STERLING CONSTRUCTION CO INC
Form ARS
March 17, 2017

Annual Report for the Year Ended December 31, 2016

Dear Fellow Shareholders,

2016 was a pivotal year for Sterling. We closed out the last of our troublesome legacy projects, improved our bidding and execution procedures, and developed a comprehensive, long-term strategy to increase profitability and growth. We also strengthened our leadership team and markedly improved our balance sheet. In addition, we began to experience the positive effects of the federal highway bill and state infrastructure funding initiatives.

During the year, our backlog grew to over a billion dollars, including unsigned awards, which was a record high for our Company. More importantly, the margin in that combined backlog grew to 8.5%, which was an increase of 120 basis points over the comparable year-end backlog margin at December 31, 2015 of 7.4%. We also made excellent progress in improving the percentage of non-heavy highway work in backlog from 10% at the end of 2015 to more than 25% by the end of 2016. By the fourth quarter of 2018, our goal is to have 50% of our backlog in non-heavy highway work, which includes airports, railroads, ports, and commercial projects. Our recently-announced agreement to acquire Tealstone Construction is an excellent example of our strategy to improve margins and diversify our industry and customer base.

We have also made significant progress in solidifying our financial position and liquidity. Our cash balance, net of our debt at the end of 2016, was $37 million, an improvement of $53 million over our cash balance at the end of 2015. Additionally, we completed a common stock offering of $19 million in May 2016 thereby improving our financial strength and positioning Sterling to take full advantage of the robust transportation infrastructure market.

We believe that 2017 will be a transformational year for Sterling. Our turnaround will be substantially behind us, and the higher-margin work in backlog will start to convert into revenue and earnings.

We want to take this opportunity to thank our shareholders, our dedicated employees, and our customers, vendors, lenders and other stakeholders for their continued support.

Sincerely,

Paul J. Varello	Milton L. Scott
Chief Executive Officer	Chairman of the Board

The Woodlands, Texas

March 17, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

[X] annual report pursuant to section 13 or 15(d) of the securities exchange act of 1934

For the fiscal year ended: December 31, 2016
[ ] 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	(I.R.S. Employer
incorporation or organization	Identification No.)
1800 Hughes Landing Blvd.	
The Woodlands, Texas	**77380**
(Address of principal executive offices)	(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 and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter prior that the registrant was required to submit and post 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 [ ]

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

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

Indicate by check mark if the registrant is a shell company (as defined in Rule 12b-2 of the Act). [ ] Yes [√] No

Aggregate market value of the voting and non-voting common equity held by non-affiliates at June 30, 2016: $116,433,206.

At March 1, 2017, the registrant had 25,051,045 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 April 28, 2017 are incorporated by reference into Part III of this Form 10-K.

Sterling Construction Company, Inc.

Annual Report on Form 10-K

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PART I

Cautionary Comment Regarding Forward-Looking Statements

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

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

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

- changes in general economic conditions, including recessions, reductions in federal, state and local government funding for infrastructure services and changes in those governments’ budgets, practices, laws and regulations;
- 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;
- 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;
- factors that affect the accuracy of estimates inherent in our bidding for contracts, estimates of backlog, percentage-of-completion accounting policies, including onsite conditions that differ materially from those assumed in our original bid, contract modifications, mechanical problems with our machinery or equipment and effects of other risks discussed in this document;
- design/build contracts which subject us to the risk of design errors and omissions;
- 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, and cost escalations associated with subcontractors and labor;

- our dependence on a limited number of significant customers;
- adverse weather conditions; although we prepare our budgets and bid contracts based on historical rain and snowfall patterns, the incidence of rain, snow, hurricanes, etc., may differ materially from these expectations;
- 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;
- 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;
- adverse economic conditions in our markets; and
- the other factors discussed in more detail in “Item 1A. Risk Factors”.

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

The forward-looking statements included in this Report are made only as of the date of this Report, and we undertake no obligation to update any information contained in this Report or to publicly release the results of any revisions to any forward-looking statements to reflect events or circumstances that occur, or that we become aware of after the date of this Report, except as may be required by applicable securities laws.

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Item 1. Business.

Overview of the Company's Business.

Sterling Construction Company, Inc. was founded in 1991 as a Delaware corporation. Our principal executive offices are located at 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: Texas Sterling Construction Co., a Delaware corporation, or "TSC"; Road and Highway Builders, LLC, a Nevada limited liability company, or "RHB"; Road and Highway Builders of California, Inc., a California corporation, or "RHBCa"; Ralph L. Wadsworth Construction Company, LLC, a Utah limited liability company, or "RLW"; J. Banicki Construction, Inc., an Arizona corporation, or "JBC"; and Myers & Sons Construction, L.P., a California limited partnership, or "Myers". 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.

Sterling is a leading heavy civil construction company that specializes in the building and reconstruction of transportation and water infrastructure projects in Texas, Utah, Nevada, Colorado, Arizona, California, Hawaii and other states in which there are construction opportunities. Its transportation infrastructure projects include highways, roads, bridges, airfields, ports and light rail. Its water infrastructure projects include water, wastewater and storm drainage systems.

Although we describe our business in this Report in terms of the services we provide, our base of customers and the geographic areas in which we operate, we have concluded that our operations consist of one reportable segment, one operating segment and one reporting unit component, which is heavy civil construction. In making this determination, the Company considered the discrete financial information used by our Chief Operating Decision Maker ("CODM"). Based on this approach, the Company noted that the CODM organizes, evaluates and manages the financial information around each heavy civil construction project when making operating decisions and assessing the Company's overall performance. Furthermore, we considered that each heavy civil construction project has similar characteristics, includes similar services, has similar types of customers and is subject to similar economic and regulatory environments.

Sterling has grown its service profile and geographic reach both organically and through acquisitions. Expansions into Utah, Arizona and California were achieved with the 2009 acquisition of RLW and the 2011 acquisitions of JBC and Myers, respectively. These acquisitions also extended Sterling's service profiles.

Recent Developments.

Financial Results for 2016, Operational Issues and Outlook for 2017 Financial Results.

In 2016, the Company had an operating loss of $4.7 million and net loss attributable to Sterling common stockholders of $9.2 million. Our gross margins have increased to 6.4% in 2016 from 4.6% in 2015 and 4.8% in 2014. Although our gross margins have recovered from 2015 and 2014 levels, the Company was challenged in 2016 with unusually poor weather conditions, including rain in Texas and snow at our Nevada jobs during the first quarter. In addition, in the fourth quarter, there was a $2.5 million charge on a negotiated global settlement with several entities which allowed the close-out of a Texas project, thus avoiding further negotiation and litigation expense along with charges on Texas projects and to under-recovered equipment costs. However, our other four operating subsidiaries collectively have exceeded gross margin expectations for the year.

The majority of our revenues and backlog is derived from fixed unit price contracts or from lump sum contracts. Fixed unit price contracts require us to provide materials and services at a fixed unit price based on approved quantities irrespective of our actual per unit costs. Lump sum contracts require that the total amount of work be performed for a single price irrespective of our actual costs. As discussed in “Item 1A. Risk Factors,” we realize a profit on our contracts only if we accurately estimate our costs and then successfully control actual costs and avoid cost overruns and our revenues exceed actual costs. If our cost estimates for a contract are inaccurate, or if we do not execute the contract within our cost estimates, then cost overruns may cause the contract not to be as profitable as we expected or result in a loss, negatively affecting our cash flow, earnings and financial position.

While the risks of cost overruns and changes in estimated contract revenues are an inherent part of the construction business, we continue to implement the following to improve the profitability of our projects, reduce the variability in profitability of our projects in the future and strengthen our internal control environment:

- We continue to change roles and responsibilities to improve functional support and controls when needed.
- We continue to hire senior management with expertise and experience in the construction industry.
- We continue to develop management tools designed to improve the estimating process and increase the oversight of that process where needed and continue to refine existing tools.

- We continue to implement processes designed to better identify, evaluate and quantify risks for individual projects where needed and continue to refine existing processes.

- We continue to improve the methodologies for allocating overhead, indirect costs and equipment costs to individual projects in order to provide more accurate job costs and future bidding estimates.

- We continue to improve the timeliness and content of reporting available to operations management.

In 2015 and 2014, our gross margins were adversely affected by downward percent-complete revisions on several projects which began in 2014 and prior which affected revenues and profitability. However, as we continue to improve our project execution and strengthen our internal control environment, these downward percent-complete revisions have been less significant which helped increase our gross margin in our operating results for 2016.

In addition to the factors discussed above which impact the profitability on individual projects, there are other factors related to federal and state spending which have also affected our business. Our highway and related bridge work is generally funded through federal and state authorizations. Funding for federal highway projects primarily originates from the Highway Trust Fund where federal motor fuel taxes are the major source of income into the fund. Additional income is provided from the General Fund and certain other funds to maintain the solvency of the fund. In the later part of 2015, we saw the passage of federal and several state, infrastructure funding plans. Refer to the section below entitled, "Our Markets and Customers," for additional information on the federal and state funding initiatives in our markets. This trend of increased federal and state spending has helped our backlog grow from $761 million at December 31, 2015 to $823 million at December 31, 2016, representing a favorable industry trend with sufficient work to be bid on within our markets with acceptable and improving gross margins. In addition to our backlog, we are the apparent low bidder for contracts that have not been officially awarded as contracts ("Unsigned Low-bid Awards"), which were $226 million at December 31, 2016 and $197 million at the end of 2015. We expect substantially all of the Unsigned Low-bid Awards at December 31, 2016, to be signed and included in backlog in the first quarter of 2017. In addition to highway and related bridge work, we continually look for projects that diversify our backlog and increase our gross margins.

Our Markets and Customers.

Currently, all of our operations, which resulted in $690 million of revenues in 2016, are performed under our heavy civil construction segment and within the United States ("U.S."). As such, we rely heavily on federal and state infrastructure spending. Within the U.S., our principal markets are Texas, California, Utah, Nevada, Colorado, Arizona and Hawaii. 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 and railroads.

The U.S. transportation construction market is forecasted to grow from $244.5 billion in 2016 to $273.4 billion in 2021. This increase is largely driven by the federal "Fixing Americas Surface Transportation Act" ("Fast Act"). The Fast

Act is the first law enacted in over ten years that provides long-term funding for transportation, meaning states can move forward with critical projects with confidence as they will now have a Federal partner over the long term. Over the next five years, spending for both public and private bridge and highway work is forecasted to grow from $148.8 billion to $165.9 billion; airports and runways are forecasted to grow from $13.1 billion to $14.8 billion; ports and waterways will increase slightly from $2.1 billion to $2.4 billion; and rail/light rail will grow from $19.3 billion to $22.6 billion. In addition to the Fast Act, certain States within our markets have passed legislation that will help funding of transportation construction. Texas has passed two constitutional amendments (Proposition 1 and Proposition 7) that will increase its transportation spend by $4.0 to $4.5 billion annually. Utah passed a gas tax increase of five cents/gallon in 2016 with an additional one cent per gallon increase over the next four years. This represents a 20% increase and is expected to generate $75 to $85 million in additional spending per year. In addition, a 1-cent sales tax increase was approved in Los Angeles, California in 2016 which will provide $3 billion a year for local road, bridge and transit projects.

Currently, our largest customers are the California DOT, the Texas DOT and the Utah DOT. These customers have each contributed more than 10% of our revenues in 2016. We routinely construct projects for these customers; however, if one or more of these customers were lost, it could have a material adverse effect on our financial results. Refer to Note 16 to the consolidated financial statements (references to “Note” or “Notes” refer to the Notes to the consolidated financial statements for the year ended December 31, 2016, included in this document), for the Company’s major customers that represent a concentration of risk due to their significant revenue contributions.

Competition.

Our competition 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 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 our bids. This in return reduces both revenue growth and margins.

Seasonality.

Our operations are typically affected by weather conditions 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.

Backlog.

Backlog is the revenue we expect to earn in future periods on our construction projects. However, Unsigned Low-bid Awards are excluded from backlog until the contract is executed by our customer. As the construction on our projects progresses, we increase or decrease backlog to take into account our estimates of the effects of changes in estimated quantities, changed conditions, change orders and other variations from initially anticipated contract revenues, including completion penalties and incentives. At December 31, 2016, our backlog was $823 million and our Unsigned Low-bid Awards were $226 million.

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

Construction Delivery Methods.

Alternative construction delivery methods describe different contractual and responsibility relationships among the owner, the builder and the designer of a project. There are three primary construction delivery methods: design-bid-build, design-build and construction management.

The traditional method by which the majority of our projects have historically been completed is design-bid-build. Under this type of construction delivery, the owner hires a design engineer to design the project and then solicits bids from construction firms and typically awards the contract to build the pre-designed project to the lowest qualifying bidder. The contractor to whom the project is awarded becomes the general contractor and is responsible for completing the project in accordance with the owner's designs using the contractor's own employees or resources, or subcontractors. Projects under this method are typically fixed unit price contracts.

Design-build is sometimes used by public entities as a method of project delivery. Unlike traditional projects where the owner first hires a design firm or designs a project itself and then puts the project out to bid for construction, design-build projects provide the owner with a single point of responsibility and a single contact for both final design and construction. The owner selects a builder who hires the design team as required and construction typically starts before the design is complete. This project delivery method is typically undertaken through either fixed unit price contracts or lump sum contracts, and price is not the only determining factor used by the owner when selecting a particular contractor.

Construction management is a method of delivering a project whereby a contractor agrees to manage a project for the owner for an agreed-upon fee, which may be fixed or may vary based upon negotiated factors. The owner of the project typically hires the contractor as a construction manager early in the design phase of the project. The construction manager works with the design team to help ensure that the design is something that can in fact be built within the owner's desired cost and other parameters and that the ultimate construction contractor will be able to understand the design drawings and specifications. There are two basic types of construction management: construction manager as advisor and construction manager at risk. In the construction manager as advisor type of arrangement, the construction manager acts as a technical consultant to the owner of the project and has no legal responsibility for the performance of the actual construction work. In the construction manager at risk type of arrangement, the construction manager becomes the prime contractor during the construction phase and makes a determination as to which portions of the work will be self-performed and which will be performed through subcontracts. In either type of construction management process, portions of a project are often submitted for bid during the course of the construction manager relationship, with the construction manager bidding, and oftentimes having the first right to bid, on portions of the project.

Contracts.

Types of Contracts.

We provide our services primarily by using traditional general contracting arrangements, including fixed unit price contracts, lump sum contracts and cost-plus contracts.

Fixed unit price contracts are generally used in competitively-bid public civil construction contracts. Contractors under fixed unit price contracts are generally committed to provide all of the resources required to complete the contract for a fixed price per unit. These contracts are generally subject to negotiated change orders, frequently due to differences in site conditions from those initially anticipated or asserted by the customer. Some fixed unit price contracts provide for penalties, if the contract is not completed on time, or incentives, if it is completed ahead of schedule.

Under a lump sum contract, the contractor typically agrees to deliver a completed project in accordance with the contract's requirements for a specific price, and the customer agrees to pay the price according to a negotiated payment schedule. In developing a lump sum bid, the contractor estimates the costs of labor, subcontracts and materials and adds an amount for overhead and profit. The amount of the profit included in the bid is based on the contractor's assessment of risk and other factors such as availability of resources. If the actual costs of labor, subcontracts, materials and overhead are higher than the contractor's estimate, the profit will be reduced or become a loss; if the actual costs are lower, the contractor may earn more profit.

In a cost plus contract, the owner of a project generally agrees to pay the cost of all of the contractor's labor, subcontracts and materials plus an amount for contractor overhead and profit (usually as a percentage of the labor, subcontracts and material cost). If actual costs are lower than the estimate, the owner benefits from the cost savings. If actual costs are higher than the estimate, the owner bears the economic burden of the additional costs.

Contract Management Process.

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

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

There are several factors that can create variability in contract performance and financial results compared to our bid assumptions on a contract. The most significant of these include the completeness and accuracy of our original bid analysis, recognition of costs associated with added scope changes, extended overhead due to customer and weather delays, subcontractor availability and performance issues, changes in productivity expectations, site conditions that differ from those assumed in the original bid, and changes in the availability and proximity of materials. In addition, our original bids for some contracts are based on the contract customer's estimates of the quantities needed to complete a contract. If the quantities ultimately needed are different, our backlog and financial performance on the contract will change. All of these factors can lead to inefficiencies in contract performance, which can increase costs and lower profits. Conversely, if any of these or other factors is more favorable than the assumptions in our bid, contract profitability can improve. Design-build projects carry additional risks such as design error risk and the risk associated with estimating quantities and prices before the project design is completed. Design errors may result in higher than anticipated construction costs and additional liability to the contract owner. Although we manage this additional risk by adding contingencies to our bid amounts, obtaining errors and omissions insurance and obtaining indemnifications from our design consultants where possible, there is no guarantee that these risk management strategies will always be successful. Generally, gross margins included in bids on design-build contracts are higher than for other types of contracts due to the higher risks involved.

The estimating process for our traditional fixed unit price competitive bid contracts typically involves three phases. Initially, we consider the level of anticipated competition and our available resources for the prospective project. If we then decide to continue considering a project, we undertake the second phase of the contract process and spend several weeks performing a detailed review of the plans and specifications, summarizing the various types of work involved and related estimated quantities, determining the contract duration and schedule and highlighting the unique and riskier aspects of the contract. Concurrent with this process, we estimate the cost and availability of labor, material, equipment, subcontractors and the project team required to complete the contract on time and in accordance with the plans and specifications. Substantially all of our estimates are made on a per-unit basis for each line item, and it is not unusual for an estimate to contain over 300 line items. The final phase consists of a detailed review of the estimate by management, including, among other things, assumptions regarding cost, approach, means and methods, productivity, risk and the estimated profit margin. This profit amount will vary according to management’s perception of the degree of difficulty of the contract, the current competitive climate and the size, availability of resources and makeup of our backlog. Our project managers are intimately involved throughout the estimating and construction process so that contract issues, and risks, can be understood and addressed generally on a timely basis.

Although the factors described above are relevant in determining the appropriate amount to bid, the contracting process is managed differently if the project is to be performed on a design-build basis or a construction manager/general contractor ("CM/GC") basis. For design-build projects, we assemble a team that may include project managers, engineers, quality managers and surveyors, to learn about a project that we have identified as one on which we may desire to bid. For some projects, pre-qualification for the project is required where each contractor and/or contracting team prepares a description of financial strengths, past experience on similar types of projects, safety record and the persons who will be on the project management and design team, after which, the customer will usually announce a short list of three to five contractors to respond to a request for proposal, generally within three months. Utilizing the limited design specifications provided by the customer, we generally meet weekly over a two to three month period with design engineers to generate a bid containing quantities, prices, timing and a description of our approach for completing the project. The customer then reviews the bids and selects the one that has the best value, and considers factors such as contractor qualifications, the time estimated to complete the project and the price bid.

For our CM/GC projects, the customer typically sends out a request for proposal to general contractors for a project. The customer scores each contractor that submits a bid based on the unit prices submitted for five to twenty items that comprise approximately 10% to 20% of the project design, the profit margin proposed, the experience of the contractor for similar types of projects, the contractor's approach to completing the specific project and whether the contractor understands the CM/GC process. A committee reviews each bid and determines the best value winner to be the general contractor. If we are the winning general contractor, we work with the customer and the engineer to design the project. As various phases of the project are designed, we usually submit bids to construct phases of the project for which we are qualified. In some situations, we also solicit bids from other construction contractors. If we are the lower bidder, we are awarded a contract for that phase. In other situations, if our bid is close to the cost estimates determined by the customer and the engineer, then we will generally be awarded the contract for a particular phase; otherwise, the customer negotiates with us on an appropriate contract price; and if those negotiations are not successful, then the customer can terminate our contract.

To manage risks of changes in material prices and subcontracting costs used in tendering bids for construction contracts, we generally obtain firm price quotations from our suppliers and subcontractors, except for fuel and trucking, before submitting a bid. For fixed unit price contracts, these quotations do not include any quantity guarantees, and we have no obligation for materials or subcontract services beyond those required to complete the respective contracts that we are awarded for which quotations have been provided. For design-build and CM/GC projects, lump sum subcontracts are often executed with subcontractors.

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

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

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

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

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

Joint Ventures.

We participate in joint ventures with other large construction companies and other partners, typically for large, technically complex projects, including design-build projects, when it is desirable to share risk and resources in order to seek a competitive advantage or when the project is too large for us to obtain sufficient bonding. Joint venture partners typically provide independently prepared estimates, furnish employees and equipment, enhance bonding capacity and often also bring local knowledge and expertise. We select our joint venture partners based on our analysis of their construction and financial capabilities, expertise in the type of work to be performed and past working relationships with us, among other criteria.

Under a joint venture agreement, one partner is typically designated as the sponsor or manager. The sponsoring partner typically provides all administrative, accounting and most of the project management support for the project and generally receives a fee from the joint venture for these services. We have been designated as the sponsoring partner in certain of our current joint venture projects and are a non-sponsoring partner in others.

Joint venture contracts with project owners typically impose joint and several liability on the joint venture partners. Although our agreements with our joint venture partners provide that each party will assume and pay its share of any losses resulting from a project, if one of our partners is unable to pay its share, we would be fully liable 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 incurs 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.

Insurance and Bonding.

All of our buildings and equipment are covered by insurance, at levels which our management believes to be adequate. In addition, we maintain general liability and excess liability insurance, workers' compensation insurance and auto insurance all in amounts consistent with our risk of loss and industry practice.

As a normal part of the construction business, we are generally required to provide various types of surety and payment bonds that provide an additional measure of security for our performance under the contract. Typically, a bidder for a contract must post a bid bond, generally for 5% to 10% of the bid amount, and on winning the bid, must post a performance and payment bond for 100% of the contract amount. 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, 2016, the Company had approximately 1,684 employees, including 1,364 field personnel. Of our 1,364 field employees, 366 were union members primarily in Nevada, Arizona, California and Hawaii, and covered by collective bargaining agreements.

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 a result of construction projects being 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 intense 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 worksites. 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 and stretch 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 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) where those reports are filed. Our website also has recent press releases, the Company's Code of Business Conduct & Ethics, the charters of the Audit Committee, Compensation Committee, and Corporate Governance & Nominating Committee of the Board of Directors and information on the Company's "whistle-blower" procedures. Our website content is made available for information purposes only. It should not be relied upon for investment purposes, and none of the information on the website is incorporated into this Report by this reference to it.

Item 1A. Risk Factors.

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

***Risks Relating to Our Business*.**

If we are unable to accurately estimate the overall risks, requirements or costs 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 approved quantities irrespective of our actual per unit costs. Lump sum contracts require that the total amount of work be performed for a single price irrespective of our actual per unit costs. We realize a profit on our contracts only if we accurately estimate our costs and then successfully control actual costs and avoid cost overruns, and our revenues exceed actual costs. If our cost estimates for a contract are inaccurate, or if we do not execute the contract within our cost estimates, then cost overruns may cause us to incur losses or cause the contract not to be as profitable as we expected. The final results under 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 projections 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;
- changes in availability, proximity and costs of materials, including steel, concrete, aggregates and other construction materials (such as stone, gravel, sand and oil for asphalt paving), as well as fuel and lubricants for our equipment;
- inability to predict the costs of accessing and producing aggregates and purchasing oil required for asphalt paving projects;
- availability and skill level of workers in the geographic location of a project;
- 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 production; 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 part.

Many of our contracts with public sector customers contain provisions that purport to shift some or all of the above risks from the customer to us, even in cases where the customer is partly at fault. Our experience has often been that public sector customers have been willing to negotiate equitable adjustments in the contract compensation or completion time provisions if unexpected circumstances arise. However, 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.

We may be unable to grow our revenues and increase our profitability.

Our revenue has fluctuated in recent years, in part through market conditions and, in 2007, 2009 and 2011, acquisitions that expanded our geographical footprint. We may be unable to grow our revenues for a variety of reasons, including decreased government funding for infrastructure projects, limits on additional growth in our current markets, reduced spending by our customers, an increased number of competitors, less success in competitive bidding for contracts, limitations on access to necessary working capital and investment capital to sustain growth, limitations on access to bonding to support increased contracts and operations, inability to hire and retain essential personnel and to acquire equipment to support growth, and inability to identify acquisition candidates and successfully acquire and integrate them into our business. A substantial decline in our revenue could have a material adverse effect on our financial condition and results of operations if we are unable to also reduce our operating expenses. See “Recent Developments Financial Results for 2016, Operational Issues and Outlook for 2017 Financial Results” above for further discussion of the impact on our financial results.

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

Our business is highly dependent on the amount and timing of infrastructure work funded by various governmental entities, which, in turn, depends on the overall condition of the economy, the need for new or replacement infrastructure, the priorities placed on various projects funded by governmental entities and federal, state or local government spending levels. Spending on infrastructure could decline for numerous reasons, including decreased revenues received by state and local governments for spending on such projects, including federal funding. The most recent recession caused a nationwide decline in home sales and an increase in foreclosures, which correspondingly resulted in decreases in property taxes and some other local taxes, which are among the sources of funding for municipal road, bridge and water infrastructure construction. State spending on highway and other projects can be adversely affected by decreases or delays in, or uncertainties regarding, federal highway funding, which could adversely affect us. We are reliant upon contracts with 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 markets and their funding sources.

We operate in Texas, Utah, Nevada, Colorado, Arizona, California, Hawaii and to a lesser extent in other states, and adverse changes to the economy and business environment in those states have had an adverse effect on, and could continue to adversely affect, our operations, which could lead to lower revenues and reduced profitability.

Because of this concentration in specific geographic locations, we are susceptible to fluctuations in our business caused by adverse economic or other conditions in these regions, including natural or other disasters. The stagnant or depressed economy, to varying degrees, in Texas, Utah, Nevada, Colorado, Arizona, California and Hawaii have adversely affected, and could continue to adversely affect, our business and results of operations.

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

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

Our 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 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 contracts, in addition to cost. Within our markets, we compete with many international, national, regional and local construction firms. Some of these competitors have achieved greater market penetration than we have in the markets in which we compete, and some may have greater financial and other resources than we do. In addition, there are a number of international and national companies in our industry that are larger than we are and that, if they so desire, could establish a presence in our markets and compete with us for contracts.

In some markets where residential and commercial projects have significantly diminished, the bidding environment in our markets has been much more competitive as construction companies that lack available work in those markets have begun bidding on projects in our markets, sometimes at bid levels below our break-even pricing. In addition, traditional competitors on larger transportation and water infrastructure projects also appear to have been bidding at less than normal margins, and in some cases at below our break-even pricing, in order to replenish their backlogs. As a result, we may need to accept lower contract margins in order to compete against competitors that have the ability to accept awards at lower prices or have a pre-existing relationship with a customer.

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.

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

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

We also rely on third-party suppliers to provide most of the materials (including aggregates, cement, asphalt, concrete, steel, pipe, oil and fuel) for our contracts, except in Utah and Nevada where we source and produce some of the aggregates we use from quarries in which we have mining rights. We do not own or operate any quarries in Texas, Arizona, California, or Hawaii. We normally do not bid on contracts unless we have commitments from suppliers for the materials and subcontractors for certain of the services required to complete the contract and at prices that we have included in our bid, except for some construction projects in Utah and Nevada where we use aggregates from quarries in which we have mining rights. Thus, to the extent that we cannot obtain commitments from our suppliers for materials and subcontractors for certain of the services, our ability to bid for contracts may be impaired. In addition, if a supplier or subcontractor is unable to deliver materials or services according to the negotiated terms of a supply/services agreement for any reason, including the deterioration of its financial condition, we may suffer delays and be required to purchase the materials/services 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.

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

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

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

Our ability to attract and retain reliable, qualified personnel is a significant factor that enables us to successfully bid for and profitably complete our work. This includes members of our management, project managers, estimators, supervisors, foremen, equipment operators and laborers. The loss of the services of any of our management could have a material adverse effect on us. Our future success will also depend on our ability to hire and retain, or to attract when needed, highly-skilled personnel. 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 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.

In Nevada, Arizona, California and Hawaii, a substantial number of our equipment operators and laborers are unionized. Any work stoppage or other labor dispute involving our unionized workforce, or inability to renew contracts with the unions, could have a material adverse effect on our operations and operating results.

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

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

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

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

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

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 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 construction projects may have a material adverse effect on our financial position, results of operations and cash flows.

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

Because all of our construction projects are built outdoors, work on our contracts is subject to unpredictable weather conditions, which could become more frequent or severe if general climatic changes occur. For example, evacuations in Texas due to hurricanes along the U.S. Gulf of Mexico coastal areas can result in our inability to perform work on all Houston-area contracts for several days. 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. 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.

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

It is generally very difficult to predict whether and when new contracts will be offered for tender, as these contracts frequently involve a lengthy and complex design and bidding process, which is affected by a number of factors, such as market conditions, 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 contract awards may also present difficulties in matching the size of our equipment fleet and work crews with contract needs. In some cases, we may maintain and bear the cost of more equipment and ready work crews than are currently required, in anticipation of future needs for existing contracts or expected future contracts. If a contract is delayed or an expected contract award is not received, we would incur costs that could have a material adverse effect on our anticipated profit.

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

Our participation in 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 upon managing the risks discussed in the various risks described in these “Risk Factors” and 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 reduction to 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.

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

Due to the size and nature of our construction contracts, one or a few customers have in the past and may in the future represent a substantial portion of our consolidated revenues and gross profits in any one year or over a period of several consecutive years. 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. 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.

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.

A significant portion of our contracts is built 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 continue to maintain the equipment in our fleet, we may be forced to obtain third-party repair services, which could increase our costs. In addition, the market value of our equipment may unexpectedly decline at a faster rate than anticipated.

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

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

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

Our workers are subject to the usual hazards associated with providing construction and related services on construction sites, plants and quarries. Operating hazards can cause personal injury and loss of life, damage to or destruction of property, plant and equipment and environmental damage. We 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.

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.

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. Immigration laws require us to take certain steps intended to confirm the legal status of our immigrant labor force, but we may nonetheless unknowingly employ undocumented immigrants. Violations of such laws and regulations could subject us to substantial fines and penalties, cleanup costs, third-party property damage or personal injury claims. In addition, these laws and regulations have become, and enforcement practices and compliance standards are becoming, increasingly stringent. Moreover, we cannot predict the nature, scope or effect of legislation or regulatory requirements that could be imposed, or how existing or future laws or regulations will be administered or interpreted, with respect to products or activities to which they have not been previously applied. Compliance with more stringent laws or regulations, as well as more vigorous enforcement policies of the regulatory agencies, could require us to make substantial expenditures for, among other things, pollution control systems and other equipment that we do not currently possess, or the acquisition or modification of permits applicable to our activities.

Our aggregate quarry 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.

Force majeure events, such as terrorist attacks or natural disasters, have impacted, and could continue to negatively impact, the U.S. economy and the markets in which we operate.

Force majeure events, such as terrorist attacks or natural disasters, have contributed to economic instability in the United States in the past and further acts of terrorism, violence, war, or natural disasters could affect the markets in which we operate, our business and our expectations. Armed hostilities may increase, or terrorist attacks, or responses from the United States, may lead to further acts of terrorism and civil disturbances in the United States or elsewhere, which may further contribute to economic instability in the United States. These force majeure events may affect our operations or those of our customers or suppliers and could impact our revenues, our production capability and our ability to complete contracts in a timely manner.

We rely on information technology systems to conduct our business, and disruption, failure or security breaches of these systems could adversely affect our business and results of operations.

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 maintained 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.

Risks Related to Our Financial Results and Financing Plans.

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

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

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

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

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

We are subject to certain covenants under our equipment-based credit facility that could limit our flexibility in managing our business.

We have an equipment-based credit facility that restricts us from engaging in certain activities, including our ability (subject to certain exceptions) to:

- incur liens or encumbrances;
- incur further indebtedness;
- dispose of a material portion of assets or merge with a third party;
- make acquisitions; and
- make investments in securities.

Our credit facility bears interest at an initial annual rate of 12%, which is subject to (i) a decrease of up to two percentage points based on the Company's fixed charge coverage ratio for each of the most recently ended four quarters beginning with the four quarterly period ended June 30, 2016; and (ii) an increase of up to two percentage points beginning December 31, 2015 based on the fixed charge coverage ratio at the end of the following four quarters. To the extent that the fixed charge ratio calculation described above results in an interest rate increase, the increase in interest expense could have a material adverse effect on our business operations, financial performance and financial condition.

We are subject to a limitation on the amount that we can borrow under our equipment-based credit facility based on the value of our collateralized equipment.

Our equipment-based credit facility is secured by all of the Company’s personal property except accounts receivable, including all of its construction equipment, which forms the basis of our borrowing capacity under our credit facility. This facility is also secured by one-half of the equipment of the Company’s 50%-owned affiliates. The sum of the amount borrowed may not exceed the lesser of $40 million or 65% of the appraised value of the collateral pledged for the facility. At December 31, 2016, the Company had approximately $24.4 million of borrowing base which was the result of calculating 65% of the appraised value of the Company’s collateral. Based on market conditions, which includes the amount of construction work available and the demand for construction equipment, the appraised value of our equipment may be subject to fluctuating values. If these market conditions are unfavorable, we may see a decline in our borrowing availability that could result in liquidity constraints, which could materially and adversely affect our business, results of operations and financial condition.

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:

- contract 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 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.

If we were required to write down all or part of our goodwill, our net earnings and net worth could be materially and adversely affected.

We had $54.8 million of goodwill recorded on our consolidated balance sheet at December 31, 2016. 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. 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 has been impaired. We perform an annual test of our goodwill to determine if it has 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 may be substantial. If we were required to write down all or a significant part of our goodwill in future periods our net earnings and equity could be materially and adversely affected.

Item 1B. Unresolved Staff Comments.

None

Item 2. Properties.

Our corporate headquarters are located in The Woodlands, Texas, in 12,340 square feet of office space leased with a seven year term. Our executive, finance and accounting offices are located at this facility. We also have an office located in Lafayette, Colorado where we lease a small office for our information technology professionals.

Our TSC office building is located in Houston, Texas, which houses TSC's executive management, project management and finance and accounting offices. The building is located on a seven-acre parcel of land on which the TSC Houston division's equipment repair center is also located. We also own land, have repair facilities and have constructed offices in San Antonio and Dallas.

Our Utah operations lease office space in Draper, Utah, near Salt Lake City, and also repair facilities in West Jordan City, Utah from entities owned primarily by certain officers of RLW. Refer to Note 17 to the consolidated financial statements for additional information regarding related party transactions.

Our Nevada operations lease office space in Sparks, Nevada, and we own our office and repair facilities located on a forty-five acre parcel of land in Lovelock, Nevada. We also lease the right to mine stone and sand at quarry sites in Nevada. In Nevada, we generally source and produce our own aggregates, either from our own quarries or from other sources near job sites where we enter into short-term leases to acquire the aggregates necessary for the job.

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.

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.

The information concerning mine safety violations and other regulatory matters required by section 1503(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act and Item 104 of Regulation S-K is included in Exhibit 95.1 of this Annual Report on Form 10-K, which is incorporated by reference.

Executive Officers of the Registrant

(At March 1, 2017)

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
Paul J. Varello	73	Chief Executive Officer	2015
Joseph A. Cutillo	51	President	2016
Con L. Wadsworth	56	Executive Vice President & Chief Operating Officer	2016
Ronald A. Ballschmiede	61	Executive Vice President & Chief Financial Officer, Chief Accounting Officer, Treasurer	2015
Roger M. Barzun	75	Senior Vice President & General Counsel, Secretary	2006

Each executive officer is elected 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.

Mr. Varello, who has been a director of the Company since January 2014, was elected Chief Executive Officer in February 2015, initially in an interim capacity. Mr. Varello is the Founder and President of Commonwealth Projects, LLC, a project development company specializing in developing LNG projects in the Caribbean Basin and Bermuda. He is the former Founder and Chairman of Commonwealth Engineering & Construction, LLC (CEC), an engineering and construction management company specializing in the design and construction of major capital projects for the oil & gas, refining, alternative fuels, power, and related energy industries, which he sold in 2014. Prior to founding CEC in May 2003, Mr. Varello was Senior Partner of Varello & Associates, a company that provided technical assessments, economic evaluations, estimates and constructability reviews to project lenders, plant operators and engineering companies from September 2001 to May 2003.

Mr. Cutillo joined the Company in October 2015 as Vice President – Strategy & Business Development. In May 2016, he was promoted to Executive Vice President & Chief Business Development Officer. In February 2017, he was elected President of the Company. 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 $200 million private equity-backed trenchless pipe rehabilitation company.

Mr. Wadsworth joined the company’s Ralph L. Wadsworth Construction Company, LLC (RLW) subsidiary in 1976 serving in various capacities until March 2016, when he ceased to be President of RLW and was elected to his current position.

Mr. Ballschmiede joined 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). Based in The Hague, Netherlands, CB&I is a leading engineering, procurement and construction contractor.

Mr. Barzun has been an officer of the Company for more than the last five years and also serves as general counsel to other companies from time to time on a part-time basis. He is a member of the bar of New York and Massachusetts.

PART II

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

The Company's common stock is traded on the NASDAQ Global Select Market ("NGS"). The table below shows the market high and low closing sales prices of the common stock for 2015 and 2016 by quarter.

	High	Low
Year Ended December 31, 2015		
First Quarter	$6.41	$2.41
Second Quarter	4.80	3.26
Third Quarter	5.50	3.72
Fourth Quarter	6.40	3.87
Year Ended December 31, 2016		
First Quarter	$6.29	$4.37
Second Quarter	5.37	4.22
Third Quarter	7.82	5.06
Fourth Quarter	8.99	6.42

On February 28, 2017, there were 818 holders of record of our common stock.

***Dividend Policy*.**

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

***Equity Compensation Plan Information*.**

Certain information about the Company's equity compensation plans is incorporated into "Item 12. — Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters" from the Company's proxy statement for its 2017 Annual Meeting of Stockholders.

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 2011 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.

	December 2011 ($)	December 2012 ($)	December 2013 ($)	December 2014 ($)	December 2015 ($)	December 2016 ($)
Sterling Construction Company, Inc.	100.00	92.29	108.91	59.33	56.45	78.55
Dow Jones US Total Return Index	100.00	116.32	154.68	174.71	175.81	197.35
Dow Jones US Heavy Construction Index	100.00	121.43	159.41	118.72	105.04	129.58

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 in the quarter ended December 31, 2016.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares (or Units) Purchased as Part of Publicly-Announced Plans or Program	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
November 1 – November 31, 2016	18,229 (1)	$ 7.11	--	--

(1) 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 Committee of the Board of Directors.

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:

	Years ended December 31,				
	2016	2015	2014	2013	2012
Revenues	$690,123	$623,595	$672,230	$556,236	$630,507
(Loss) income before income taxes and earnings attributable to noncontrolling interests	$(7,324)	$(17,179)	$(4,593)	$(68,804)	$17,133
Income tax (expense) benefit	(88)	(7)	(632)	(1,222)	579
Net (loss) income	(7,412)	(17,186)	(5,225)	(70,026)	17,712
Noncontrolling owners' interests in earnings of subsidiaries and joint ventures	(1,826)	(3,216)	(4,556)	(3,903)	(18,009)
Net loss attributable to Sterling common stockholders before noncontrolling interest revaluation	(9,238)	(20,402)	(9,781)	(73,929)	(297)
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)	--	(7,686)	(3,992)
Net loss attributable to Sterling common stockholders	$(9,238)	$(39,176)	$(9,781)	$(81,615)	$(4,289)
Net loss per share attributable to Sterling common stockholders:					
Basic and diluted	$(0.40)	$(2.02)	$(0.54)	$(4.91)	$(0.26)
Weighted average number of common shares outstanding used in computing per share amounts:					
Basic and diluted	23,140	19,375	18,063	16,635	16,421
Cash dividends declared	$--	$--	$--	$--	$--
Balance sheet:					
Total assets	$301,823	$266,165	$306,451	$273,018	$331,510
Long-term debt	$1,549	$15,324	$37,021	$8,331	$24,201
Equity attributable to Sterling common stockholders	$107,434	$95,845	$133,686	$128,893	$210,148
Book value per share of outstanding common stock attributable to Sterling common stockholders	$4.30	$4.85	$7.11	$7.74	$12.74
Shares outstanding	24,987	19,753	18,803	16,658	16,495

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

Overview.

We are a company that operates in one segment, heavy civil construction, through our subsidiaries and which specializes in the building and reconstruction of transportation and water infrastructure in Texas, Utah, Nevada, Colorado, Arizona, California, Hawaii and other states in which there are profitable construction opportunities. Its transportation infrastructure projects include highways, roads, bridges, airfields, ports and light rail. Its water infrastructure projects include water, wastewater and storm drainage systems. We have strategically expanded our operations, either by establishing an office in a new market, often after having successfully bid on and completed a project in that market, or by acquiring a company that gives us an immediate entry into a market.

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
- Contracts receivable, including retainage
- Valuation of long-lived assets and goodwill
- Income taxes
- Segment reporting

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

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 under the percentage-of-completion method, the valuation of long-lived assets (including goodwill), and income taxes. Management continually evaluates all of its estimates and judgments based on available information and experience; however, actual amounts could differ from those estimates.

Revenue Recognition.

The majority of our construction contracts with our customers are "fixed unit price" and "lump sum" 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). Most of our state and municipal contracts provide for termination of the contract for the convenience of the owner, with provisions to pay us only for work performed through the date of termination.

Revenue from these construction contracts is recognized using the percentage-of-completion accounting method. Under this method, revenue is recognized as costs are incurred in an amount equal to cost plus the related expected profit based on the ratio of costs incurred to estimated final costs. This cost-to-cost measure is used because management considers it to be the best available measure of progress on these contracts. Contract costs consist of direct costs on contracts, including labor, materials, amounts payable to subcontractors and those indirect costs related to contract performance, such as indirect salaries and wages, equipment maintenance, repairs, fuel and depreciation, insurance and payroll taxes. Contract cost is recorded as incurred, and revisions in contract revenue and cost estimates are reflected in the accounting period when known. 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 change orders, 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.

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 for which we have a change of scope for which we believe we are contractually entitled to additional price but a price change associated with the scope change 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 support these requirements, the existence of the following items must be satisfied: 1. 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; 2. 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; 3. Costs associated with the claim are identifiable or otherwise determinable and are reasonable in view of the work performed; and 4. The evidence supporting the claim is objective and verifiable, not based on management's subjective evaluation of the situation or on unsupported representations. Revenues in excess of contract costs incurred on claims are 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.

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

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. Results for 2016, 2015 and 2014 were adversely affected by certain weather conditions and revisions to estimated profitability on our construction projects. See "Recent Developments Financial Results for 2016, Operational Issues and Outlook for 2017 Financial Results" above and "Results of Operations Fiscal Year Ended December 31, 2016 Compared with Fiscal Year Ended December 31, 2015" for further discussion of the impact on our financial results.

Contracts Receivable, Including Retainage.

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 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 on active contracts 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, 2016 and 2015, contracts receivable included $23.4 million and $19.8 million of retainage, respectively, which is being contractually withheld by customers until completion of the contracts.

There are certain contracts that are completed in advance of full payment. When the receivable will not be collected within our normal operating cycle, we consider it a long-term contract receivable and it is recorded in “Other assets, net” in our balance sheet. We consider the credit quality of the borrower to assess the appropriate discount rate to apply and continuously monitor the borrower’s credit quality. At December 2016 and 2015, there were no such long-term contract receivables recorded in our consolidated balance sheets.

As the majority of our construction contracts are entered into with federal, state or municipal government customers, credit risk is minimal. The Company ascertains that funds have been appropriated by the governmental project owner prior to commencing work on such projects. 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 mechanics liens, which give the Company high priority in the event of lien foreclosures following financial difficulties of private owners.

Contracts receivable are written off based on individual credit evaluation and specific circumstances of the customer, when such treatment is warranted. There was no bad debt expense recorded in 2016 and 2014 and a minimal amount recorded in 2015.

Based upon a review of outstanding contracts receivable, historical collection information and existing economic conditions, management has determined that all of contracts receivable at December 31, 2016 are fully collectible and accordingly, no allowance for doubtful accounts against contracts receivable was recorded.

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, 2016 and 2015, there were no events or changes in circumstances that would indicate a material impairment of our long-lived assets.

Goodwill must be tested for impairment at least annually and we performed our most recent annual impairment test of historical goodwill on October 1, 2016. Based on our one reporting unit, our test indicated there was no impairment of goodwill. See “Segment Reporting” below for further information regarding the determination of our reporting unit. Note 8 to the consolidated financial statements discusses the two valuation approaches 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. These valuation approaches are impacted by a number of factors but the key factors are the Company’s stock price, the estimated control premium and our estimated forecast of future cash flows. The valuation approaches contain uncertainty regarding the estimates used. One of the largest uncertainties relates to local, state and government spending which management expects to increase in the upcoming years. There are a number of other uncertainties with respect to our future financial performance that could impact estimated future cash flows. These are discussed in a number of places including “Item 1A. Risk Factors.” Based on our valuation approaches, we determined that the fair value of the Company’s equity was above the carrying value of the Company’s equity at December 31, 2016 and 2015. At December 31, 2016 and 2015, we had goodwill with a carrying amount of approximately $54.8 million.

Income Taxes.

Deferred tax assets and liabilities are recognized based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. We regularly review our deferred tax assets for recoverability and, where necessary, establish a valuation allowance.

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. To assess the likelihood, we use historical three-year accumulated losses, estimates and judgment regarding our future taxable income, as well as the jurisdiction in which this taxable income is generated, to determine whether a valuation allowance is required. Such evidence can include our current financial position, our results of operations, both actual and forecasted results, the reversal of deferred tax liabilities, and tax planning strategies as well as the current and forecasted business economics of our industry. Additionally, we record uncertain tax positions at their net recognizable amount, based on the amount that management deems is more likely than not to be sustained upon ultimate settlement with the tax authorities in the domestic and international tax jurisdictions in which we operate. On the basis of our evaluations, at December 31, 2016 and 2015, a full valuation allowance was recorded on our net deferred tax assets and we had no material uncertain tax positions.

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.

Segment Reporting.

We operate in one operating segment and have only one reportable segment and one reporting unit component, which is heavy civil construction. In making this determination, the Company considered the discrete financial information used by our Chief Operating Decision Maker ("CODM"). Based on this approach, the Company noted that the CODM organizes, evaluates and manages the financial information around each heavy civil construction project when making operating decisions and assessing the Company's overall performance. The service provided by the Company, in all instances of our construction projects, is heavy civil construction. Furthermore, we considered that each heavy civil construction project has similar characteristics, includes similar services, has similar types of customers and is subject to similar economic and regulatory environments which would allow aggregation of individual operating segments into one reportable segment if multiple operating segments existed.

In addition, the Company noted that even if our local offices were to be considered separate components of our heavy civil construction operating segment, those components could be aggregated into a single reporting unit for purposes of testing goodwill for impairment because our local offices all have similar economic characteristics and are similar in all of the following areas:

- The nature of the products and services — each of our local offices perform similar construction projects — they build, reconstruct and repair roads, highways, bridges, airfields, ports, light rail and water, waste water and storm drainage systems.
- The nature of the production processes — our heavy civil construction services rendered in the construction process for each of our construction projects performed by each local office is the same — they excavate dirt, remove existing pavement and pipe, lay aggregate or concrete pavement, pipe and rail and build bridges and similar large structures in order to complete our projects.
- The type or class of customer for products and services — substantially all of our customers are state departments of transportation, cities, counties, and regional water, rail and toll-road authorities. A substantial portion of the funding for the state departments of transportation to finance the projects we construct is furnished by the federal government.
- The methods used to distribute products or provide services — the heavy civil construction services rendered on our projects are performed primarily with our own field work crews (laborers, equipment operators and supervisors) and equipment (backhoes, loaders, dozers, graders, cranes, pug mills, crushers, and concrete and asphalt plants).
- The nature of the regulatory environment — we perform substantially all of our projects for federal, state and municipal governmental agencies, and all of the projects that we perform are subject to substantially similar regulation under U.S. and state department of transportation rules, including prevailing wage and hour laws; codes established by the federal government and municipalities regarding water and waste water systems installation; and laws and regulations relating to workplace safety and worker health of the U.S. Occupational Safety and Health Administration and to the employment of immigrants of the U.S. Department of Homeland Security.

While profit margin objectives included in contract bids have some variability from contract to contract, our profit margin objectives are not differentiated by our CODM or our office management based on local office location. Instead, the projects undertaken by each local office are primarily competitively-bid, fixed unit or negotiated lump sum price contracts, all of which are bid based on achieving gross margin objectives that reflect the relevant skills required, the contract size and duration, the availability of our personnel and equipment, the makeup and level of our existing backlog, our competitive advantages and disadvantages, prior experience, the contracting agency or customer, the source of contract funding, anticipated start and completion dates, construction risks, penalties or incentives and general economic conditions.

Market Outlook and Trends

Market outlook: Our core business is primarily driven by federal, state and municipal funding. The late 2015 passage of the federally funded five-year $305 billion surface transportation bill will increase the annual federal highway investment by 15.1% over the five-year period from 2016 to 2020. In addition to the Federal program, several of the states in our key markets have instituted actions to further increase annual spending. In Texas, two constitutional amendments were passed, which will increase the annual funds allocated to transportation projects by $4.0 billion to $4.5 billion per year. In Utah, a 20% gas tax increase was put into effect January 1, 2016, which is the first state gas tax increase in 18 years. In addition, a 1-cent sales tax increase was approved in Los Angeles, California in 2016 which will provide $3 billion a year for local road, bridge and transit projects.

Bid discipline and project execution: To ensure that we take full advantage of the improved market conditions and maximize profitability we have completed an extensive evaluation of our projects' historical success 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, we believe will enable us to focus our resources on the most beneficial projects and significantly reduce our risk. In addition, in order to strengthen these processes and capitalize further on the improved market conditions, we appointed a Chief Operating Officer late in the first quarter of 2016.

Backlog, backlog gross margin and gross margin trends:

	Backlog	Gross Margin in Backlog
	(Dollar amounts in thousands)	
Fourth quarter of 2016	$823,000	8.2%
Third quarter of 2016	$820,000	8.0%
Second quarter of 2016	$810,000	7.8%
First quarter of 2016	$854,000	7.7%
Fourth quarter of 2015	$761,000	7.0%

Our total margin in backlog has increased approximately 120 basis points, from 7.0% at December 31, 2015 to 8.2% at December 31, 2016. During 2016 we won approximately $749 million worth of new projects at an average margin of 9%. The increases noted above are primarily the result of the improving market conditions and actions that we have taken to improve bid discipline.

Our gross margin has increased 39.1% from the full year of 2015 compared to the full year of 2016. This increase is a result of the improving market conditions, our enhanced bid discipline and our improving project execution.

Summary of Financial Results for 2016.

In 2016, we had operating loss of $4.7 million, loss before income taxes and earnings attributable to noncontrolling interest owners of $7.3 million, net loss attributable to Sterling common stockholders of $9.2 million and net loss per diluted share attributable to Sterling common stockholders of $0.40.

Results of Operations.

Backlog at December 31, 2016.

At December 31, 2016, our backlog of construction projects was $823 million, as compared to $761 million at December 31, 2015. Our contracts are typically completed in 12 to 36 months. At December 31, 2016 and 2015, there was approximately $226 million and $197 million, respectively, excluded from our consolidated backlog where we were the apparent low bidder, but had not yet been formally awarded the contract or the contract price had not been finalized. Backlog included $53 million and $12 million attributable to our share of estimated revenues related to joint ventures where we are a noncontrolling joint venture partner at December 31, 2016 and 2015, respectively.

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 and their funding sources.

Fiscal Year Ended December 31, 2016 Compared with Fiscal Year Ended December 31, 2015

	2016	2015	% Change
	(Dollar amounts in thousands)		
Revenues	$ 690,123	$ 623,595	10.7 %
Gross profit	43,854	$ 28,953	51.5
General and administrative expenses	(38,623)	(41,880)	(7.8)
Other operating (expense) income, net	(9,960)	(1,460)	NM
Operating income (loss)	(4,729)	(14,387)	(67.1)
Interest income	33	460	(92.8)
Interest expense	(2,628)	(3,012)	(12.7)
Loss on extinguishment of debt	--	(240)	NM
Loss before income taxes and earnings attributable to noncontrolling interests	(7,324)	(17,179)	(57.4)
Income tax expense	(88)	(7)	NM
Net loss	(7,412)	(17,186)	(56.9)
Noncontrolling owners' interests in earnings of subsidiaries	(1,826)	(3,216)	(43.2)
Net loss attributable to Sterling common stockholders before noncontrolling interest revaluation	(9,238)	(20,402)	(54.7)
Revaluation of noncontrolling interest due to a new agreement	--	(18,774)	NM
Net loss attributable to Sterling common stockholders	$ (9,238)	$ (39,176)	(76.4)
Gross margin	6.4 %	4.6 %	39.1
Operating margin (deficit)	(0.7)%	(2.3)%	(69.6)
Contract backlog, end of year	$ 823,000	$ 761,000	8.1

NM – Not meaningful.

Revenues.

Revenues for 2016 increased $66.5 million, or 10.7%, compared with the prior year. As our markets continue to improve, so has the trend of increasing backlog which increased $62 million from December 31, 2015 to December 31, 2016. This trend has contributed to the increased execution of projects and has favorably affected revenues in 2016. Specifically, the $66.5 million increase is attributable to a total increase of approximately $106 million primarily due to the ramp up of two large Utah projects constructed by our majority-owned joint venture and construction on large projects in Nevada and Hawaii. This increase was offset by approximately $39 million of decreased project activity primarily in California and Texas due to the winding down of a large project in California and heavy rainfall and a slower ramp up of new work driven by owner delays in Texas.

Gross profit.

Gross profit increased $14.9 million, or 51.5% in 2016 compared with the prior year. Gross margin also increased to 6.4% in 2016 from 4.6% in 2015, primarily as a result of constructing higher margin projects which stem from higher margins in our backlog. Our backlog margins have increased from 7.0% to 8.2% as of December 31, 2015 and 2016, respectively. In addition, these projects are being executed with less downward percent-complete revisions which have positively affected profitability in 2016.

While there are a number of factors which cause the costs incurred and gross profit realized on our contracts to vary, sometimes substantially, from our original projections, the primary factors which result in downward revisions are:

- conditions or contract requirements that differed from those assumed in the original bid or contract;
- delays in taking measures to address issues which arose during construction; and
- subcontractor performance issues and vendor material spot shortages which caused project progress delays.

At times, we may be entitled to claim proceeds related to customer-caused delays, errors in specification and designs or other causes of unanticipated additional costs related to certain projects; however, we cannot predict the amount of claim proceeds or the timing of the receipt of such proceeds. Claims are included in the calculation of revenue when realization is probable and amounts can be reliably determined to the extent costs are incurred. Revenues in excess of contract costs incurred on claims are 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.

At December 31, 2016, we had approximately 125 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.

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 upon completing work associated with 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 may be taken.

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, we concluded that including the unapproved change order, claim and entitled unpaid project price amounts of $2.2 million, $9.2 million and $3.9 million, respectively, at December 31, 2016, and $1.6 million, $5.2 million and $3.9 million, respectively, at December 31, 2015, in "Costs and estimated earnings in excess of billings on uncompleted contracts" on our consolidated balance sheets was in accordance with GAAP. 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.

Other operating (expense) income, net.

Other operating (expense) income, net, includes 50% of earnings and losses related to members' interests, gains and losses from sales of property, plant and equipment, and other miscellaneous operating income or expense. Members' interest earnings are treated as an expense while losses are treated as income as earnings would increase the amount in our liability account "Members' interest subject to mandatory redemption and undistributed earnings," and losses would decrease this liability. Other operating expense increased to $10.0 million in 2016 from $1.5 million in 2015, with the increase being primarily the result of an increase in Members' interest earnings of approximately $8.9 million and $1.2 million related to our JBC earn-out expense.

General and administrative expenses.

General and administrative expenses decreased $3.3 million during 2016 to $38.6 million from $41.9 million in 2015. This decrease is primarily the result of certain non-recurring costs related to consulting services performed and employee severance payments of $1.2 million and $2.9 million, respectively, recognized in 2015 offset by an increase in certain employee and employee benefit costs in 2016.

As a percentage of revenues, general and administrative expenses decreased to 5.6% in 2016 from 6.7% in 2015. The decreases in general and administrative expenses, as a percentage of revenue, are primarily the result of the leverage generated from generally fixed costs and increases in revenues.

Income taxes.

Our effective income tax rates for 2016 and 2015 were minimal in both periods. In 2016 and 2015, our effective income tax rate varied from the statutory rate primarily as a result of our deferred tax asset valuation allowance. We expect our tax rate to remain low due to our net operating losses available to offset taxable income.

In order to determine that a valuation allowance was necessary, management assessed the available positive and negative evidence to estimate whether sufficient future taxable income would be generated to use the existing deferred tax assets. A significant piece of objective negative evidence evaluated was the cumulative loss incurred over the three-year period ended December 31, 2016. The cumulative three-year period loss that ended in the fourth quarter of 2016 was the result of the write-downs recorded during the past three years. 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, 2016, a full valuation allowance of $58.0 million has been recorded on our net deferred tax assets including federal and state net operating loss carryforwards as they are not likely to be realized. The amount of the deferred tax asset considered realizable could be adjusted if objective negative evidence is no longer present and additional weight may be given to subjective evidence such as our projections for growth.

Net income attributable to noncontrolling interests.

The decrease of $1.4 million to $1.8 million from $3.2 million in net income attributable to noncontrolling interest owners for the year ended December 31, 2016 compared with the same period in 2015 is primarily related to the November 2015 agreement entered with Myers. This agreement changed our accounting treatment of our Myers 50% noncontrolling interest, which was included in “noncontrolling owners’ interests in earnings of subsidiaries and joint ventures,” to “other operating (expense) income, net” after the agreement was executed. The Myers’ 50% portion of earnings totaled $3.7 million, $3.2 million of which was recorded in “noncontrolling owners’ interest in earnings of subsidiaries and joint ventures” and $0.5 million was recorded in “other operating expense (income), net.” During 2016, the only income attributable to noncontrolling interests was primarily from our Utah construction joint venture where our joint venture partner has a 40% noncontrolling interest. Net income attributable to noncontrolling interest from construction joint ventures was $1.8 million and an immaterial amount in 2016 and 2015, respectively.

Revaluation of noncontrolling interest due to a new agreement.

Refer to the section below titled “*Fiscal Year Ended December 31, 2015 Compared with Fiscal Year Ended December 31, 2014, – Revaluation of noncontrolling interest due to a new agreement*” for the explanation of the 2015 increase.

Fiscal Year Ended December 31, 2015 Compared with Fiscal Year Ended December 31, 2014

	2015	2014	% Change
	(Dollar amounts in thousands)		
Revenues	$ 623,595	$ 672,230	(7.2)%
Gross profit	$ 28,953	$ 32,421	(10.7)
General and administrative expenses	(41,880)	(36,897)	13.5
Other operating (expense) income, net	(1,460)	252	NM
Operating loss	(14,387)	(4,224)	NM
Interest income	460	754	(39.0)
Interest expense	(3,012)	(1,123)	NM
Loss on extinguishment of debt	(240)	--	NM
Loss before income taxes and earnings attributable to noncontrolling interests	(17,179)	(4,593)	NM
Income tax expense	(7)	(632)	(98.9)
Net loss	(17,186)	(5,225)	NM
Noncontrolling owners’ interests in earnings of subsidiaries	(3,216)	(4,556)	(29.4)
Net loss attributable to Sterling common stockholders before noncontrolling interest revaluation	(20,402)	(9,781)	NM
Revaluation of noncontrolling interest due to a new agreement	(18,774)	--	NM
Net loss attributable to Sterling common stockholders	$ (39,176)	$ (9,781)	NM

Gross margin	4.6	%	4.8	%	(4.2)
Operating margin (deficit)	(2.3	)%	(0.6	)%	NM
Contract backlog, end of year	$ 761,000		$ 764,000		(0.4)

NM – Not meaningful.

Revenues.

Revenues for 2015 decreased 7.2% or $48.6 million compared to the prior year. Of the $48.6 million decrease, $37.6 million was the net decrease in revenues for the Company which largely related to the completion of several large projects in Texas which were ongoing in 2014 and were replaced with smaller, lower revenue projects in 2015; approximately $8.2 million was related to the significant downward first quarter of 2015 percent-complete revisions on Texas projects; and $2.8 million related to the out-of-period correction of an error, which decreased revenue. The majority of the $8.2 million decrease in revenues resulted from adjustments to our production rates related to material, labor and equipment costs on certain Texas projects. During the first half of 2015, we identified an escalation of these costs compared to our estimated costs and noted that there was no way to mitigate or reduce these increases. Therefore, we adjusted our estimated total costs to reflect these additional costs over the remaining duration of the contracts. The increases primarily resulted from greater than anticipated increases in wages at our Texas subsidiary beginning in the first half of 2015, additional material costs as prior purchase orders expired and new purchase orders with higher costs were obtained as a result of extending the construction period due to project delays, and increases in equipment rates due to an unanticipated increase in equipment repair costs (which repairs are typically performed in the winter months due to slower activity caused by the colder and wetter weather, primarily in January and February). As these Texas projects were in a loss position, the effect of downward percent-complete revisions decreases revenues, gross profits and operating losses by the same amounts. This occurs because there are no additional estimated gross profit amounts which would absorb a portion of the downward percent-complete revisions.

Gross profit.

Gross profit decreased $3.5 million in 2015 compared with the prior year. Gross margin also decreased to 4.6% in 2015 from 4.8% in 2014 primarily as a result of the downward percent-complete revisions made to certain projects in the first quarter of 2015, largely related to construction projects in Texas.

While there are a number of factors which cause the costs incurred and gross profit realized on our contracts to vary, sometimes substantially, from our original projections, the primary factors which resulted in downward revisions in estimates in 2015 were:

- conditions or contract requirements that differed from those assumed in the original bid or contract;
- delays in taking measures to address issues which arose during construction; and
- subcontractor performance issues and vendor material spot shortages which caused project progress delays.

We may be entitled to claim proceeds related to customer-caused delays, errors in specification and designs or other causes of unanticipated additional costs related to certain projects; however, we cannot predict the amount of claim proceeds or the timing of the receipt of such proceeds. Claims are included in the calculation of revenue when realization is probable and amounts can be reliably determined to the extent costs are incurred. Revenues in excess of contract costs incurred on claims are 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.

At December 31, 2015, we had approximately 104 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.

Other operating (expense) income, net.

Other operating (expense) income, net, includes 50% of earnings and losses related to members' interests, gains and losses from sales of property, plant and equipment and other miscellaneous operating income or expense. Members' interest earnings are treated as an expense while losses are treated as income as earnings would increase the amount in our liability account "Members' interest subject to mandatory redemption and undistributed earnings," and losses would decrease this liability. The decrease of $1.8 million, to other operating expense of $1.5 million in 2015 from other operating income of $0.3 million in 2014, is primarily the result of an increase in Members' interest earnings.

General and administrative expenses.

General and administrative expenses increased $5.0 million during 2015 to $41.9 million from $36.9 million in 2014. This increase is primarily the result of certain non-recurring costs related to consulting services performed and employee severance payments of $1.2 million and $2.9 million, respectively, recognized in 2015.

As a percentage of revenues, general and administrative expenses increased to 6.7% in 2015 from 5.5% in 2014. The increases in general and administrative expenses, as a percentage of revenue, are primarily the result of the non-recurring consulting services and employee severance costs paid during 2015 and the decline in revenue mentioned above. Excluding these non-recurring costs, general and administrative expenses would have been 6.0% in 2015.

Income taxes.

Our effective income tax rates for 2015 and 2014 were minimal and (13.8)%, respectively. In 2015 and in 2014, our effective income tax rate varied from the statutory rate primarily as a result of our deferred tax asset valuation allowance.

In order to determine that a valuation allowance was necessary, management assessed the available positive and negative evidence to estimate whether sufficient future taxable income would be generated to use the existing deferred tax assets. A significant piece of objective negative evidence evaluated was the cumulative loss incurred over the three-year period ended December 31, 2015. The cumulative three-year period loss that ended in the fourth quarter of 2015 was the result of the write-downs recorded during the past three years. 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, 2015, a full valuation allowance of $56.4 million has been recorded on our net deferred tax assets including federal and state net operating loss carryforwards as they are not likely to be realized. The amount of the deferred tax asset considered realizable could be adjusted if objective negative evidence is no longer present and additional weight may be given to subjective evidence such as our projections for growth.

Net income attributable to noncontrolling interests.

The decrease of $1.4 million to $3.2 million from $4.6 million in net income attributable to noncontrolling interest owners for the year ended December 31, 2015 compared with the same period in 2014 is primarily related to net income attributable to the 50% noncontrolling interest in Myers. Approximately $0.5 million of the $1.4 million decrease related to the accounting treatment which was the result of entering into a new agreement in November 2015.

The accounting treatment now requires noncontrolling interest earnings of certain members to flow through "Other (expense) income, net" in our consolidated statement of operations (refer to Note 4 in our consolidated financial statements), and the remaining $0.9 million was primarily related to lower income generated from Myers in 2015.

Revaluation of noncontrolling interest due to a new agreement.

Revaluation of noncontrolling interest due to a new agreement increased as a result of an amendment to a Myers agreement entered into in November 2015. Due to this agreement, $18.8 million was reclassified to the liability account "Members' interest subject to mandatory redemption and undistributed earnings" and reduced "Additional paid in capital" ("APIC") on the Company's consolidated balance sheets. This $18.8 million represented the portion of the revaluation of noncontrolling interest above the $7.4 million held as "Noncontrolling interest" in the consolidated balance sheet when the agreement was executed. According to GAAP, this reduction to APIC was treated similarly to a dividend to a preferred shareholder and reduced net income attributable to Sterling's stockholders and earnings per share.

Liquidity and Sources of Capital.

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

	Years Ended December 31,	
	2016	2015
Net cash (used in) provided by:		
Operating activities	$ 44,499	$ 8,969
Investing activities	(8,174)	(4,488)
Financing activities	2,034	(22,898)
Total (decrease) increase in cash and cash equivalents	$ 38,359	$ (18,417)

	As of December 31,	
	2016	2015
Cash and cash equivalents	$ 42,785	$ 4,426
Working capital	$ 29,316	$ 30,610

Operating Activities.

During 2016, net cash provided by operating activities was $44.5 million. The drivers of operating activities cash flows were primarily the result of our net loss discussed above, non-cash items, the change in our accounts receivable, inventory, net contracts in progress and accounts payable balances (collectively, “Contract Capital”), and the change in members’ interests subject to mandatory redemption and undistributed earnings as discussed below.

The significant non-cash items reconciled to operating activities include depreciation and amortization expense which was $16.0 million in 2016 and $16.5 million in 2015. Depreciation expense has decreased from 2015 to 2016 as a result of our efforts to maintain our current fleet of equipment and supplement it as necessary with more economical project specific leased equipment. In addition, there was a non-cash revaluation of noncontrolling interest of $18.8 million in 2015 which was discussed above,

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, 2016 and 2015 and variances were as follows (amounts in thousands):

	YTD Changes in Components of Contract Capital		
	2016	2015	Variance
Costs and estimated earnings in excess of billings on uncompleted contracts	$ (5,800)	$ 6,498	$ (12,298)
Billings in excess of costs and estimated earnings on uncompleted contracts	33,544	4,907	28,637
Contracts in progress, net	27,744	11,405	16,339
Contracts receivable, including retainage	(2,020)	(3,216)	1,196
Receivables from and equity in construction joint ventures	5,800	(3,777)	9,577
Inventories	(1,173)	4,866	(6,039)
Accounts payable	8,138	(7,834)	15,972
Contract Capital, net	$ 38,489	$ 1,444	$ 37,045

The 2016 change in Contract Capital increased liquidity by $38.5 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. Contract Capital is also impacted at period-end by the timing of accounts receivable collections and accounts payable payments for our projects.

Members' interests subject to mandatory redemption and undistributed earnings decreased $5.2 million and increased $27.5 million in 2016 and 2015, respectively. The decrease during 2016 is primarily the result of distributions made to the Members while the increase in 2015 was due to the amended Myers agreement and increases in earnings which were not distributed.

Investing Activities.

During 2016, net cash used in investing activities was $8.2 million, compared to $4.5 million in 2015. The primary driver of investing activities cash flows in 2016 was an increase in purchases of capital equipment combined with less cash proceeds from the sale of property and equipment. In 2015, the cash used in investing activities was the cash used as collateral for our letter of credit requirements and for use in an escrow account where both amounts were designated as restricted cash in 2015 as purchases of equipment were offset by proceeds from the sale of equipment.

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 $11.6 million in 2016, which included $0.7 million of financed capital expenditures. Proceeds from the sale of property and equipment totaled $2.7 million for 2016 with an associated net gain of $0.4 million. For the year ended December 31, 2015, capital expenditures totaled $10.8 million, which included $2.7 million of financed capital expenditures, while proceeds from the sale of property and equipment totaled $8.5 million with an associated net gain of $1.5 million. The level of proceeds for the sale of equipment declined in 2016 as a result of the increased sales in 2015 from our initiative to sell non-core and underutilized equipment. Management intends to continue its 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.

At December 31, 2016 and 2015, restricted cash of approximately $3.0 million was designated as collateral for a standby letter of credit in the same amount in accordance with contractual agreements and restricted cash of approximately $2.0 million represents cash deposited by a customer, for the benefit of the Company, in an escrow account which is restricted until the customer releases the restriction upon the completion of the job.

Financing Activities.

During 2016, net cash provided by financing activities was $2.0 million compared to net cash used in financing activities of $22.9 million for 2015. The increase in cash provided by financing activities in 2016 was primarily a result of net proceeds of $19.1 million received from the issuance of common stock which was offset by the Revolving Loan payoff and Term Loan monthly payments along with a total $10.0 million prepayment made in 2016.

During 2015, the drivers of financing activities cash flows were primarily due to the change of our prior credit facility with Comerica Bank, N.A. (“Prior Credit Facility”), usage and repayment of our equipment-based revolver and distributions to owners as discussed below.

Financing activities in 2015 consisted of the net repayments on our Prior Credit Facility of $34.6 million and cumulative drawdowns and repayments on our equipment-based revolver of $14.6 million and cash received from our equipment-based term loan of $18.0 million, net of repayments, both of which were used to fund our operating activities and replace our Prior Credit Facility. Distributions to noncontrolling interest owners were $3.4 million for the year.

Cash and Working Capital.

Cash at December 31, 2016, was $42.8 million which increased from the prior year based on the items mentioned above. Our working capital largely remained flat with a slight decrease of $1.0 million to $29.3 million from $30.6 million at December 31, 2016 and 2015, respectively.

Credit Facility and Other Sources of Capital.

In addition to our available cash, cash equivalents and cash provided by operations, from time to time, we use borrowings under our available credit or equipment-based credit facilities to finance our capital expenditures and working capital needs.

In May 2015, the Company and its wholly-owned subsidiaries entered into a $40.0 million loan and security agreement with Nations Equipment Finance, LLC (“Nations”), consisting of a $20.0 million term loan and a $20.0 million Revolving Loan (combined, the “Equipment-based Facility”), which replaced the Company’s Prior Credit Facility. The sum of the outstanding balances of the Equipment-based Facility may not exceed the lesser of $40.0 million or 65% of the appraised value of the collateral pledged for the loans. At December 31, 2016, the Company had a borrowing base of approximately $24.4 million, which was the result of calculating 65% of the appraised value (where appraised value equals net operating liquidated value) of the Company’s collateral. The amount of the Revolving Loan that may be borrowed from time to time is the lesser of $20.0 million or the available borrowing base. The Revolving Loan may be utilized to provide ongoing working capital and for other general corporate purposes. At December 31, 2016, we had $2.7 million outstanding on the Term Loan, net of $0.8 of deferred loan costs, zero drawn on the Revolving Loan, and $20.0 million of borrowings available.

The Equipment-based Facility bears interest at an initial fixed annual rate of 12%, which is subject to (i) a decrease of up to two percentage points based on the Company's fixed charge coverage ratio for each of the most recently ended four quarters beginning with the four quarters ending June 30, 2016; and (ii) an increase of up to two percentage points beginning December 31, 2015 based on the fixed charge coverage ratio at the end of the following four quarters. The interest rate has not changed since inception and continues to be 12%. Principal on the Term Loan is payable in 47 monthly installments (with accrued interest) with a final payment of the then outstanding principal amount on May 29, 2019. The Term Loan may be prepaid in any year but is subject to a pre-payment fee that declines as the Term Loan nears maturity. Outstanding Revolving Loans are payable in full thirty days before the maturity date of the Term Loan.

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The Equipment-based Facility is secured by all of the Company's personal property except accounts receivable, including all of its construction equipment, which forms the basis of availability under the Revolving Loan. The Equipment-based Facility is also secured by one-half of the equipment of the Company's 50%-owned affiliates, Road and Highway Builders, LLC and Myers & Sons Construction, L.P. pursuant to a separate security agreement with those entities. If a default occurs, Nations may exercise the Company's rights in the collateral, with all of the rights of a secured party under the Uniform Commercial Code, including, among other things, the right to sell the collateral at public or private sale.

The proceeds of the Term Loan of $20.0 million and our initial draw of $14.6 million in 2015 under the Revolving Loan were utilized by the Company to repay the balance outstanding and terminate the Prior Credit Facility and for other general corporate purposes. In addition, in connection with incurring this debt, we recorded $1.3 million in deferred debt issuance costs, which are included in “Long-term debt, net of current maturities” and “Current maturities of long-term debt” in our consolidated balance sheet and are being amortized on a straight line basis over the term of the Equipment-based Facility. In order to extinguish the Prior Credit Facility debt, the Company incurred costs of $0.2 million in 2015, which is included in “Loss on extinguishment of debt” in the Company’s consolidated statement of operations.

The Company’s Equipment-based Facility has no financial covenants; however, it contains restrictions on the Company’s ability to:

- Incur liens and encumbrances on equipment;
- Incur further indebtedness;
- Dispose of a material portion of assets or merge with a third party;
- Make acquisitions; and
- Make investments in securities.

Due to the 2015 Equipment-based Facility agreement, the Company’s Letter of Credit, which under our Prior Credit Facility reduced the Company’s borrowing availability, is now collateralized with cash.

Average combined borrowings under the Equipment-based Facility for the 2016 fiscal year were $18.1 million, and the largest amount of borrowings under the Equipment-based Facility was $31.6 million in January 2016. Average combined borrowings under the Prior Credit Facility and the Equipment-based Facility for the 2015 fiscal year were $25.9 million, and the largest amount of borrowings was under the Equipment-based Facility and was $34.6 million, in June 2015.

Interest expense was $2.6 million for the 2016 fiscal year compared to $3.0 million and $1.1 million in 2015 and 2014, respectively. The decrease in interest expense in 2016 compared with 2015 was due to the decreased debt outstanding during the period offset by prepayment fees. The increase in interest expense in 2015 compared to 2014 was driven by the increased interest rate on the Equipment-based Facility entered into in 2015, as described above.

Based on our average borrowings for 2016 and our 2017 forecasted cash needs, we continue to believe that the Company has sufficient liquid financial resources to fund our requirements for the next twelve months 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, or we continue to incur losses, our working capital could be materially and adversely affected. Refer to “Item 1A. Risk Factors” for further discussion of liquidity related risks.

On May 9, 2016, the Company completed an underwritten public offering of 5,175,000 shares of the Company’s common stock, which included the full exercise of the sole underwriter’s over-allotment option, at a price to the public of $4.00 per share ($3.77 per share net of underwriting discounts). The net proceeds from the offering of $19.1 million, after deducting underwriting discounts and other offering expenses, were used for working capital, repayment of our indebtedness under the revolving loan portion of our Equipment-based Facility and for general corporate purposes.

Due to the continuing improvement in our market strategy along with several large project awards during the year, we will continue to explore additional capital alternatives to further strengthen our financial position in order to take advantage of this improving transportation infrastructure market. This would include the potential sale of assets, businesses or equity, the favorable resolution of outstanding contract claims, refinancing our Equipment-based Facility, or a combination thereof. We expect to use proceeds from these initiatives to invest in projects meeting our gross margin, overall profitability and other requirements, as well as pursuing projects or investments in adjacent markets.

Purchase of Concrete Company.

On March 8, 2017, the Company entered into a definitive agreement to buy Tealstone Construction ("Tealstone"), a Denton, Texas-based concrete construction company for $85 million, subject to specified post-closing adjustments. Tealstone is a market leader in commercial and residential concrete construction in the Dallas-Fort Worth Metroplex. The company serves commercial contractors and multi-family developers, as well as national homebuilders in Texas and Oklahoma.

Sterling plans to finance the acquisition through a combination of $15 million of seller financing, 1,882,058 shares of Sterling common stock, and $55 million of debt from Sterling's new $85 million credit facility, which will replace the existing facility. The transaction is expected to close in the second quarter of 2017 and is contingent on customary closing conditions including new debt financing and regulatory approvals.

Contractual Obligations.

The following table sets forth our fixed, non-cancelable obligations at December 31, 2016:

	Payments due by period				
	Total	**<1 Year**	**1 - 3 Years**	**4 – 5 Years**	**>5 Years**
	(Amounts in thousands)				
Equipment-based term loan	$2,729	$2,729	$--	$--	$--
Equipment-based term loan - interest*	286	286	--	--	--
Operating leases**	11,315	3,634	5,026	2,395	260
Notes payable for equipment	2,665	1,116	1,485	64	--
Earn-out liability	1,242	1,242	--	--	--
Members' interest subject to mandatory redemption and undistributed earnings***	45,230	--	--	--	45,230
	$63,467	$9,007	$6,511	$2,459	$45,490

* Our obligation for interest on our equipment-based term loan is calculated using a 12% interest rate. This rate may increase or decrease by 2% based on the calculated results of our earnings to fixed charge ratio. Refer to Note 9 in the footnotes to our consolidated financial statements for further information.

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

*** Mandatory redemption is based on the death or disability of the interest holders which is not expected to occur within the next five years. 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.

Interest on our Equipment-based Facility is paid monthly in accordance with our Term Loan payment schedule. In 2016 and 2015, interest paid on the Equipment-based Facility and Prior Credit Facility was approximately $2.6 million and $2.9, respectively.

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

As is customary in the construction business, we are required to provide surety bonds to secure our performance under construction contracts. Our ability to obtain surety bonds primarily depends upon our capitalization, working capital, past performance, management expertise and reputation and certain external factors, including the overall capacity of the surety market. Surety companies consider such factors in relationship to the amount of our backlog and their underwriting standards, which may change from time to time. 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 2017 to be similar to the $11.6 million incurred in 2016; however, the award of a project requiring significant purchases of equipment or other factors could result in increased expenditures.

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 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.

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 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.

At December 31, 2016, there was approximately $107 million of construction work to be completed on unconsolidated construction joint venture contracts, of which $53 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, 2016, 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 to the consolidated financial statements 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 our sources of market risk. Outstanding indebtedness under our Prior Credit Facility incurred interest at floating rates. There were no borrowings under this facility at December 31, 2016. As the new Equipment-based Facility does not bear interest at floating rates, we are not subject to an impact on our results of operations from a change in interest rates. However, our interest rate could increase by 2% based on our fixed charge coverage ratio as noted above in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Sources of Capital.

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.

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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, 2016. 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, 2016 to ensure that the information required to be disclosed by the Company in this Report is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms and is accumulated and communicated to the Company's management including the principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

Management’s Report on Internal Control over Financial Reporting.

The Company’s management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934). Under the supervision and with the participation of the Company’s management, including the principal executive officer and principal financial officer, the Company conducted an evaluation of the effectiveness of internal control over financial reporting at December 31, 2016. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in the 2013 Internal Control-Integrated Framework. The Company’s management has concluded that, at December 31, 2016, the Company’s internal control over financial reporting is effective based on these criteria.

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, 2016, 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 significant changes in our internal control over financial reporting occurred during the three months ended December 31, 2016, other than the inclusion of creating a management team and its outside advisors to review and challenge the various inputs to the Company’s valuation model, 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.

The information required in this item is contained in the Company's proxy statement for its Annual Meeting of Stockholders to be held on April 28, 2017 and is incorporated herein by reference. The information can be found under the following headings in the proxy statement:

Item 10 Information	**Location or Heading in the Proxy Statement**
Directors	Election of Directors (Proposal 1) Board Operations
Compliance With Section 16(a) of the Exchange Act	Stock Ownership Information
Code of Ethics	The Corporate Governance & Nominating Committee
Communication with the Board; nominations; Board and committee meetings; committees of the Board; Board leadership and risk oversight; and director compensation.	The Board of Directors

Information relating to the Company's executive officers is set forth at the end of Part I of this Report under the caption "*Executive Officers of the Registrant*" and is incorporated herein by reference.

Item 11. Executive Compensation.

The information required in this item is contained in the Company's proxy statement for its Annual Meeting of Stockholders to be held on April 28, 2017 and is incorporated herein by reference. The information can be found under the headings Executive Compensation and Board Operations in the proxy statement.

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

The information required in this item is contained in the Company's proxy statement for its Annual Meeting of Stockholders to be held on April 28, 2017 and is incorporated herein by reference.

- Equity Compensation Plan Information can be found in the proxy statement under the heading *Executive Compensation*.
- Information regarding the ownership of the Company’s common stock can be found in the proxy statement under the heading *Stock Ownership Information*.

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

The information required in this item is contained in the Company’s proxy statement for its Annual Meeting of Stockholders to be held on April 28, 2017 and is incorporated herein by reference.

- Information regarding any relationships between directors and officers and the Company can be found in the proxy statement under the heading *Transactions with Related Persons*.
- Information about director independence can be found in the proxy statement under the heading *Election of Directors (Proposal 1)*.

Item 14. Principal Accounting Fees and Services.

The information required in this item is contained in the Company’s proxy statement for its Annual Meeting of Stockholders to be held on April 28, 2017 and is incorporated herein by reference. The information can be found in the proxy statement under the heading *Information about Audit Fees and Audit Services*.

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, 2016 and 2015

Consolidated Statements of Operations for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Comprehensive Loss for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Stockholders' Equity for the years ended December 31, 2016, 2015 and 2014

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	Purchase Agreement, dated as of December 3, 2009, by and among Kip Wadsworth, Ty Wadsworth, Con Wadsworth, Tod Wadsworth and Sterling Construction Company, Inc. (incorporated by reference to Exhibit 2.1 to Sterling Construction Company, Inc.'s Current Report on Form 8-K, filed on December 3, 2009 (SEC File No. 1-31993)).
3.1	Certificate of Incorporation of Sterling Construction Company, Inc. as amended through May 2, 2016 (incorporated by reference to Exhibit 3 to Sterling Construction Company, Inc.'s Current Report on Form 8-K, filed on May 2, 2016 (SEC File No. 1-31993)).
3.2	Amended and Restated Bylaws of Sterling Construction Company, Inc. (incorporated by reference to Exhibit 3.2 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2015, filed on March 14, 2016 (SEC file No. 1-31993)).
4.1	Form of Common Stock Certificate of Sterling Construction Company, Inc. (incorporated by reference to Exhibit 4.5 to Sterling Construction Company, Inc.'s Form 8-A, filed on January 11, 2006 (SEC File No. 1-31993)).
10.1#	The Sterling Construction Company, Inc. Stock Incentive Plan as amended through May 9, 2014 (incorporated by reference to Exhibit 10.2 to Sterling Construction Company, Inc.'s. Current Report on Form 8-K, filed on May 13, 2014 (SEC File No. 1-31993)).
10.2#	Forms of Stock Option Agreement under the Oakhurst Company, Inc. 2001 Stock Incentive Plan (now known as The Sterling Construction Company, Inc. Stock Incentive Plan) (incorporated by reference to Exhibit 10.52 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2004, filed on March 29, 2005 (SEC File No. 1-31993)).
10.3	Call Option Agreement, dated as of May 29, 2015, by and among Clinton W. Myers, Clinton Charles Myers, Trustee, and Sterling Construction Company, Inc. (incorporated by reference to Exhibit 10.13 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K/A for the year ended December 31, 2015, filed on April 4, 2016 (SEC file No. 1-31993)).
10.4	Call Option Agreement, dated as of May 29, 2015, by and between Richard H. Buenting and Sterling Construction Company, Inc. (incorporated by reference to Exhibit 10.14 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K/A for the year ended December 31, 2015, filed on April 4, 2016 (SEC file No. 1-31993)).
10.5#	Standard Non-Employee Director Compensation adopted by the Board of Directors to be effective March 1, 2016 (incorporated by reference to Exhibit 10.3 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2015, filed on March 14, 2016 (SEC file No. 1-31993)).

10.6.1	Loan and Security Agreement dated as of May 29, 2015 between Nations Fund I, LLC, Nations Equipment Finance, LLC, as administrative and collateral agent, Sterling Construction Company, Inc. and its wholly-owned subsidiaries (incorporated by reference to Exhibit 10.1 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.6.2	Term Loan Promissory Note dated May 29, 2015 in the amount of $20,000,000 (incorporated by reference to Exhibit 10.2 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.6.3	Revolving Loan Promissory Note dated May 29, 2015 in the amount of $20,000,000 (incorporated by reference to Exhibit 10.3 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.6.4	Security Agreement dated as of May 29, 2015 between Nations Fund I, LLC, Nations Equipment Finance, LLC, as administrative and collateral agent, Road and Highway Builders, LLC, and Myers & Sons Construction, L.P. (incorporated by reference to Exhibit 10.4 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.6.5	Real Property Waiver dated May 29, 2015 between Nations Equipment Finance, LLC as administrative and collateral agent, and Texas Sterling Construction Co. relating to 3475 High River Road, Fort Worth Texas (incorporated by reference to Exhibit 10.5 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.6.6	Real Property Waiver dated May 29, 2015 between Nations Equipment Finance, LLC as administrative and collateral agent, and Texas Sterling Construction Co. relating to 5638 FM 1346, San Antonio, Texas (incorporated by reference to Exhibit 10.6 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.6.7	Real Property Waiver dated May 29, 2015 between Nations Equipment Finance, LLC as administrative and collateral agent and Texas Sterling Construction Co. relating to 20810 Fernbush Ln., Houston, Texas (incorporated by reference to Exhibit 10.7 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.6.8	Intercreditor Agreement dated as of May 29, 2015 among Nations Equipment Finance, LLC, as administrative and collateral agent, Nations Fund I, LLC, and Sterling Construction Company, Inc. and its wholly-owned subsidiaries (incorporated by reference to Exhibit 10.8 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on June 3, 2015 (SEC File No. 1-31993)).
10.7.1#	Employment Agreement dated as of March 17, 2006 between Sterling Construction Company, Inc. and Roger M. Barzun (incorporated by reference to Exhibit 10.11 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K/A for the year ended December 31, 2009, filed on March 18, 2010 (SEC File No. 1-31993)).
10.7.2#	Amendment dated January 18, 2012 of the Employment Agreement dated as of March 17, 2006 between Sterling Construction Company, Inc. and Roger M. Barzun (incorporated by reference to Exhibit 10.7.1 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K filed on March 17, 2014 (SEC File No. 1-31993)).
10.8#	Employment Agreement dated December 28, 2012 between Ralph L. Wadsworth Construction Company, LLC and Con L. Wadsworth (incorporated by reference to Exhibit 10.9 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K filed on March 17, 2014 (SEC File No. 1-31993)).
10.9#	Separation & Release Agreement executed on July 3, 2015 between Thomas R. Wright and Sterling Construction Company, Inc. (incorporated by reference to Exhibit 10.1 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on July 7, 2015 (SEC File No. 1-31993)).
10.10#	Employment arrangement of Ronald A. Ballschmiede (incorporated by reference to the description contained in Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on November 11, 2015 (SEC File No. 1-31993)).
10.11.1#	Program Description — 2015 Short-Term Incentive Compensation Program & 2015 Long-Term Incentive Compensation Program (incorporated by reference to Exhibit 10.1 to Sterling Construction Company, Inc.'s

Current Report on Form 8-K filed on December 17, 2014 (SEC File No. 1-31993)).

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10.11.2#	Form of Long-Term Incentive Program Award Agreement (incorporated by reference to Exhibit 10.2 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on December 17, 2014 (SEC File No. 1-31993)).
10.11.3#	Amended form of Long-Term Incentive Program Award Agreement (incorporated by reference to Exhibit 10.9.3 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K filed on March 16, 2015 (SEC File No. 1-31993)).
10.12#	Employment Agreement dated as of March 9, 2015 between Sterling Construction Company, Inc. and Paul J. Varello (incorporated by reference to Exhibit 10.10 to Sterling Construction Company, Inc.'s Annual Report on Form 10-K filed on March 16, 2015 (SEC File No. 1-31993)).
10.13.1#	Program Description — 2016 Executive Incentive Compensation Program (incorporated by reference to Exhibit 10.1 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on February 26, 2016 (SEC File No. 1-31993)).
10.13.2#	Form of 2016 Executive Incentive Compensation Program Restricted Stock Award Agreement (incorporated by reference to Exhibit 10.2 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on February 26, 2016 (SEC File No. 1-31993)).
10.13.3#	Program Description — 2017 Executive Incentive Compensation Program (incorporated by reference to Exhibit 10.1 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on February 5, 2017 (SEC File No. 1-31993)).
10.13.4#	Form of 2017 Executive Incentive Compensation Program Restricted Stock Award Agreement (incorporated by reference to Exhibit 10.2 to Sterling Construction Company, Inc.'s Current Report on Form 8-K filed on February 5, 2017 (SEC File No. 1-31993)).
21	Subsidiaries of Sterling Construction Company, Inc.:

Name	State of Incorporation or Organization
Texas Sterling Construction Co.	Delaware
Texas Sterling – Banicki, JV LLC	Texas
Road and Highway Builders, LLC	Nevada
Road and Highway Builders Inc.	Nevada
RHB Properties, LLC	Nevada
Road and Highway Builders of California, Inc.	California
Sterling Hawaii Asphalt, LLC	Hawaii
Ralph L. Wadsworth Construction Company, LLC	Utah
Ralph L. Wadsworth Construction Co. LP	California
J. Banicki Construction, Inc.	Arizona
Myers & Sons Construction, L.P.	California

23.1*	Consent of Grant Thornton LLP.
31.1*	

	Certification of Paul J. Varello, Chief Executive Officer of Sterling Construction Company, Inc.
31.2*	Certification of Ronald A. Ballschmiede, Executive Vice President & Chief Financial Officer of Sterling Construction Company, Inc.
32.1*	Certification pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350) of Paul J. Varello Chief Executive Officer, and Ronald A. Ballschmiede, Executive Vice President & Chief Financial Officer of Sterling Construction Company, Inc.
95.1*	Mine Safety Disclosure.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

Management contract or compensatory plan or arrangement.

* Filed herewith.

Item 16. Form 10-K Summary

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

Sterling Construction Company, Inc.

Date: March 9, 2017 By: /s/ Paul J. Varello
Paul J. Varello, Chief Executive Officer
(duly authorized officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	**Title**	**Date**
/s/ Milton L. Scott Milton L. Scott	Chairman of the Board of Directors	March 9, 2017
/s/ Paul J. Varello Paul J. Varello	Director Chief Executive Officer (principal executive officer)	March 9, 2017
/s/ Ronald A. Ballschmiede Ronald A. Ballschmiede	Executive Vice President & Chief Financial Officer (principal financial officer and principal accounting officer)	March 9, 2017
/s/ Marian M. Davenport Marian M. Davenport	Director	March 9, 2017
/s/Maarten D. Hemsley Maarten D. Hemsley	Director	March 9, 2017
/s/ Charles R. Patton Charles R. Patton	Director	March 9, 2017
/s/ Richard O. Schaum	Director	

March 9, 2017

Richard O. Schaum

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Sterling Construction Company, Inc.

We have audited the accompanying consolidated balance sheets of Sterling Construction Company, Inc. (a Delaware corporation) and subsidiaries (the "Company") as of December 31, 2016 and 2015 and the related consolidated statements of operations, comprehensive loss, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sterling Construction Company, Inc. and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, the Company adopted new accounting guidance in 2016 related to the presentation of deferred loan costs.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2016, based on criteria established in the 2013 *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 9, 2017 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Houston, Texas

March 9, 2017

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Sterling Construction Company, Inc.

We have audited the internal control over financial reporting of Sterling Construction Company, Inc. (a Delaware corporation) and subsidiaries (the "Company") as of December 31, 2016, based on criteria established in the 2013 *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. 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.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in the 2013 *Internal Control—Integrated Framework* issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements of the Company as of and for the year ended December 31, 2016, and our report dated March 9, 2017 expressed an unqualified opinion on those financial statements.

/s/ GRANT THORNTON LLP

Houston, Texas

March 9, 2017

STERLING CONSTRUCTION COMPANY, INC. & SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

As of December 31, 2016 and 2015

(Amounts in thousands, except share and per share data)

	2016	2015
ASSETS		
Current assets:		
Cash and cash equivalents	$42,785	$4,426
Contracts receivable, including retainage	84,132	82,112
Costs and estimated earnings in excess of billings on uncompleted contracts	32,705	26,905
Inventories	3,708	2,535
Receivables from and equity in construction joint ventures	7,130	12,930
Other current assets	5,448	6,013
Total current assets	175,908	134,921
Property and equipment, net	68,127	73,475
Goodwill	54,820	54,820
Other assets, net	2,968	2,949
Total assets	$301,823	$266,165
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$67,097	$58,959
Billings in excess of costs and estimated earnings on uncompleted contracts	64,100	30,556
Current maturities of long-term debt	3,845	4,856
Income taxes payable	78	67
Accrued compensation	5,322	5,977
Other current liabilities	6,150	3,896