



IMPROVE YOUR FINANCIAL GAME PLAN

No. 6: Purchase Orders / Subcontract Management - A
Line Drive!

BY MIKE ODE

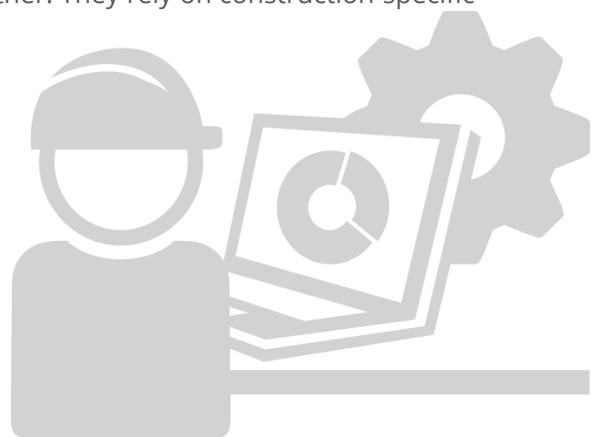
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Editor's Note: This is the sixth article in the series, "Software Feature Line-Up," by Mike Ode. Each Article focuses on must-have accounting software features.

These days, contractors must do everything they can to control their job costs. Controlling material and subcontractor expenses is especially critical because mismanagement can jeopardize both cash flow and profits. To avoid these risks, many companies use purchase order and subcontract management systems. The big hitters take it a step further. They rely on construction specific accounting systems to help streamline the processes and improve their decision-making capabilities.

Purchase orders—still considered the best accounting practice for managing the ordering of goods and services—have been around for more than 100 years. They allow companies to specify, confirm, and track every detail of an order placed with a vendor. In construction, purchase orders (and similar subcontract management systems) are even more valuable since they enable contractors to never lose sight of committed costs from the beginning to the end of a project. Efficient construction purchase order/subcontract systems provide such advantages as:



- Guarding against overpaying or double-paying invoices
- Ordering flexibility to avoid project delays
- Verifying delivery of goods
- Monitoring subcontract retainage

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.

Why Use Purchase Orders/Subcontracts?

Purchase orders/subcontracts track the costs of a project. By definition, they are the contracts that determine the sale conditions. They spell out price, delivery specifications, payment guidelines and other terms. From an accounting perspective, there are two benefits of using purchase orders/ subcontracts for construction materials and supplies:

- A purchase order/subcontract allows contractors to track the monetary, or billing, aspect of the transaction so that they can see not only committed costs, but also the remaining committed costs (expenses that are forthcoming but have not yet been billed) throughout the life of a project.
- A purchase order/subcontract creates a system for tracking the physical, or quantity, aspect of the purchase agreement so that contractors can better manage the materials/work needed for jobs or supplies held in inventory.

Tracking Committed Costs

From a monetary standpoint, purchase orders help contractors track material billings and committed costs, while subcontract management systems help them monitor billings, retainage and committed costs associated with subcontractors. Without a system in place to track these costs from start to finish, contractors run the risk of thinking a job is more profitable than it really is, overpaying suppliers or simply running out of cash.

Job cost accounting systems that offer purchase order and subcontract management features allow contractors to take advantage of these critical cost control measures without adding to their workload. For example, instead of requiring users to physically match a supplier's invoice with a filed purchase order, the software would automatically link purchase orders/ subcontracts to payable invoices to ensure a cross-check between ordering and payments. Other timesaving features include data entry default options, customizable purchase order/subcontract templates and the ability to search by vendor, job, buyer or status.

Of course, while improving purchase order efficiency is important, the real benefit of using sophisticated accounting systems always comes back to better job cost reporting. Systems that integrate purchase order and subcontract management features with accounts payable and job costing modules have the ability to produce job cost reports with committed cost details (including change order amounts, invoiced amounts, remaining committed costs and paid to date). Available at the job, cost code or cost class level, these reports help contractors catch potential budget overages before they happen. Even before a report is run, some systems have the capability of comparing purchase orders/subcontracts to the job budget to prevent or warn users if they are going to exceed their budget.

Tracking Supply Quantities

When contractors do not adequately track their material and supply purchases, they risk tying up cash that could be used elsewhere in the company or running out of supplies needed to keep jobs moving forward. Quantity control, therefore, becomes a huge need—and yet another reason why contractors turn to purchase order systems. But depending on how large a company's operations become, the system itself can lead to a lot of time-consuming work, not to mention huge paper trails.

The most realistic way for a company to track and manage its supply quantities is with the help of a sophisticated construction-accounting system. Eliminating both the guesswork and the manual work of tracking orders, these applications protect against budget-eating project delays due to supply shortages. Here's just one example: A contractor receives a shipment of supplies but is shorted 100 items by the supplier. The contractor enters the packing list into the accounting system, where it automatically ties to the original purchase order. A back-order report tells everyone (within the office and at the jobsite) how many items are currently available. The contractor can then immediately contact the supplier and determine when the next shipment will arrive.

Equally important, if the supplier attempts to bill for more items than were shipped, the system notifies the contractor that the invoice does not match the packing list.

As an added bonus, some systems integrate with an inventory module. This allows users to maintain a perpetual inventory and do away with physical counts as the only means of knowing what is on hand. Simple reports identify what is available and what is on back-order, and the system also allows for maximum and minimum reporting to help the purchase order manager stay ahead of the game.

Some of the most time-consuming office tasks within construction have to do with managing the ordering of supplies and services. Construction-specific technology is available to help streamline

these processes and provide contractors with the cost controls needed to maintain, and gain, that winning edge.



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