

6 Tips for contractors to manage costs and mitigate financial risks

The construction industry has been experiencing cost increases, and fluctuations will likely continue. Here are six ways contractors and subcontractors can mitigate risks related to cost volatility, supply-chain issues and labor shortages.

Consider price-escalation clauses or cost-plus contracts

Price-escalation clauses have typically been limited to cost increases for materials, but they can also be used to pass rising labor costs on to customers. Customers may try to negotiate out of the clause, but the high demand for services may give contractors more leverage.

Focus on timely and accurate reporting

Timely job cost accounting and reporting can help contractors identify even minor cost increases early. Fine-tuning accounting and reporting, including reviewing job profitability and comparisons to monthly estimates, can provide valuable insights about your business and potentially make it easier to obtain financing and bonding.

Bring contract cost increases to customers as soon as possible

Raising the topic of cost increases with customers is easier when identified through timely cost allocation and revenue recognition. Once a job is done, it's much harder to get the customer to cover elevated costs. Accurate accounting and recordkeeping supported by proper documentation can help you pursue cost-escalation clauses.

Be vigilant about timely billing and collections

It's important to quickly complete documentation, contractual and legal reminders, invoicing authorizations, and billing. Proactively notify customers about potential cost increases and past-due invoices and be prepared for potential cash-flow issues in the event of collection delays.

Incentivize project managers to meet profitability goals

Project managers with a stake in profitability goals tend to be more hands-on about managing costs. They should closely review all job cost reports and quickly make course corrections or talk with management about passing on higher costs.

Consider outsourcing accounting and reporting

Accounting for construction contracts is a specialized and technical area of accounting. If current technology or staff aren't able to provide the accounting and reporting your business needs, consider engaging an accounting firm with construction expertise