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ACCOUNTING FOR THE SMALL SUBCONTRACTOR

By SHIRLEY JANE SCHMID, Baltimore Chapter, ASWA

The most difficult job, as an accountant for a small electrical contracting firm, is to try to get management to understand all the factors to be considered in determining job costs. In many small subcontracting firms, management consists of men who after years of experience as excellent mechanics and masters of their trade have gone into business for themselves.

Naturally, they are interested in whether they are making money or not, but they are not familiar with all the items that make up job costs. They may feel that such items as overhead are not too important, they may not like to see the job sheets "cluttered up" with a lot of "theoretical" items that tend to increase job costs. They see a certain amount of labor and material involved in each job. To these costs they want to add a percentage which they feel adequate for overhead and profit and then the insurance and taxes on the job. If the records are properly kept, they will listen to reason.

The functions, then, of an accountant in a small electrical contracting business such as I am describing, are (1) to keep an accurate record of job costs, including all costs as best he can interpret them, and (2) then to present management with a clear and succinct statement of these costs with suggestions and recommendations for future improvement.

Our method of recording job costs are comparable to those used in other types of businesses. Control accounts establish the overall job costs; then, detailed job cost sheets accumulate labor, material and overhead for each job.

Each day, material invoices received are posted directly to the individual job cost sheets and directly to the general material control account. At the end of each week, direct labor is posted from the mechanics' time cards directly to the individual job cost sheets with the indirect labor being accumulated for overhead purposes. Each week, the totals posted to each job sheet must be in agreement with the amount posted to the control accounts for that week.

Incorrect allocation of labor and material may present a problem. Although difficult to solve completely, errors can be kept at

a minimum. Workers are urged to check that the job they are allocating material and labor to is the correct one. The job foreman is usually consulted to see if proper time and material are being charged to the jobs. Each foreman likes to see his jobs make money and he will watch these items carefully as a rule. The accountant himself can keep a check by becoming familiar with each job.

Generally, materials are ordered for each job to meet special requirements. Very little inventory is carried as jobs are figured to individual specifications. It is our policy to have a small quantity of supplies in the storeroom for the mechanics' convenience.

The bookkeeper bills from the individual cost sheets weekly as the jobs are completed, or partial billings on large contracts; and at the end of each month, the total labor and material taken from the individual job cost sheets that have not yet been billed determine the inventory for the month.

Our method of allocating overhead to the individual job cost sheet is our major problem. We segregate some items that many contractors bill on a cost plus basis and on these items bill for cost only. A bill that we send out can be analyzed as follows:

Labor—cost posted to job sheet plus overhead plus profit

Material—cost posted to job sheet plus overhead plus profit

Insurance & Taxes—cost only

The amount of overhead charged to each individual job cost sheet is our "experience rate" times total labor and material cost. Over a period of years we have found that this usually amounts to 10%.

In determining the amount of insurance and taxes to be charged to each job, we use an "experience" rate based on 10% of the labor cost plus 10% of the amount of indirect (unproductive) labor or shop time or supervision that each job must bear.

This supervision is another item that we separate from overhead although we do not bill it as a separate item. This item represents the time the general management spends on looking at jobs, estimating, laying out the work to the mechanics and supervising the jobs that are in progress.

Some of this time can be charged directly to the jobs themselves, but most of it cannot. We feel that this kind of time belongs to all the jobs and each must bear part. Again we have fixed a rate, at present, 20%, of the direct labor which we charge at the end of each week to each job for supervision. We pay insurance and taxes on this indirect labor and therefore include it when determining insurance and taxes.

The rate used in determining supervision is computed at the end of each year or the following year by taking the ratio or percentage of total productive labor for the year to the total of unproductive labor. This amount could be determined weekly or even monthly, but we find the yearly rate is accurate enough.

With these figures on hand, the bookkeeper can bill accordingly. If the job is a contract job, management knows immediately how much money it has made or lost. If the job is done on a cost plus basis, the bookkeeper has a basis on which to compute the profit.

Presenting management with clear and succinct statements of the cost of doing business and making recommendations for improvements are functions of the accountant. It is not difficult to prepare routine statements similar to those prepared for most businesses. However, in our business we prepare an additional report that we have found most useful.

Job analysis sheets are made from the job cost sheets upon the completion of jobs and after receipt of full payment. These sheets carry columns for: Job, Labor Cost, Material Cost, Insurance & Taxes, Overhead, Supervision, Total Costs and Selling Price. From these sheets we can see the jobs on which we have a profit or loss. The totals of these sheets tell us as a whole whether we are making profits on the various types of jobs, and the breakdown on each sheet tells us where the gains or losses occur. The sheets are set up according to contractors or according to certain places—such as, Medical Arts Bldg.—with one miscellaneous sheet for the jobs we do for individual customers.

In addition, we can then compare the actual job cost with the cost our estimator used. If there is too much difference between the estimate of labor and material and the actual cost, the difference is noted and discussed at once and plans are made to avoid a recurrence of such an error.

Also from these analyses we single out the most profitable types of electrical work for us. We have found, for instance, that

industrial work is more profitable than house wiring so we try to obtain as many commercial jobs as possible. We have also discovered that the mechanics on our payroll are more adept at control wiring than at some other kinds. Thus, we bid often on jobs with air conditioning contractors featuring control wiring.

Finally, we can take the totals of all the costs from our job analysis sheets and compare them with the actual costs as reflected in our accounts. If the difference in percentage of our estimated costs for overhead, supervision or insurance and taxes are too great, we adjust the rate for future use, always trying and hoping to maintain as accurate job cost sheets as possible.

There are factors in the contracting business, comparable to hurricanes or other unpredictable events, that occur after a job begins and can become very serious. A case to illustrate:

When a contract has been awarded to wire a school, the electrical contractor places his order for material and fixtures that are needed, complying with architects' and engineers' specifications as much as possible (therefore low inventories). This fixture order is placed with a proper supply house and 90 days delivery is promised as the contract must be completed in 6 months. After the 90 day period, the contractor checks on the fixture order that he is about ready for. The supply house contacts the manufacturer, and they in turn reply that the entire plant has been shut down due to a flood in the area, or a strike, or fire or reasons beyond their control. The plant will remain closed for 2 more weeks, when production resumes, delivery of material cannot be made before 60 more days. Meantime, at the school project, due to the interruption of coordination between the trades, since the fixtures were unavailable, ceilings and walls will have to be torn out and replaced when they arrive—all at the electrical contractor's expense. Delivery not being made as promised in 6 months, a penalty for every day over the promised time is levied against the contractor. A substitute fixture, comparable to the one specified for the job was submitted, but the architect and engineer would not accept it and the electrical contractor was caught in a web of circumstances not of his own making.

When a contractor bids and accepts a contract for a job he is bound for performance as stated in the contract and can be

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of work. Completion is termed as such when there is a cessation of labor for a continuous period of 60 days.

A valid claim of lien must contain the following:

1. Statement of the amount of the claimant's demand after deduction of all just credits and off-sets.
2. The name of the owner or reputed owner.
3. A general statement of the kind of work done or materials furnished by the claimant.
4. The name of the person by whom the claimant was employed to perform his labor or to whom he furnished the materials.
5. A description of the property sought to be charged with the lien sufficient to identify the property.

No mistakes or errors in the statement of the demand, or of the amount of credits and offsets allowed, or of the balance asserted to be due to claimant, or in the description of the property against which the claim is filed shall invalidate the lien, unless the court finds that such mistakes or error in the statement of the demand, credits and offsets, or of the balance due was made with the intent to defraud, or the court shall find that an innocent third party without notice, direct or constructive has, since the claims were filed, become the bonafide owner of the property liened upon, and that the notice of claim was so deficient that it did not put the party upon further inquiry in any manner.

The lien is wholly invalid unless verified by the claimant or some other person in his behalf; an acknowledgment is not a verification. The lien must be recorded in the office of the County Recorder of the County in which the property or some part of the property is situated.

No lien binds any property for a longer period than 90 days unless within that time proceedings to enforce the same are commenced.

The Mechanic's Lien is preferred to any lien, mortgage, deed of trust, or other encumbrance upon the premises and buildings. The Subcontractor is entitled to recover only such amount as may be due him according to the terms of his contract after deducting all claims of other parties for work done and materials furnished for his contract.

The regular monthly aging of the accounts keeps an established time protection record on them for the filing of liens since

normal invoicing is done very promptly upon completion of labor on the job. This gives adequate time for filing of liens even if the Subcontractor's trade is the last one on the project.

When the foregoing routine is well established, the Subcontractor's cash flow is consistent; Bad Debt Account is negligible. Invoices are not returned from the General Contractor because of improper method of invoicing or incorrect percent of completion on Progress Billings, and payments are usually made by the General Contractor in his current month's operations. It is possible at any time to check Accounts Receivable per job and Contractor. Statements are more prompt, since the Accounts Receivable Ledger is current at all times. Slow Accounts are automatically tabulated, since the aging is done each month; Mechanic's Lien Rights can be used where necessary. "Work in Process" Subsidiary Ledger at all times reflects a complete picture of Job operation: Cost versus Unbilled and Billed portion of Contract, without any additional accounting, since the detail posting of the Accounts Receivable is done to this Ledger instead of the Accounts Receivable Detail Ledger. Management can readily see if percentages of Progress Billing submitted are sufficient in comparison with his cost or his investment in "Work in Process."

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held for non-performance. It is not possible to foresee such conditions as above or even to allow for same when figuring an estimate. Competition in the construction field is very keen and "break even" points are closely watched by the accountant on most of the larger projects. Possible losses from close bidding burden the jobs. Bankruptcy results from a series of underestimations on larger jobs. A contractor can absorb a few losses on smaller contracts, but one loss on a million dollar contract is very serious. We have found that our method of checking and analyzing the jobs helps avoid some of the pitfalls awaiting the small subcontractor.

A subcontracting firm may flourish without an accountant, but with one who is ready and able to use the accounting tools to keep management informed of the constant progress in the firm's affairs, it has greater potential for growth and profits.