The keys to successful FF&E CapEx spending

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Sound financial planning with an experienced accounting team can make FF&E and CapEx spending much easier.

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Early in my career, a client told me that if we do a great job on sourcing, purchasing and delivery of furniture, fixtures and equipment, but have issues in the accounting process, we will not be hired again.

The client didn't want to talk about pattern, color, quality, budget or schedule. Rather, during the interview process, it was all about the project closeout process: all the key elements that happen after the FF&E is delivered. The highlights of what I have learned purchasing millions of dollars of FF&E per day for hotels in 37 countries are outlined below.

Smooth project cash flow

The financial process actually starts before the first purchase order is issued, as the funding process must be discussed. It is the purchasing agent's responsibility to review and establish the project cash flow and then at minimum update it on a monthly basis or more frequently as needed. Is the project a new build with a lender and funding requests to be done by specific dates? Is it a renovation owned by a NYSE real estate investment trust or major private equity firm where all the renovation funds are available on short notice? Who are the key people needed to approve the funding requests? Is there an outside project manager or owner's representative involved?

The purchasing agent should establish a separate bank account for each project, and there should be no interest earned on the client's funds. He or she must also work with the ownership group to balance the overall timing of the funding. While no owner wants more funds drawn out than are necessary, for projects that have a funding process of 30 days or longer, we also don't want to be caught short on funds as this may cause delays in the manufacturing process.

The purchasing agent is tasked with approving all vendor invoices and ensuring that deposits paid have been accurately applied, that only allowable manufacturing overages have been billed, and—although it sounds obvious—that the correct entity has been paid. For hoteliers not used to the project accounting process, it is not always clear whether to pay the vendor, the vendor's factor, the sales organization or another entity.

Once the purchase orders are issued and deposits and balance payments are made, how are all the purchases coded to the client's general ledger? Does the client have its own specific general ledger codes for each FF&E item? What about projects with historic tax credits? The purchasing agent must work out the coding of each purchase before the purchase order is placed so that each item that is to receive a tax credit can be identified on the project financial statements as product delivers. In addition, all supporting documentation must be available to the client 24/7, as well as a summary on a monthly basis throughout the life of the project. Note that a typical FF&E project will involve hundreds of vendors and their corresponding hundreds of invoices, because each time a product ships, an invoice is generated.

Familiarity with tax issues

For projects both inside and outside the U.S., the purchasing agent must be aware of trade agreements with specific countries and duties and tariffs for both raw materials and completed goods. Also, clients should ensure the purchasing agent's procurement system is equipped to buy out a project in multiple currencies, handle applicable value-added tax and other country-specific issues.

A key item for every project in the U.S. is handling sales tax accruals. Is the nominated vendor registered to collect sales tax in the location of the project? If yes, the tax will be shown on the product invoice and paid when the vendor is paid for the product. If not, the purchasing agent must accrue that tax so that when the project is closed out there is no sudden budget shortfall to handle the accrued taxes, which on large projects can be in excess of six figures. We recently had a call from an asset manager at a REIT—the State of Illinois was auditing a hotel that we renovated four years ago. Within an hour, our team and system were able to show, invoice by invoice, whether the tax was paid with the product or whether it was accrued. The property passed the state's sales tax audit with flying colors.

An often overlooked project accounting issue in the U.S. is tax on freight. In 34 states, if the vendor is involved in routing the freight, on the vendor's own truck or on an independent carrier, the freight is taxable. If a third party is used to route the freight, the freight is not taxable and tens of thousands of dollars of the owner's money can be saved.

The “ship to” address is also important. If a project uses a warehouse in a state next to the project location, the tax rate may be based on the warehouse location, since that is considered the “final destination” by that state. And with all the states scrambling for every tax dollar, a well-thought-out comparison of total warehouse costs versus tax rate must be made. This is especially critical if the project state has zero tax and the warehouse state has a more normal 8%+ tax rate.

The same thought process must also be used when shipping fabrics from one state to another for flame or stain treatment, then to a third state to be upholstered or fabricated into a window treatment, then to a fourth state for the project location. An experienced FF&E purchasing accounting team is needed to make sure that each state receives what it is owed, if anything, and that the purchasing agent acts as a fiduciary for every penny of the owner’s capital expenditure funds.

Overall, the key to a consistent, timely (within 60 days of the last FF&E shipment) and accurate project accounting process is an upfront kickoff meeting so all parties understand their roles and the communication flow. From understanding the project’s funding requirements, handling sales tax, coding of assets, multiple currencies, duties and tariffs, to special circumstances (historic tax credits or tax-exempt status) all must be handled by a dedicated, experienced team committed to acting as the owner’s fiduciary throughout the process.

Alan Benjamin is President of Benjamin West, the global FF&E and OS&E purchasing firm, operating in 37 countries from 7 offices. Mr. Benjamin became a member of the International Society of Hospitality Consultants (ISHC) in 2000, and co-chaired the ISHC’s 2007 and 2014 CapEx studies. He’s a speaker at all the major industry conferences.