

# Owner's Headaches

by John Meibers

## HOW TO AVOID A CASH FLOW CRISIS

**C**ash flow has always been a top concern for contractors. But today's lower work volume, smaller margins and tighter credit standards have made it more important than ever to put solid policies and procedures in place to collect timely payments.

When a construction contract is awarded, the contractor expends a good amount of time, effort and money getting their subcontractors lined up, materials ordered and field crews in place. During this early flurry of activity, however, many contractors pay little attention to the process of getting paid. The problem is, waiting until a project is well under way to address cash flow is risky. A single job that is significantly un-paid can ruin your entire year—or even put your company out of business.

Poor cash flow doesn't need to jeopardize your livelihood. With a bit of proactive planning using the advice below, you can eliminate most blocks to receiving payment.

### Perform a Contract Review

Before signing the contract, understand exactly what you're signing. Be wary of no-lien contracts, for example, or waiving all lien rights up front. It's a good idea to add your own amendments to the contract if possible, because issues such as schedule delays and prevailing wage rate increases can affect your costs.

On some projects, retainage is flexible. But don't expect the owner or general contractor (GC) to offer you a



reduced percentage. During contract negotiations, do your best to minimize retainage by asking for a lower rate. If you are working directly with the GC, try to negotiate the same retainage percentage that the GC has with the owner. You don't want to reach the end of the project and have the GC holding 10 percent retainage on your subcontract when the owner is only holding 2 percent on the GC's contract.

If you don't understand a clause in the contract, or aren't comfortable with some of the language, consult an expert before you sign. It's an expensive endeavor to litigate contract disputes after the ink is dry!

### Identify the Four Rs of Billing

Once the contract is in place, you'll want to identify the four Rs of project billing.

1. *Right person*—Who needs to get

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your billings? Depending on the company, your key point of contact could be the project manager, office manager, controller or another employee. For expeditious payment, make sure your invoices go to the right person.

2. *Right place*—Where should you send your invoices? Mailing a progress billing to a satellite office when checks are cut from the corporate headquarters could cause a payment delay. And if e-mailed invoices are acceptable, it doesn't make sense to snail mail your

billings.

3. **Right forms**—What payment application forms and additional documents are required for the project? To ensure prompt payment, identify whether AIA or alternate billing forms are required, and always submit your invoices on the correct forms and provide any additional required documents (prevailing wage reports, waivers and so forth).
4. **Right time**—When does your billing need to be submitted? Knowing when checks are cut and how long invoices spend moving through the approval process allows you to time your billing submissions to optimize the payment lifecycle.

In addition to identifying the four Rs, take the initiative to follow-up once your invoice is sent. An invoice approval delay due to an outstanding

question can significantly affect your cash flow.

### Manage Your Receivables

Review your accounts receivable on a weekly basis and put an experienced person in charge of collections. Contractors with the best cash flow don't have to chase money that's three months past due, because they stay on top of payment delays by regularly monitoring receivables.

Put some thought into identifying the best person in your organization to manage your receivables and pursue collections. The right temperament for this task isn't meek and mild. It takes a firm and authoritative personality to successfully collect past due payments.

### Track Liens and Waivers

To protect your company when submitting a signed waiver with a draw request, be clear that you're only

releasing lien up to the amount of payment received. In addition, consider adding a footnote stating that the waiver only becomes effective upon receipt of payment.

If the project has multiple lien levels, failure to collect waivers from second tier subcontractors and suppliers could delay payment. Put a process in place for tracking these waivers and submitting timely documents, such as Notice of Furnishings statements.

### Get Retainage Released

As a project nears substantial completion, ask for partial release of retainage if the contract supports that request. If not, make it a priority to tie up loose ends. Get sign-off on unapproved change orders so you can bill for them. Complete your outstanding punch list items. And submit your as-builts and warranties.

Retainage often represents the profit for the project. Do everything

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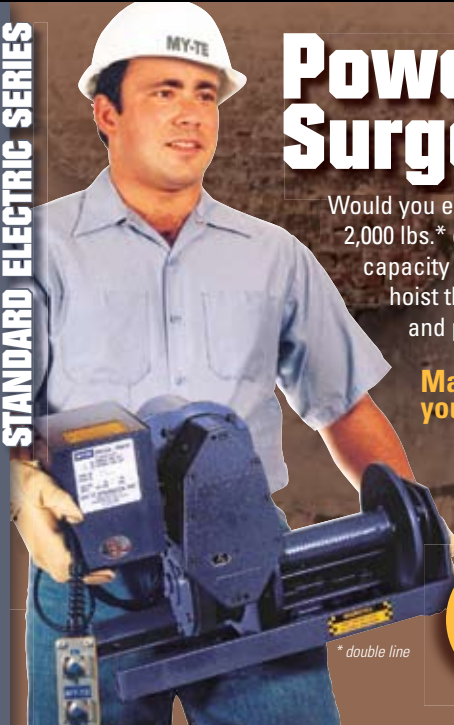
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### Evaluate Your Cash Flow Tools

Many contractors use spreadsheets to track the vital details related to cash flow. But using construction-specific technology to manage the processes discussed here allows you to automate the many steps toward payment and gain visibility into areas that need improvement.

I'm a big believer in process improvement through historical data tracking, which is difficult to do using spreadsheets. Construction software gives you the historical perspective to identify the types of jobs that drain cash flow and the owners or GCs that pay slowly. This information allows you to make decisions that lead to

better cash flow.

You may think that generic accounting software and spreadsheets get the job done—until you experience the tools available in a construction accounting program. Imagine tracking retainage to the penny, for example, and having associated notes that outline what is required for final payment. Or the ability to track and generate progress billings and lien waivers with a click of the mouse. These are just two ways that construction technology helps.

### Building Best Cash Flow Practices

Managing your business to optimize cash flow is an ever-evolving process. At the end of each job, ask yourself what you learned and what you could have done better. Then, take action to improve and refine every aspect of

your process, from contract signing to receipt of final payment.

Don't hesitate to consult a professional for advice if needed, or replace inadequate technology. The investment you make up front to establish best practices for cash flow management should yield a significant return on investment while giving you a better chance of avoiding a cash flow crisis. ■

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