43	(0.40)	(2.02)	(0.54)
Weighted average number of common shares outstanding used in computing per share amounts:					
Basic	26,903	26,274	23,140	19,375	18,063
Diluted	27,194	26,712	23,140	19,375	18,063
Cash dividends declared	\$—	\$—	\$—	\$—	\$—
Balance sheet:					
Total assets	\$482,573	\$463,298	\$301,823	\$266,165	\$306,451
Long-term debt	\$79,117	\$86,160	\$1,549	\$15,324	\$37,021
Equity attributable to Sterling common stockholders	\$164,401	\$141,333	\$107,434	\$95,845	\$133,686
Shares outstanding	27,064	27,051	24,987	19,753	18,803

## Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Overview

Sterling Construction Company, Inc. is a construction company that specializes in heavy civil infrastructure construction and infrastructure rehabilitation as well as residential construction projects. We operate primarily in Arizona, California, Colorado, Hawaii, Nevada, Texas and Utah, as well as other states in which there are feasible construction opportunities. Heavy civil construction projects include highways, roads, bridges, airfields, ports, light rail, water, wastewater and storm drainage systems, foundations for multi-family homes, commercial concrete projects and parking structures. Residential construction projects include concrete foundations for single-family homes.

On April 3, 2017, the Company consummated the acquisition of 100% of the outstanding stock of Tealstone and entered into the Oaktree Facility providing for a term loan of \$85 million with a maturity date of April 4, 2022, which replaced the then existing debt facility. We have determined that with the acquisition of Tealstone there are two reportable segments: heavy civil construction and residential construction. Refer to Note 18 - Segment Information for a discussion of reportable segments and related financial information.

### 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, the 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. Certain of the Company's accounting policies require higher degrees of judgment than others in their application. These include the recognition of revenue and earnings from construction contracts earned over time, the valuation of long-lived assets, income taxes and purchase accounting. Management continually evaluates all of its estimates and judgments based on available information and experience; however, actual amounts could differ from those estimates.

### Critical Accounting Policies

On an ongoing basis, the Company evaluates the critical accounting policies used to prepare its consolidated financial statements, including, but not limited to, those related to:

- Revenue recognition
- Valuation of long-lived assets and goodwill
- Income taxes

Our significant accounting policies are described in Note 1 - Summary of Business and Significant Accounting Policies to the consolidated financial statements, and conform to the Financial Accounting Standards Board's Accounting Standards Codification (or GAAP or ASC).

### Revenue Recognition

#### Heavy Civil Construction

The Company engages in various types of heavy civil construction projects principally for public (government) owners. Credit risk is minimal with public owners since the Company ascertains that funds have been appropriated by the governmental project owner prior to commencing work on such projects. The majority of our public contracts are fixed unit price contracts. 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). While most public contracts are subject to termination at the election of the government entity, in the event of termination the Company is entitled to receive the contract price for completed work and reimbursement of termination-related costs. Credit risk with private owners is minimized because of statutory mechanic's liens, which give the Company high priority in the event of lien foreclosures following financial difficulties of private owners.

Our contracts generally take 12 to 36 months to complete. The Company primarily provides a one-year warranty, two-year in rare cases, for workmanship under its contracts when completed. Warranty claims historically have been insignificant.



Revenues are recognized over time (formerly known as percentage-of-completion method), using the ratio of costs incurred to estimated total costs for each contract. This cost to cost measure is used because management considers it to be the best available measure of progress on these contracts. Contract costs include all direct material, labor, subcontract and other costs and those indirect costs related to contract performance, such as indirect salaries and wages, equipment repairs and depreciation, insurance and payroll taxes. Administrative and general expenses are charged to expense as incurred. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined. Changes in job performance, job conditions and estimated profitability, including those changes arising from contract penalty provisions and final contract settlements may result in revisions to costs and income and are recognized in the period in which the revisions are determined.

Contracts receivable are generally based on amounts billed to the customer and currently due in accordance with our contracts. Many of the contracts under which the Company performs heavy civil construction work contain retainage provisions. Retainage refers to that portion of billings made by the Company, but held for payment by the customer pending satisfactory completion of the project. Retainage is classified as a current asset regardless of the term of the contract and is generally collected within one year of the completion of a contract. At December 31, 2018 and 2017, contracts receivable included \$47.4 million and \$43.5 million of retainage, respectively, which is being contractually withheld by customers until milestones specified in the contract are complete.

Change orders are modifications of an original contract that effectively change the existing provisions of the contract without adding new provisions or terms. Change orders may include changes in specifications or designs, manner of performance, facilities, equipment, materials, sites and period of completion of the work. Either we or our customers may initiate change orders.

The Company considers unapproved change orders to be contract variations involving a change of scope for which we believe we are contractually entitled to additional revenue, but the change associated with the scope has not yet been agreed upon with the customer. Costs associated with unapproved change orders are included in the estimated cost to complete the contracts and are treated as project costs as incurred. The Company recognizes revenue equal to costs incurred on unapproved change orders when realization of price approval is probable. Unapproved change orders involve the use of estimates, and it is reasonably possible that revisions to the estimated costs and recoverable amounts may be required in future reporting periods to reflect changes in estimates or final agreements with customers. Change orders that are unapproved as to both price and scope are evaluated as claims.

The Company considers claims to be amounts in excess of agreed contract prices that we seek to collect from our customers or others for customer-caused delays, errors in specifications and designs, contract terminations, change orders that are either in dispute or are unapproved as to both scope and price, or other causes of unanticipated additional contract costs. Claims are included in the calculation of revenue when realization is probable and amounts can be reliably determined to the extent costs are incurred. To support these requirements, the existence of the following items must be satisfied: (i) the contract or other evidence provides a legal basis for the claim; or a legal opinion has been obtained, stating that under the circumstances there is a reasonable basis to support the claim; (ii) additional costs are caused by circumstances that were unforeseen at the contract date and are not the result of deficiencies in the contractor's performance; (iii) costs associated with the claim are identifiable or otherwise determinable and are reasonable in view of the work performed; and (iv) the evidence supporting the claim is objective and verifiable, not based on management's feel for the situation or on unsupported representations. Revenue in excess of contract costs incurred on claims is recognized when an agreement is reached with customers as to the value of the claims, which in some instances may not occur until after completion of work under the contract. Costs associated with claims are included in the estimated costs to complete the contracts and are treated as project costs when incurred.

The Company has projects where we are in the process of negotiating, or awaiting final approval of, unapproved change orders and claims with our customers. The Company is proceeding with its contractual rights to recoup additional costs incurred from its customers based on completing work associated with change orders, including change orders with pending change order pricing, or claims related to significant changes in scope which resulted in substantial delays and additional costs in completing the work. Unapproved change order and claim information has been provided to our customers and negotiations with the customers are ongoing. If additional progress with an acceptable resolution is not reached, legal action will be taken.

The accuracy of our revenue and profit recognition in a given period is dependent on the accuracy of our estimates of the revenues and costs to finish uncompleted contracts. Our estimates for all of our significant contracts use a highly detailed “bottom up” approach. However, our projects 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 projects 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 project 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.

### Residential Construction

Residential construction revenue and related profit are recognized when construction on the concrete foundation unit is completed. Residential construction employs an assembly line construction process to perform the majority of this concrete construction services. We assign to our subcontractors different, but sequential tasks at a particular job site. This assembly line process minimizes potential bottlenecks and increases productivity. Residential construction agreements are negotiated up front with the customer. The time from starting construction to finishing is typically less than one month.

### Valuation of Long-Lived Assets and Goodwill

Long-lived assets, which include property, equipment and acquired intangible assets, including goodwill, 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 fair values and 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. For the years ended December 31, 2018 and 2017, there were no events or changes in circumstances that would indicate a material impairment of our long-lived assets.

We test goodwill for impairment at least annually and we performed our most recent annual impairment test of historical goodwill as of October 1, 2018. Our test indicated there was no impairment of goodwill for our heavy civil construction or residential construction reporting units. See “Segment Reporting” below for further information regarding the determination of our reporting units. Note 8 - Goodwill and Other Intangibles discusses the valuation approach used by the Company to determine the fair value of the Company’s equity for purposes of evaluating whether there is an indication of goodwill impairment. During the 2018 and 2017 annual test, we used a qualitative assessment to determine if it is more likely than not that an impairment exists. Factors considered include macroeconomic, industry and competitive conditions, financial performance and reporting unit specific events. These are discussed in a number of places including “Item 1A. Risk Factors.” No impairments were recorded to our goodwill during the years ended December 31, 2018, 2017 and 2016. At December 31, 2018 and 2017, we had goodwill with a carrying amount of \$85.2 million.

### Income Taxes

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act makes broad and complex changes to the U.S. tax code, including, but not limited to, (1) reducing the U.S. federal corporate tax rate from 35 percent to 21 percent; (2) eliminating the corporate alternative minimum tax (AMT) and changing how existing AMT credits can be realized; (3) creating a new limitation on deductible interest expense; and (4) changing rules related to uses and limitations of net operating loss carryforwards created in tax years beginning after December 31, 2017; (5) expanding the limitation for executive compensation deductions; and (6) implementing 100% immediate expensing of qualified property. As a result of the reduced federal corporate tax rate under the Tax Act, the Company has reduced the value of its net deferred tax assets \$19.3 million to reflect the enacted rate. This reduction in 2017 was entirely offset with a corresponding reduction of our valuation allowance, which resulted in no charge to the tax provision for the year. The Tax Act also provides that existing AMT credit carryforwards are refundable beginning in 2018. The Company has approximately \$0.2 million of AMT credit carryforwards that are expected to be fully refunded by 2022. Therefore, we have recorded a tax benefit and receivable for these credits in our December 31, 2017 financial statements.

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. Deferred tax liabilities are a consideration in the analysis of whether to apply a valuation allowance because taxable temporary differences may be used as a source of taxable income to support the realization of deferred tax assets. A deferred tax liability that relates to an asset with an indefinite life, such as goodwill, may not be considered a source of income and should not be netted against deferred tax assets for valuation allowance purposes. The Company has a deferred tax liability for the excess of book over tax basis difference in its goodwill. A \$1.5 million deferred tax expense has been recorded to reflect this liability.

Valuation allowances are established to reduce deferred tax assets if we determine that it is more likely than not (e.g., a likelihood of more than 50%) that some or all of the deferred tax assets will not be realized in future periods. Management assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to use the existing deferred tax assets. This assessment includes any impact from the newly enacted Tax Act. A significant piece of objective negative evidence evaluated was the recurring historical losses from 2013 to 2016 and the first quarter of 2017. Such objective evidence limits the ability to consider other subjective evidence such as our projections for future growth. On the basis of this evaluation, as of December 31, 2018, the Company continued to maintain a valuation allowance of \$31.7 million on the net deferred tax assets including federal and state net operating losses as they are not likely to be realized. The amount of the deferred tax asset considered realizable, however, could be adjusted in the future if objective negative evidence or cumulative losses are no longer present and additional weight may be given to subjective evidence such as our projections for growth. Deferred tax liabilities are a consideration in the analysis of whether to apply a valuation allowance because taxable temporary differences may be used as a source of taxable income to support the realization of deferred tax assets.

If our estimates or assumptions regarding our current and deferred tax items are inaccurate or are modified, these changes could have potentially material impacts on our earnings.

## Market Outlook and Trends

### Heavy Civil Construction

Sterling's heavy civil construction business is primarily driven by federal, state and municipal funding. Federal funds, on average, provide 50% of annual State Department of Transportation (DOT) capital outlays for highway and bridge projects. Several of the states in Sterling's key markets have instituted actions to further increase annual spending. In November 2018, various state and local transportation measures were passed securing, and in some cases increasing, funding of \$1.57 billion in California, \$1.27 billion in Texas, \$528.5 million in Arizona, \$128.2 million in Colorado and \$87 million in Utah. In October 2018, the Federal Aviation Administration reauthorized \$3.35 billion annually for the next five years. This reauthorization also includes more than \$1 billion a year for airport infrastructure grants and about \$1.7 billion for disaster relief.

In Texas, two constitutional amendments were passed in 2015, which will increase the annual funds allocated to transportation projects from \$4.0 billion to \$4.5 billion per year. Texas also has locally approved bonds estimated at \$1.3 billion that were approved in November 2017. In Utah, a 20% gas tax increase to support infrastructure projects was put into effect January 2016, which is the first state gas tax increase in 18 years. The State of Utah also approved, in 2017, a \$1 billion bond package for infrastructure improvements. A 1-cent sales tax increase was approved in Los Angeles, California in 2016 that will provide \$3 billion per year for local road, bridge and transit projects. In addition, California approved a 10 year \$52 billion bill that provides an annual \$5 billion in incremental funding for use on highway transit repair projects.

In addition to the state locally funded actions, Sterling is in year four of the 2015 federally funded five-year \$305 billion surface transportation bill that increased the annual federal highway investment by 15.1% over the five-year period from 2016 to 2020. Should the federal government approve substantive, incremental infrastructure investment in 2019, it would be an additional growth catalyst; however, it would be unlikely to create significant business impact before 2020 or 2021. See “Item 1. Business—Our Markets, Competition and Customers” for a more detailed discussion of its markets and their funding sources.

#### Bid Discipline and Project Execution

To ensure that the Company takes full advantage of the improved market conditions and maximize profitability, Sterling has completed an extensive evaluation of its historical success on heavy civil construction projects based on project size, end customer, product delivered and geography. The knowledge gained has now been incorporated into a more formal and rigorous bid evaluation and approval process which, along with the institution of common processes, will enable the Company to focus its resources on the most beneficial projects and significantly reduce its risk.

## Backlog

At December 31, 2018, our Backlog of construction projects, made up solely of our heavy civil construction segment, was \$850.7 million, as compared to \$744.4 million at December 31, 2017. The contracts in Backlog are typically completed in 12 to 36 months. Contracts in which we are the apparent low bidder for projects (“Unsigned Low-bid Awards”) are excluded from Backlog until the contract is executed by our customer. Unsigned Low-bid Awards were \$292.7 million at December 31, 2018 and \$250.2 million at the end of 2017. The combination of our Backlog and Unsigned Low-bid Awards, which we refer to as “Combined Backlog” totaled \$1.1 billion and \$1.0 billion as of December 31, 2018 and 2017, respectively. Backlog includes \$33.6 million and \$55.1 million attributable to our share of estimated revenues related to joint ventures where we are a noncontrolling joint venture partner at December 31, 2018 and 2017, respectively. We anticipate that approximately 75% of our Backlog will be recognized as revenues during 2019, with substantially all remaining recognized in the twelve months following.

Heavy civil contracts-in-progress which were not substantially complete totaled 149 and 164 at December 31, 2018 and 2017, respectively. These contracts are of various sizes, of different expected profitability and in various stages of completion. The nearer a contract progresses toward completion, the more visibility we have in refining our estimate of total revenues (including incentives, delay penalties and change orders), costs and gross profit. Thus, gross profit as a percent of revenues can increase or decrease from comparable and sequential quarters due to variations among contracts and depending upon the stage of completion of contracts.

We expect that our markets will continue to improve, driven by the conditions discussed in “Item 1. Business.” Furthermore, we believe that the Company is well-established in our particular markets and has the management depth and experience which gives us the ability to perform a broad range of work that will allow us to succeed in current market conditions and to continue to compete successfully for projects as they become available at acceptable profit margin levels. See “Item 1. Business — Our Markets and Customers” for a more detailed discussion of our markets.

### Backlog and gross margin:

	Backlog	Gross Margin in Backlog
	(Dollar amounts in thousands)	
Fourth quarter of 2018	\$850,725	8.5%
Third quarter of 2018	\$832,815	8.7%
Second quarter of 2018	\$884,611	8.2%
First quarter of 2018	\$884,622	8.1%
Fourth quarter of 2017	\$744,389	8.4%

Our total margin in Backlog has increased approximately 10 basis points, from 8.4% at December 31, 2017 to 8.5% at December 31, 2018. Our Unsigned Low-bid Awards were \$292.7 million at an average margin of 9.9% at December 31, 2018. The increases noted above are primarily the result of the improving market conditions and actions that we have taken to improve bid discipline.

### Residential Construction

Sterling's residential construction business was a component of the Tealstone acquisition. Continuing revenue growth of its residential construction business is directly related to the growth of new home starts in its key markets. The Company's core customer base is primarily made up of leading national home builders as well as regional and custom home builders. Sterling's customers' average growth during 2018 was approximately 10% in the Dallas-Fort Worth Metroplex. During 2018, Sterling initiated the expansion of the residential business into the Houston market and surrounding areas.





Edgar Filing: STERLING CONSTRUCTION CO INC - Form 10-K

Fiscal Year Ended December 31, 2018 Compared with Fiscal Year Ended December 31, 2017

	2018	2017	% Change	
	(Dollar amounts in thousands)			
Revenues	\$1,037,667	\$957,958	8.3	%
Gross profit	110,332	\$89,092	23.8	%
General and administrative expenses	(50,620 )	(48,351 )	4.7	%
Other operating expense, net	(17,101 )	(14,565 )	17.4	%
Operating income	42,611	26,176	62.8	%
Interest income	1,017	314	223.9	%
Interest expense	(12,350 )	(9,800 )	26.0	%
Loss on extinguishment of debt	—	(755 )	NM	
Income before income taxes and noncontrolling interests in earnings	31,278	15,935	96.3	%
Income tax expense	(1,738 )	(118 )	NM	
Net income	29,540	15,817	86.8	%
Noncontrolling interests in earnings	(4,353 )	(4,200 )	3.6	%
Net income attributable to Sterling common stockholders	\$25,187	\$11,617	116.8	%
Gross margin	10.6	% 9.3	% 14.0	%
Operating margin	4.1	% 2.7	% 51.9	%
Backlog, end of year	\$850,725	\$744,389	14.3	%
NM – Not meaningful.				

#### Revenues

Revenues for 2018 increased \$79.7 million, or 8%, compared with the prior year. The increase is attributable to organic growth of \$37.9 million and the inclusion of twelve months of revenue in 2018 from Tealstone operations compared to nine months in 2017 of \$41.8 million.

#### Gross profit

Gross profit increased \$21.2 million, or 24%, in 2018 compared with the prior year. Gross margin also increased to 10.6% in 2018 from 9.3% in 2017. Approximately \$6.9 million of the year over year increase in gross profit was attributable to the inclusion of a full year of revenues from Tealstone. The remaining gross profit increase reflects improved performance by heavy civil construction driven by higher gross margins in opening backlog and the substantial completion of heavy civil construction projects in Hawaii and the Rocky Mountain region.

#### General and administrative expenses

General and administrative expenses increased \$2.3 million during 2018 to \$50.6 million from \$48.4 million in 2017. This increase is primarily from the inclusion of twelve months compared to nine months of cost and associated growth of Tealstone and increased bid pursuit costs in our heavy civil business.

As a percentage of revenues, general and administrative expenses decreased to 4.9% in 2018 from 5.0% in 2017. The decrease in general and administrative expenses, as a percentage of revenue, is primarily the result of the leverage

generated from generally fixed costs and increases in revenues.

33

---

### Other operating expense, net

Other operating expense, net, includes Members' interest, acquisition earn-out expense and other miscellaneous operating income or expense. Other operating expense, net, increased to \$17.1 million in 2018 from \$14.6 million in 2017, driven primarily from an increase in Members' interest earnings of approximately \$3.6 million, partially offset by a reduction in the loss on the sale of an asset and reduced acquisition costs from 2017. See Note 5 - Consolidated 50% Owned Subsidiaries, including Variable Interest Entities ("VIE").

### Interest expense

Interest expense for the year ended December 31, 2018 was \$12.4 million compared to \$9.8 million in 2017. The increase in interest costs is due to increased borrowings to replace our Equipment-based Facility and complete the Tealstone acquisition, the result of twelve months of interest included in 2018 compared to nine months in 2017, and higher interest rates.

### Loss on extinguishment of debt

As part of the replacement of our Equipment-based Facility, \$0.8 million in debt extinguishment costs was expensed and included as a "loss on extinguishment of debt" on our statement of operations for the year ended December 31, 2017.

### Income taxes

Our effective income tax rate for 2018 and 2017 was minimal. In 2018 and 2017, our effective income tax rate varied from the statutory rate primarily as a result of the utilization of federal income tax carryforwards which resulted in a change in valuation allowance on our net deferred tax assets. The Company has a deferred tax liability for the excess of book over tax basis difference in its goodwill. A \$1.5 million deferred tax expense has been recorded to reflect this liability.

### Net income attributable to noncontrolling interests

Net income attributable to noncontrolling interest in both 2018 and 2017 relates to two joint venture projects in the Rocky Mountain region, in which we hold the majority interest. Both of these projects are substantially complete at the end of 2018.

### Segment Results

	Year Ended December 31,			
	2018	% of Total	2017	% of Total
<b>Revenue</b>				
Heavy Civil Construction	\$885,971	85%	\$849,966	89%
Residential Construction	151,696	15%	107,992	11%
Total Revenue	\$1,037,667		\$957,958	
<b>Operating Income</b>				
Heavy Civil Construction	\$21,524	51%	\$10,822	41%
Residential Construction	21,087	49%	15,354	59%
Total Operating Income	\$42,611		\$26,176	

## Heavy Civil Construction

### Revenues

Heavy civil construction revenues were \$886 million for the year ended December 31, 2018, which represented an increase of \$36 million, compared to 2017. Approximately \$106 million was related to an increase in commercial and aviation projects, partially offset by a decrease in heavy highway of \$65 million primarily from our two large construction joint venture projects in the Rocky Mountain region. The overall increase is partially attributable to our focus on growing higher margin products and the remainder to the inclusion of a full year of Tealstone Commercial in 2018 compared to nine months in 2017. The balance of the revenue growth was generated across our geographic operations reflecting the improving heavy civil construction market.

## Operating income

Operating Income was \$21.5 million for the year ended December 31, 2018, an increase of \$10.7 million, in our heavy civil construction segment compared to 2017. The improvement was primarily the result of higher gross margins driven by improved bid discipline, project management and project execution of \$14.2 million and additional gross profit from the increased volume of approximately \$3.3 million. These increases were partially offset by increases in general and administrative expense of \$2.3 million, from increased bid pursuit costs and also the inclusion of a full twelve months of Tealstone commercial in 2018 compared to nine months in 2017. Finally, other operating expenses increased as a result of an additional \$3.6 million of Members' interest expense driven by higher 2018 earnings levels from our Consolidated 50% owned subsidiaries.

## Residential Construction

### Revenues

Our residential construction segment was a component of the Tealstone acquisition acquired on April 3, 2017. Its principal market is Texas, specifically the Dallas-Fort Worth Metroplex area. The core customer base for residential construction segment is primarily made up of leading national home builders, as well as regional and custom home builders. Residential construction initiated the expansion into the Houston market and surrounding communities in 2018. Our residential construction segment contributed \$151.7 million in revenue during 2018 compared to \$108 million in 2017. The year over year increase of \$43.7 million is attributable to \$12.5 million of organic growth and the remaining \$31.2 million a result of twelve months of revenues included in 2018 compared to nine months in 2017.

### Operating income

The residential construction segment operating income increased to \$21.1 million in 2018 from \$15.4 million in 2017. The increase in operating income reflects twelve months in 2018 compared to nine months in 2017 and additional volume from revenues as described above. We continue to see volume increases comparable to our customers' growth rates.

Fiscal Year Ended December 31, 2017 Compared with Fiscal Year Ended December 31, 2016

	2017	2016	% Change	
	(Dollar amounts in thousands)			
Revenues	\$957,958	\$690,123	38.8	%
Gross profit	\$89,092	\$42,058	111.8	%
General and administrative expenses	(48,351 )	(36,844 )	31.2	%
Other operating expense, net	(14,565 )	(9,943 )	46.5	%
Operating income	26,176	(4,729 )	NM	
Interest income	314	33	NM	
Interest expense	(9,800 )	(2,628 )	272.9	%
Loss on extinguishment of debt	(755 )	—	100	%
Income (loss) before income taxes and earnings attributable to noncontrolling interests	15,935	(7,324 )	NM	
Income tax expense	(118 )	(88 )	34.1	%
Net income (loss)	15,817	(7,412 )	NM	
Noncontrolling owners' interests in earnings of subsidiaries	(4,200 )	(1,826 )	130.0	%
Net (income) loss attributable to Sterling common stockholders	11,617	(9,238 )	NM	
Gross margin	9.3	% 6.1	% 52.5	%
Operating margin (deficit)	2.7	% (0.7 )	% NM	
Backlog, end of year	\$744,389	\$823,000	(9.6	)%
NM – Not meaningful.				

### Revenues

Revenues for 2017 increased \$267.8 million, or 38.8%, compared with the prior year. Approximately one half of the increase year over year is attributable to the inclusion of approximately nine months of revenues from Tealstone which we acquired on April 3, 2017. The balance of revenue growth was attributable to improved activity in our heavy civil construction, primarily to large construction joint venture projects and other projects in the Rocky Mountain region.

### Gross profit

Gross profit increased \$47.0 million, or 112% in 2017 compared with the prior year. Gross margin also increased to 9.3% in 2017 from 6.1% in 2016. Approximately one half of the year over year increase in gross profit was attributable to the inclusion of approximately nine months of revenues from the Tealstone Acquisition. The remaining gross profit increase reflects the increased revenue and gross profit attributable to the heavy civil construction projects.

At December 31, 2017, we had approximately 164 contracts-in-progress which were less than 90% complete of various sizes, of different expected profitability and in various stages of completion. The nearer a contract progresses toward completion, the more visibility we have in refining our estimate of total revenues (including incentives, delay penalties and change orders), costs and gross profit. Thus gross profit as a percent of revenues can increase or decrease from comparable and sequential quarters due to variations among contracts and depending upon the stage of

completion of contracts.

Based upon our review of the provisions of our contracts, specific costs incurred and other related evidence supporting the unapproved change orders, claims and our entitled unpaid project price, together with the views of the Company's outside claim consultants, Sterling concluded that it was appropriate to include in project price amounts of \$10.0 million at December 31, 2017 and \$15.3 million at December 31, 2016, in "Costs and estimated earnings in excess of billings on uncompleted contracts" on our consolidated balance sheets. We expect these matters will be resolved without a material adverse effect on our financial statements. However, unapproved change order and claim amounts are subject to negotiations which may cause actual results to differ materially from estimated and recorded amounts.

36

---

### General and administrative expenses

General and administrative expenses increased \$11.5 million during 2017 to \$48.4 million from \$36.8 million in 2016. This increase is primarily the result of \$3.7 million attributable to the inclusion of approximately nine months of Tealstone operations, \$1.0 million attributable to higher stock-based and incentive compensation and \$1.4 million attributable to higher pre-bid contract and recruiting costs in the Rocky Mountain region.

As a percentage of revenues, general and administrative expenses decreased to 5.0% in 2017 from 5.3% in 2016. The decrease in general and administrative expenses, as a percentage of revenue, is primarily the result of the leverage generated from generally fixed costs and increases in revenues.

### Other operating expense, net

Other operating expense, net, includes 50% of earnings related to Members' interests, gains and other miscellaneous operating income or expense. Members' interest earnings are treated as an expense and increase to our liability account. Other operating expense, net increased to \$14.6 million in 2017 from \$9.9 million in 2016, driven primarily from an increase in Members' interest earnings of approximately \$2.4 million, \$0.5 million related to our earn-out expense, a loss of \$1.1 million from the sale of a facility and \$0.6 million of acquisition related costs.

### Income taxes

Our effective income tax rate for 2017 and 2016 were minimal in both periods. In 2017 and 2016, our effective income tax rate varied from the statutory rate primarily as a result of taxes on subsidiaries' and joint ventures' earnings allocated to noncontrolling interests, tax credits, and the change in valuation allowance.

### Net income attributable to noncontrolling interests

The increase of \$2.4 million to \$4.2 million from \$1.8 million in net income attributable to noncontrolling interest owners for the year ended December 31, 2017 compared with the same period in 2016 is driven by increased activity in our construction joint venture projects in the Rocky Mountain region, in which we hold the majority interest.

### Segment Results

	Year Ended December 31,			
	2017	% of Total	2016	% of Total
Revenue				
Heavy Civil Construction	\$ 849,966	89%	\$ 690,123	100%
Residential Construction	107,992	11%	—	—%
Total Revenue	\$ 957,958		\$ 690,123	
Operating Income (Loss)				
Heavy Civil Construction	\$ 10,822	41%	\$(4,729 )	100%
Residential Construction	15,354	59%	—	—%
Total Operating Income (Loss)	\$ 26,176		\$(4,729 )	





## Heavy Civil Construction

### Revenues

Heavy civil construction revenues were \$850.0 million for the year ended December 31, 2017. This represented an increase in our heavy civil construction segment of \$159.8 million, or 23% compared to 2016. The increase was primarily attributable to the increased revenues of approximately \$100 million related to large construction joint venture projects and other projects in the Rocky Mountain region. One of these joint venture contracts was substantially complete at the end of 2017 with the other expected to be complete near the end of 2018. Additionally, included in our December 31, 2017 Unsigned Low-bid awards is a \$136 million project in Utah with construction starting in late spring 2018. The acquired Tealstone Commercial business added approximately \$30 million of revenue in 2017. The balance of the revenue growth was generated across the balance of our geographic operations reflecting the improving heavy civil construction market.

### Operating income

Operating Income was \$10.8 million for the year ended December 31, 2017, an increase of \$15.6 million, in our heavy civil construction segment compared to 2016. The improvement was primarily the result of higher gross margins driven by improved bid discipline, project management and project execution of \$7.2 million, additional gross profit from the increased revenue of approximately \$12.6 million and increased absorption of fixed costs totaling approximately \$2.5 million. These increases were offset by increases in general and administrative expense of \$3.0 million, primarily higher incentive based costs, including stock based compensation and higher personnel recruiting costs in the Rocky Mountain Region. Finally, other operating expenses increased by \$3.6 million primarily as a result of an additional \$2.6 million of member's interest expense driven by the higher 2017 earnings from our Consolidated 50% owned subsidiaries and a loss of \$1.1 million from the sale of an excess facility.

## Residential Construction

### Revenues

Our residential construction segment was a component of the Tealstone acquisition acquired on April 3, 2017. It's principal market is Texas, specifically the Dallas-Fort Worth area and the surrounding communities. The core customer base for residential construction segment is primarily made up of leading national home builders as well as regional and custom home builders. Our residential construction segment contributed \$108.0 million of revenue attributable to the inclusion of nine months of revenue from the acquisition date. On a comparable unaudited pro forma revenue basis, for the nine months ended December 31, 2016, revenue was \$86.9 million providing a pro forma period over period revenue growth of 24%. This pro forma revenue growth rate reflects the strength of the segment's primary market, the Dallas-Fort Worth area, in Texas.

### Operating income

The residential construction segment operating income totaled \$15.4 million in 2017 reflecting the nine months of operating performance since the Tealstone Acquisition on April 3, 2017. On a comparable unaudited pro forma basis, for the nine months ended December 31, 2016, operating income was \$11.8 million providing a pro forma period over period growth of 30%.

## Liquidity and Sources of Capital

The following tables set forth information about our cash flows and liquidity (amounts in thousands):

	Years Ended	
	December 31, 2018	2017
Net cash (used in) provided by:		
Operating activities	\$39,474	\$24,767
Investing activities	(11,382 )	(55,897 )
Financing activities	(17,950 )	72,298
Total increase in cash and cash equivalents	\$10,142	\$41,168

	As of December	
	31,	
	2018	2017
Cash and cash equivalents	\$94,095	\$83,953
Working capital	\$123,442	\$96,234

38

---

## Operating Activities

During 2018, net cash provided by operating activities was \$39.5 million compared to \$24.8 million in 2017, driven by the increase in net income year over year.

## Cash and Working Capital

Cash at December 31, 2018, was \$89.3 million, and includes the following components (amounts in thousands):

	As of December	
	31,	
	2018	2017
Generally Available	\$42,605	\$34,031
Consolidated 50% Owned Subsidiaries	31,026	31,056
Construction Joint Ventures	20,464	18,866
Total Cash	\$94,095	\$83,953

The increase in generally available cash is primarily due to the improvement in cash flow from operations, partially offset by \$10.4 million of repayments on the Oaktree Facility during 2018. The increase in construction joint venture cash levels is driven by the substantial completion of a large Rocky Mountain region construction joint venture project. Sterling's working capital increased \$27.2 million to \$123.4 million at December 31, 2018 from \$96.2 million at December 31, 2017, due to the above cash factors and the Contract Capital discussion below.

The need for working capital for our business varies due to fluctuations in operating activities and investments in our Contract Capital. The changes in components of Contract Capital at December 31, 2018 and 2017 and variances were as follows (amounts in thousands):

	Changes in Components of		
	Contract Capital		
	2018	2017	Variance
Costs and estimated earnings in excess of billings on uncompleted contracts	\$(4,430 )	\$(1,463 )	\$(2,967 )
Billings in excess of costs and estimated earnings on uncompleted contracts	33	(2,029 )	2,062
Contracts in progress, net	(4,397 )	(3,492 )	(905 )
Contracts receivable, including retainage	(11,094 )	(29,923 )	18,829
Receivables from and equity in construction joint ventures	659	(4,250 )	4,909
Accounts payable	1,969	13,579	(11,610 )
Contract Capital, net	\$(12,863)	\$(24,086)	\$11,223

The 2018 change in Contract Capital reduced liquidity by \$12.9 million. Fluctuations in our Contract Capital balance, and its components, are not unusual in our business and are impacted by the size of our projects and changing type and mix of projects in our Backlog. Our Contract Capital is particularly impacted by the timing of new awards and related payments of performing work and the contract billings to the customer as we complete our projects, like we are experiencing on our large construction joint venture projects. Contract Capital is also impacted at period-end by the timing of accounts receivable collections and accounts payable payments for our projects. The significant change in 2017 for contract receivables and accounts payable is attributable to activity on our large construction joint venture projects and other projects in the Rocky Mountain region.

## Investing Activities

During 2018, net cash used in investing activities was \$11.4 million, compared to net cash used of \$55.9 million in 2017. In 2018, the cash used in investing activities was driven by purchases of capital equipment less cash proceeds from the sale of property and equipment. In 2017 the \$55 million paid on April 3, 2017, as part of the Tealstone acquisition was the primary driver of investing activities cash flows.



Capital equipment is acquired as needed to support changing levels of production activities and to replace retiring equipment. Expenditures for the replacement of certain equipment and to expand our construction fleet totaled \$13.2 million in 2018, which included a minimal amount of financed capital expenditures. Proceeds from the sale of property and equipment totaled \$1.8 million for 2018 with an associated net gain of \$0.6 million, reflecting our continuing initiative to optimize utilization of our existing fleet of equipment based on current and projected workloads while supplementing our fleet with leased and financed equipment as needed.

For the year ended December 31, 2017, capital expenditures totaled \$9.4 million, while proceeds from the sale of property and equipment totaled \$8.4 million with an associated net loss of \$0.2 million. The proceeds from the sale of property and equipment increased in 2017 reflecting our continuing initiative to optimize utilization of our existing fleet of equipment based on current and projected workloads while supplementing our fleet with leased and financed equipment as needed. In addition, in 2017 we sold our Dallas Texas facility for approximately \$3.0 million reflecting our ongoing efforts to improve our operating effectiveness in Texas.

#### Financing Activities

During 2018, net cash used by financing activities was \$18.0 million compared to net cash provided of \$72.3 million for 2017. The use of cash was primarily attributable to the repayments of the Oaktree Facility of \$10.4 million and the purchase of treasury stock of \$4.7 million. The increase in cash provided by financing activities in 2017 was primarily a result of net proceeds of \$85 million received from the Oaktree Facility, which was utilized to fund the Tealstone acquisition and the repayment of our remaining balance on our equipment-based facility term loan.

#### Other Sources of Capital

In addition to our available cash, cash equivalents and cash provided by operations, from time to time we use borrowings to finance acquisitions, our capital expenditures and working capital needs.

#### Borrowing Arrangements

On April 3, 2017, the Company, as borrower, and certain of its subsidiaries, as guarantors, entered into a Loan and Security Agreement with Wilmington Trust, National Association, as agent, and the lenders party thereto (the "Oaktree Facility"), providing for a term loan of \$85,000,000 (the "Loan") with a maturity date of April 4, 2022, which replaced the then existing debt facility. The Loan is secured by substantially all of the assets of the Company and its subsidiaries.

Interest on the Loan is equal to the one-, two-, three- or six-month London Interbank Offered Rate, or LIBOR, plus 8.75% per annum on the unpaid principal amount of the Loan, subject to adjustment under certain circumstances. Interest on the Loan is generally payable monthly. There are no amortized principal payments; however, the Company is required to prepay the Loan, and in certain cases pay a prepayment premium thereon, with proceeds received from the issuances of debt or equity, transfers, events of loss and extraordinary receipts. The Company is required to make an offer quarterly to the lenders to prepay the Loan in an amount equal to 75% of its excess cash flow, plus accrued and unpaid interest thereon and a prepayment premium. In 2018, prepayments of \$10.4 million were made.

The Oaktree Facility contains various covenants that limit, among other things, the Company's ability and certain of its subsidiaries' ability to incur certain indebtedness, grant certain liens, merge or consolidate, sell assets, make certain loans, enter into acquisitions, incur capital expenditures, make investments, and pay dividends. In addition, the Company is required to maintain the following principal financial covenants:

-

a ratio of secured indebtedness to EBITDA of not more than 2.00 to 1.00 for the trailing four consecutive fiscal quarters ending December 31, 2018, reducing to 1.8 to 1.00 for the four consecutive quarters ending September 30, 2019 through maturity in 2022;

daily cash collateral of not less \$15,000,000;

gross margin in contract backlog of not less than \$65,000,000 for the average of the trailing four consecutive fiscal quarters ending December 31, 2018, increasing to \$70,000,000 on March 31, 2019;

net capital expenditures during the trailing four consecutive fiscal quarters shall not exceed \$15,000,000;

bonding capacity shall be maintained at all times in an amount not less than \$1,000,000,000; and

the EBITDA of Tealstone Residential Concrete, Inc. shall not be less than \$12,000,000 for each of the trailing four consecutive fiscal quarters.

The Company was in compliance with these covenants at December 31, 2018 and 2017.

The Oaktree Facility also includes customary events of default, including events of default relating to non-payment of principal or interest, inaccuracy of representations and warranties, breaches of covenants, cross-defaults, bankruptcy and insolvency events, certain unsatisfied judgments, loan documents not being valid, calls under the Company's bonds, failure of specified individuals to remain employed by the Company, and a change of control. If an event of default occurs, the lenders will be able to accelerate the maturity of the Oaktree Facility and exercise other rights and remedies.

Deferred loan costs and warrants totaled \$10.4 million, which included attorney fees, investment bank fees as well as amounts paid to the lenders and which were discounted from the loan amount. Warrants valued at \$3.5 million were included as well. Refer to Note 9 - Secured Credit Facility and Other Debt for additional information on the warrants. Deferred loan costs are amortized on a straight-line basis, which approximates the effective interest method, over the five-year life of the Loan. Amortization expense of \$2.1 million and \$1.6 million have been included in interest expense for the years ended December 31, 2018 and 2017.

During 2018 we repaid \$10.4 million on the Oaktree Facility. As part of the retirement of our Equipment-based Facility, \$0.8 million in debt extinguishment costs was expensed and included as a "loss on extinguishment of debt" on our statement of operations for the year ended December 31, 2017.

#### Notes and Deferred Payments to Sellers

As part of the Tealstone Acquisition, the Company issued \$5.0 million of promissory notes bearing interest at 8% to the sellers and agreed to make \$2.4 million and \$7.5 million of non-interest bearing deferred cash payments on the second and third anniversaries of the closing date, respectively. Based on a 12% discount rate, the Company recorded \$11.6 million as notes and deferred payments to sellers in long-term debt on our consolidated balance sheet at the acquisition closing date. Accreted interest expense was \$1.2 million and \$0.8 million for the years ended December 31, 2018 and 2017, respectively. The promissory notes are due on April 3, 2020.

#### Notes Payable for Transportation and Construction Equipment

The Company has purchased and financed various transportation and construction equipment to enhance the Company's fleet of equipment. The notes payable related to the purchase of financed equipment was \$0.6 million and \$1.6 million at December 31, 2018 and 2017, respectively. The purchases have payment terms ranging from 3 to 5 years and the associated interest rates range from 3.15% to 6.92%.

#### Fair Value

The Company's debt is recorded at its carrying amount in the consolidated balance sheets. As of December 31, 2018 and 2017, the carrying values of our debt outstanding approximated the fair values and were \$88.8 million and \$99.0 million, respectively.

#### Borrowings

Based on our average borrowings for 2018 and our 2019 forecasted cash needs, we continue to believe that the Company has sufficient liquid financial resources to fund our requirements for the next year of operations, including our bonding requirements. Furthermore, the Company is continually assessing ways to increase revenues and reduce costs to improve liquidity. However, in the event of a substantial cash constraint and if we were unable to secure adequate debt financing, our working capital could be materially and adversely affected. Refer to "Item 1A. Risk Factors" for further discussion of liquidity related risks.



#### Issuance of Warrants and Common Stock

On April 3, 2017, the Company issued warrants (the “Warrants”) to the lenders under the Oaktree Facility (including any permitted trustees, the “Holders”) pursuant to which the Holders have the right to purchase, for a period of five years from the date of issuance, up to an aggregate of 1,000,000 shares of the Company’s common stock (the “Warrant Shares”) at an initial exercise price of \$10.25 per share, subject to adjustment for stock splits, combinations and similar recapitalization events and weighted-average anti-dilution upon the issuance by the Company of shares of common stock or rights, options or convertible securities exercisable for common stock in the future at a price below the exercise price of the Warrants. The total fair value of the Warrants was \$3,500,000, which was recorded as a loan discount and netted against our new Loan and included in “additional paid in capital” on our balance sheet.

On April 3, 2017, in connection with the Tealstone Acquisition, the Company issued 1,882,058 shares of the Company's common stock to the Tealstone sellers. The total fair value of which was \$17.1 million. See Note 2 - Tealstone Acquisition for additional details.

### Capital Strategy

We will continue to explore additional revenue growth and capital alternatives to further strengthen our financial position in order to take advantage of the improving heavy civil infrastructure market. We expect to pursue strategic uses of our cash to invest in projects or businesses that meet our gross margin targets, overall profitability and other requirements, as well as managing our debt balances, pursuing investments in adjacent markets or other opportunities.

### Contractual Obligations

The following table sets forth our fixed, non-cancelable obligations at December 31, 2018:

	Payments due by period				
	Total	<1 Year	1 - 3 Years	4 - 5 Years	>5 Years
	(Amounts in thousands)				
Operating leases*	\$ 11,460	\$ 4,553	\$ 5,862	\$ 1,029	\$ 16
Oaktree Facility	74,571	—	—	74,571	—
Debt Facility interest	27,732	8,506	17,035	2,191	—
Notes and deferred payments to Sellers, Tealstone Acquisition (inclusive of outstanding interest)	14,926	2,426	12,500	—	—
Notes payable for equipment	612	544	68	—	—
Earn-out Liability**	1,546	1,546	—	—	—
Members' interest subject to mandatory redemption and undistributed earnings***	49,343	—	—	—	49,343
	\$ 180,190	\$ 17,575	\$ 35,465	\$ 77,791	\$ 49,359

\* Operating leases are stated at minimum annual rentals for all operating leases having initial non-cancelable lease terms in excess of one year.

\*\* The Tealstone earn-out arrangement requires the Company to pay up to an aggregate of \$15 million in earn-out payments on the first, second, third and fourth anniversaries of the closing date to continuing Tealstone management or their affiliates if specified financial performance levels are achieved.

\*\*\* Mandatory redemption is based on the death or disability of the interest holders. Undistributed earnings can be distributed upon unanimous consent from the members and for tax distributions. At this time we cannot predict when such distributions will be made. The Company has purchased two separate \$20 million death and permanent total disability insurance policies to mitigate the Company's cash draw if such events were to occur.

### Bonding

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. We have pledged all proceeds and other rights under our construction contracts to our bond surety company. Events that affect the insurance and bonding markets may result in bonding becoming more difficult to obtain in the future, or being available only at a significantly greater cost. To date, we have not encountered difficulties or material cost increases in obtaining new surety bonds.

### Capital Expenditures

Capital equipment is acquired as needed by increased levels of production and to replace retiring equipment. Management expects capital expenditures in 2019 to be similar to the \$13.2 million incurred in 2018; however, the award of a project requiring significant purchases of equipment or other factors could result in increased expenditures.

42

---

## Inflation

Inflation generally has not had a material impact on our financial results; however, from time to time increases in oil, fuel, and steel prices have affected our cost of operations. Anticipated cost increases and reductions are considered in our bids to customers on proposed new construction projects.

Where we are the successful bidder on a heavy civil construction project, we execute purchase orders with material suppliers and contracts with subcontractors covering the prices of most materials and services, other than oil and fuel products, thereby mitigating future price increases and supply disruptions. These purchase orders and contracts do not contain quantity guarantees and we have no obligation for materials and services beyond those required to complete the contracts with our customers. There can be no assurance that increases in prices of oil and fuel used in our business will be adequately covered by the estimated escalation we have included in our bids and there can be no assurance that all of our vendors will fulfill their pricing and supply commitments under their purchase orders and contracts with the Company. We adjust our total estimated costs on our projects when we believe it is probable that we will have cost increases which will not be recovered from customers, vendors or re-engineering.

Inflation affects our residential construction projects minimally, as the time from starting construction to finishing is typically less than one month.

## Off-Balance Sheet Arrangements and Joint Ventures

We participate in various construction joint venture partnerships in order to share expertise, risk and resources for certain highly complex projects. The joint venture's contract with the project owner typically requires joint and several liability among the joint venture partners. Although our agreements with our joint venture partners provide that each party will assume and fund its share of any losses resulting from a project, if one of our partners was unable to pay its share, we would be fully liable for such share under our contract with the project owner. Circumstances that could lead to a loss under these guarantee arrangements include a partner's inability to contribute additional funds to the venture in the event that the project incurred a loss or additional costs that we could incur should the partner fail to provide the services and resources toward project completion that had been committed to in the joint venture agreement. See Item 1A "Risk Factors."

At December 31, 2018, there was approximately \$67.4 million of construction work to be completed on unconsolidated construction joint venture contracts, of which \$33.6 million represented our proportionate share. Due to the joint and several liability under our joint venture arrangements, if one of our joint venture partners fails to perform, we and the remaining joint venture partners would be responsible for completion of the outstanding work. As of December 31, 2018, we are not aware of any situation that would require us to fulfill responsibilities of our joint venture partners pursuant to the joint and several liability under our contracts.

Off-balance sheet arrangements related to the operating leases are included in the table in "Contractual Obligations" above.

## New Accounting Pronouncements

Refer to "Recent Accounting Pronouncements" in Note 1 - Summary of Business and Significant Accounting Policies for a discussion of new accounting pronouncements. To the extent known, we expect the effect of these recent accounting pronouncements on future periods to be in line with what is stated in Note 1.



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

Changes in interest rates are one of Sterling's sources of market risk. Interest on outstanding indebtedness under the Oaktree Facility is equal to the one-, two-, three- or six-month London Interbank Offered Rate, or LIBOR, plus 8.75% per annum on the unpaid principal amount of the Loan, subject to adjustment under certain circumstances. Sterling's interest rates for the periods ended December 31, 2018 and 2017 were 11.18% and 10.12%, respectively. This represents an increase of approximately 100 basis points year over year. There are no amortized principal payments; however, the Company is required to prepay the Loan, and in certain cases pay a prepayment premium thereon, with proceeds received from the issuances of debt or equity, transfers, events of loss and extraordinary receipts. The Company is required to make an offer quarterly to the lenders to prepay the Loan in an amount equal to 75% of its excess cash flow, plus accrued and unpaid interest thereon and a prepayment premium. At December 31, 2018, we had a term loan of \$74.6 million outstanding under this facility. A 1% increase in the interest rate would increase interest expense by \$0.7 million per year.

See "Inflation" above regarding risks associated with materials and fuel purchases required to complete our construction contracts.

#### Item 8. Financial Statements and Supplementary Data

Financial statements start on page F1.

#### Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None

#### Item 9A. Controls and Procedures

##### Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures include, but are not limited to, 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) as of December 31, 2018. 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, 2018 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. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect our transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. Also, projections of any evaluation of effectiveness 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. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

Management conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2018. In making this assessment, management used the criteria described in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that our internal control over financial reporting was effective as of December 31, 2018.

#### Attestation Report of the Registered Public Accounting Firm

Grant Thornton LLP, the independent registered public accounting firm that audited our consolidated financial statements included in this annual report on Form 10-K, has issued an attestation report on the effectiveness of the Company's internal control over financial reporting as of December 31, 2018, included in "Item 15. Exhibits and Financial Statement Schedules" under the heading "Reports of the Company's Independent Registered Public Accounting Firm".

#### 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 changes in our internal control over financial reporting occurred during the three months ended December 31, 2018, 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.

#### Item 9B. Other Information

None



### PART III

#### Item 10. Directors, Executive Officers and Corporate Governance

Information required by this item will be contained in our definitive proxy statement to be filed with the SEC pursuant to Regulation 14A relating to our 2019 annual meeting of stockholders and is incorporated herein by reference. The information required by Item 10 regarding our executive officers appears in a separately captioned heading "Executive Officers of the Registrant" after Item 4 in Part I of this report. Our code of business conduct is available at [www.strlco.com](http://www.strlco.com) under Investor Relations-Corporate Governance and is available in print to any stockholder who requests a copy. Amendments to or waivers of our code of business conduct granted to any of our directors or executive officers will be published promptly on our website. Such information will remain on our website for at least 12 months.

#### Item 11. Executive Compensation

Information required by this item will be contained in our definitive proxy statement to be filed with the SEC pursuant to Regulation 14A relating to our 2019 annual meeting of stockholders and is incorporated herein by reference.

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

Information required by this item will be contained in our definitive proxy statement to be filed with the SEC pursuant to Regulation 14A relating to our 2019 annual meeting of stockholders and is incorporated herein by reference.

#### Item 13. Certain Relationships and Related Transactions, and Director Independence

Information required by this item will be contained in our definitive proxy statement to be filed with the SEC pursuant to Regulation 14A relating to our 2019 annual meeting of stockholders and is incorporated herein by reference.

#### Item 14. Principal Accounting Fees and Services

Information required by this item will be contained in our definitive proxy statement to be filed with the SEC pursuant to Regulation 14A relating to our 2019 annual meeting of stockholders and is incorporated herein by reference.

PART IV

Item 15. Exhibits, and Financial Statement Schedules

The following Financial Statements and Financial Statement Schedules are filed with this Report:

Financial Statements:

Reports of the Company's Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2018 and 2017

Consolidated Statements of Operations for the years ended December 31, 2018, 2017 and 2016

Consolidated Statements of Comprehensive Income (Loss) for the years ended December 31, 2018, 2017 and 2016

Consolidated Statements of Cash Flows for the years ended December 31, 2018, 2017 and 2016

Consolidated Statements of Stockholders' Equity for the years ended December 31, 2018, 2017 and 2016

Financial Statement Schedules

None.

Exhibits

The following exhibits are filed with this Report.

Explanatory Note

Prior to changing its name to Sterling Construction Company, Inc. in November 2001, the Company's name was Oakhurst Company, Inc. References in the following exhibit list use the name of the Company in effect at the date of the exhibit.

Number	Exhibit Title
2.1	<u>Stock Purchase Agreement, dated March 8, 2017, by and among Sterling Construction Company, Inc. the sellers identified therein, Gary Roger Engasser II, as</u>

sellers'  
representative  
and the  
principals  
identified  
therein  
(incorporated  
by reference  
to Exhibit 2.1  
to Sterling  
Construction  
Company,  
Inc.'s Current  
Report on  
Form 8-K,  
filed on March  
9, 2017 (SEC  
File No.  
1-31993)).  
Certificate of  
Incorporation  
of Sterling  
Construction  
Company, Inc.  
as amended  
through April  
28, 2017  
(incorporated  
by reference  
to Exhibit 3 to  
Sterling  
Construction  
Company,  
Inc.'s Current  
Report on  
Form 8-K,  
filed on May  
3, 2017 (SEC  
File No.  
1-31993)).

3.1

3.2