A wall and ceiling contractor, whose growth rate has ranged from 20-25% each of the last four years, is uneasy. His job cost system no longer relates, because his sales volume has grown so much.

The focus of the problem is the contractor’s job cost system, which charges all direct costs to a job. He can’t measure whether he has or has not made money until the job is completed.

In the days his volume was lower, he was on every job at least twice a week. He knew how each was progressing and had a working idea of the profitability for each job. He no longer possesses that knowledge, because higher volume makes it impossible to know that much about all his jobs.

He is uneasy, because he feels he has lost an element of control. His controller finds the situation no less frustrating. The increase in volume has made the accounting functions considerably harder. It was easier to keep track of things when the company had 10-15 jobs in progress, rather than the 40-60 now in the works.

In the high-volume atmosphere, neither the contractor nor the controller can simply poke his head around the corner and ask one of his salesmen about the coding of an invoice for a particular job. The invoice must now be routed to one of three salesmen, and if it happens to go to the wrong one, it has to be re-routed until it reaches the proper person. The firm is still getting good accounting information about its jobs, but this system takes more time and is more difficult to manage.

This contractor’s situation is not unique. Many contractors are experiencing the same pains of growth and the strain it creates on both management and the information system it uses. This contractor needs to ask himself a key question: what is his information used for? Generally, there are four uses the contractor can make of management information. They are:

• As a measuring device. Is he making a profit? How much has he spent on a job? Usually measurement has more value if it is compared to a budgeting or estimated figure, such as measuring actual job cost against the projected job costs.

• As a control device. This is management’s biggest reason for using the information. The assumption is that if you can measure events accurately, you have a sound basis to make decisions which affect the performance of a job, a profit center or the company as a whole. For instance, if you have a unit cost system and are measuring the grid suspension system and find the unit cost for the first floor is double what you estimated, you should be able to make adjustments to reduce the unit cost of the second and third floors. Using information to control activities is vital to successful management.

• As a device to produce information for government or accounting requirements. You may not be that interested in providing this information, but a fact of life is that you must meet certain requirements. This can help you if you’re turning over data you might not have obtained if you weren’t forced to provide it to someone else. One example of an information requirement with no management value is those certified payroll reports on federally funded jobs. They serve no useful purpose for management, but if you don’t produce them, you don’t do federal jobs.

• As historical information. If you know what it costs to build a particular type of system, you should be able to
make a more accurate cost estimate on any future work of a similar nature.

Assessing the Problem

Generally, the contractor has probably used his information well as a measuring device, especially on an after-the-fact basis. However, he has probably not done as well in utilizing the information as a control device or in estimating.

A good part of the problem is that he doesn’t have the unit costs. Instead, he’s probably breaking costs down by types: so much for materials, labor, scaffolding or any number of other direct costs. These costs are being charged directly to the job, instead of against various activities or phases within the job.

Since his salesmen have made their estimates based on unit costs and quantities, the non unit cost system leaves him no real feedback on the estimates, at least not on the basis they were made. Even job spot checks to evaluate quantity and labor costs won’t provide a meaningful comparison to these estimates.

The irony is that the foremen are quite capable of getting the needed production information if they’re told at the beginning of each job exactly what is wanted and how it is to be reported.

This contractor has simply reached the sufficiency of size to justify fully computerizing his operations. Given the automated EDP systems designed for contractors, he’s in a favorable position of cost-benefits. The time is right for him to make certain his field and business office will use a computerized system once it is available. His key will be making input accurate and gaining a total commitment from all of his people.

Setting Up

Obviously, once the commitment to computerization is made, there is some groundwork to be done. Commitment by his people is one element of this, but so is understanding what is sought from the computerized system.

The contractor’s major deficiency is lack of phase or activity costing, and once he gets into that, it will involve production quantities. Is he ready? Not really, at this point. Instead, labor is his key variable cost of operation. While it would be nice to initially have all other costs broken down to phases, at this point it is neither worth the time or the effort.

Instead, the contractor should decide to phase labor costs. He will need to work with his controller, and probably his CPA to design a new cost system with input from all salesmen and foremen or superintendents. The new monthly total job cost will show all of the jobs per month and job costs to date by the type of cost.

Once the design is in, the contractor should call a meeting which includes the controller, CPA, salesmen and superintendents and foremen who worked on the design. He should introduce each piece and form to be used in the system so they will be clearly understood by everyone who uses them.  

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For instance, he may use a typical weekly job cost form. It identifies the job by number, job name and by the initials of the salesman who sold it. He’ll use a master list of codes to identify the phases and activities of the individual job. Thus, in addition to a description of the activity or phase, he has a universal code identifying exactly what’s being done on the job.

The form also identifies activity in terms of workmen’s compensation insurance, which can save a bundle on insurance premiums by assigning labor cost to a particular workmen’s compensation category rather than guessing at the figure at the end of the fiscal year, when it is time to pay next year’s insurance.

The next step would be to identify a unit of measure to define each activity in its smallest measurable part. Some examples would be LF for linear feet, LS for lump sum, EA for each, and SF for square feet. This will give an accurate indication of consumption and cost of various items, and usually, it would be expressed in terms of dollars. Pennies would generally be eliminated, except in cases of unit costs and average hourly wages. This is because the system is a management tool for control, and in most cases, pennies aren’t significant for that purpose.

What He Now Knows

Now that the contractor has a workable form, he has three comparisons at work for him in calculating labor hours, labor costs, production quantity and unit cost. The first is the estimate. The second is the actual job-to-date cost for budget comparison. Finally, he has a period cost, which can be used to measure a current week’s cost against those in previous weeks.

He can now also analyze his job based on reported quantities and dollars. He can view his quantity on the basis of number of units completed versus the estimated units and dollars can now be measured on the basis of actual cost versus the estimates. Either can show a distortion if viewed separately. Even where some items don’t lend themselves to unit costing, he can use percentages for his comparison.

The breakout of average hourly labor cost is especially helpful for the salesman who made the job estimate. It might indicate a high overtime factor or show the difference in how the crews are composed. A detail report, indicating labor distribution to the job each week can be added to the report to track regular and overtime hours per person.

He can also track overruns. In cases where quantities on lump sum jobs have been estimated at a number lower than what is required to do a job, the actual overrun cost will be shown to date, unless the estimate quantity is charged. This can keep projected cost to complete from showing up as a negative number and will bring the reporting much closer to the actual status of the job.

Helping His People

Now that the contractor has achieved what he wanted, he will seek to make the system as easy as possible for his people. Using a computer-generated quantity report, foremen can now be prompted in their reporting to avoid mis-coding.

By emphasizing the importance of a prejob conference, the contractor can get the salesman and superintendent together to discuss how the job was estimated, what items are in which phase codes, and what production is expected. As time goes on, the salesman becomes fully responsible for cost control, and he’ll know how to handle exceptions. That lets the contractor step out of the immediate job picture to do other things, but gives him the elements of control he lost in his pre-computer operations.

Using the information

In implementing his new system, the contractor investigated various ways to move. In reviewing the computer systems designed for interior contractors, he decided to use the Concord System. By not loading job-to-date information into the system at startup, he avoided having incomplete information on jobs already in progress. Normally, his jobs are completed within three months, so when the job-to-date input was made, within four months after the decision to go onto computer, the company was receiving weekly labor job cost reports.

Initially, the costing system was set up to require only minor modifications to tailor the Concord programs to the exact requirements of the company. In the meantime, the contractor scheduled a review session every two weeks with

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his field management to look at job cost reports and analyze the jobs.

He quickly found the value of his job cost reports. He found labor costs too high due to a slow start up and inexperienced crew, and he made necessary adjustments. He found the unit cost too high on taping material, and within a week, the problem was resolved. When the unit cost for soffit skewed 30 percent over, he was able to determine that improved production and correcting outdated figures used in the estimate by the salesman would save future problems.

In essence, the system identified bad estimating and allowed the contractor to make up for it with good productivity in another area of the job.

Within a year, the contractor was no longer uneasy. He was sold on the new system and attributed his increase in gross profits to his ability to control costs on the job and to improve his estimating procedures.

The foremen and salesmen remained enthusiastic about the information generated by the reports. During job cost report reviews, they not only received the necessary reports, they had an opportunity to discover the “why” of job cost information. In checking invoices against the information, they were able to correct those with errors.

In all, the computer had begun to get our contractor thinking about even more improvement in his profit picture. Now that his labor costs were being brought in on target, he was ready to then address the costs of his materials. This would eliminate the false sense of profitability experienced on jobs where the labor cost was correct, but materials and equipment costs exceeded estimates.

The simple truth is that this contractor is now ready to move into a job cost reporting system that adds the unit costs of materials to the tracking of the labor cost information. But the contractor is prepared to do this, because back in the very beginning, when he set up his labor cost program and opted for the Concord System, he was aware the system includes the particular software to enable him to add programs as he needs them and his company has grown to absorb them. Eventually, he will have a complete system integrated with his general ledger, accounts payable and payroll.

His success will be guaranteed by the fact he understands the final element in a good job cost system: management’s use of it. This interior contractor will use his to control the outcome of his job. He understands that there is no point in having a sophisticated system and not using the information available for job control. In the end, he will have made a real investment in his job cost system, but he will benefit from it, because the system will produce a return on the investment.