



IMPROVE YOUR FINANCIAL GAME PLAN

No. 7: Game-Saving Plays – Over/Under Billing and
Bonding Reports

BY MIKE ODE

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Editor's Note: This is the seventh article in the series, "Software Feature Line-Up," by Mike Ode. Each Article focuses on must-have accounting software features. To read the previous articles, visit www.constructionbusinessowner.com.

When the game is on the line, not many coaches would send an inexperienced rookie to the plate. Similarly, project owners today are managing their risks by requiring that contractors obtain bonding. As it turns out, bonding can be good for contractors, too. Not only does a surety bond confirm the contractor's financial credibility, it may also provide construction owners with a competitive edge when bidding for new jobs.

So what's the key to meeting rigorous surety requirements? It begins with the over/under billing report, also referred to as the work in progress (WIP) schedule. Important as these reports are, not every accounting system has the ability to produce them. Contractors using generic small business software, for example, must turn to manual methods of data collection and computation, which can take hours, or even weeks, to complete. As a result, these reports are often produced—and perhaps looked at—just once each year, along with financial statements. Without the opportunity to view such reports on a regular basis, many contractors are missing valuable job data that could help them address serious issues throughout the life of a job.



AUTOMATE OVER/UNDER BILLING REPORTS

Fortunately, there exists today several accounting software packages designed specifically to meet the unique needs of the construction industry, namely over/under-billing reports. Unlike basic accounting packages that do not have the ability to store (or track) original estimates, contract amounts or change orders to estimates and contracts, sophisticated job cost accounting systems do. This enables the contractor to determine a job's percentage of completion— the basis for the over/under billing report.

Compare the processes needed to produce such reports using a generic accounting system vs. a construction specific system. Creating over/under billing reports via generic accounting software would typically require the following steps:

1. Gather numerous system and spreadsheet reports by job, including: estimates and change orders, accounts payable reports (sometimes broken down by overhead, materials and equipment), payroll reports and billing reports for the period.
2. If a job spans multiple years, calculate actual costs in prior years and revenue earned in prior years.

Despite the benefits, a lot of contractors avoid using purchase orders/ subcontracts because they think the processes are too time-consuming and cumbersome. And that is probably true if an unsophisticated or generic accounting system is being used. Most construction-specific job cost accounting systems, on the other hand, are designed to automate these processes, allowing companies to efficiently track and manage all material, supplies and subcontractor expenses.

3. Create a spreadsheet and manually enter data, job by job.
4. Determine the percent complete for each job.
5. Finally, compute the over billings and under billings for each job.

It's a complicated process, even for the smallest contractor. With a sophisticated job cost accounting system, however, the process might look more like this:

1. Having already entered timesheet data in payroll and all invoices in accounts receivable and having imported a detailed job budget, run an "over/under billing report" for each job.

It's usually that simple.

USE OVER/UNDER BILLING REPORTS FOR BETTER JOB MANAGEMENT

Better access to reporting almost always leads to better data analysis. Case in point: the over/under billing report. Instead of waiting until year-end to create over/under billing reports for financial statements and bonding purposes, financially savvy contractors are using these reports on a regular basis to stay on top of their jobs. Producing such a report on a monthly basis, for example, allows contractors to spot trends and gives them time to make changes when a job is headed for trouble.

When reviewing month-to-month over/under billings, contractors should pay attention to significant fluctuations. Over billing has its advantages, such as using the owner's capital instead of the contractor's, but it can also indicate "job borrow"—using cash from one job to fund another job. Eventually, that will bring a contractor down. Under billing, meanwhile, can lead to serious cash flow problems and should therefore prompt a thorough review of why incurred costs have not been billed. Are there unprocessed change orders out there? Is there a problem with billing practices? Is the contract owner paying promptly?

BECOME A PLAYER IN TODAY'S COMPETITIVE BIDDING MARKET

These days, a contractor's ability to acquire work is directly dependent on the company's access to surety bonds. More and more private project owners or their lenders are requiring surety bonds on their construction projects. In some cases, subcontractors with contracts as little as \$50,000 are required to obtain bonds. In the public sector, where construction money is most abundant, surety bonds are required by law as a way to protect taxpayer dollars.

The over/under billing report—a requirement of surety companies— represents just one piece in the bonding criteria puzzle. Bond producers look at many financial characteristics (such as strength of the balance sheet, financial statement presentations, history of successful projects, etc.) to determine a contractor's operating capability. Above all, they want to see a well-managed, profitable enterprise. According to a recently published surety survey, "construction companies must continue to pay strict attention to their company's financial well-being and operating performance to ensure their ability to attain bonding."

Many contractors realize having the right accounting software system is essential to attaining bonding status and building a successful company. Generic accounting systems can help companies with basic bookkeeping and accounting tasks, but they don't provide the reporting that contractors need to understand how each job affects their bottom line. To successfully manage their financial

operations—and obtain bonding— contractors are turning to accounting systems with construction-rich reporting features. It's a win-win solution.



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Foundation Software is the developer of FOUNDATION® – America's #1 Construction Accounting Software. For 30 years, we've been dedicated to giving contractors the back office tools they need to manage their job cost accounting, project management, and scheduling.

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