



Mastering Construction Accounting with RealNet Accounting: Your Strategic Partner

With over 20 years of experience in accounting, RealNet Accounting is your go-to partner for navigating the financial complexities of the construction industry. We understand that construction accounting is not like traditional accounting. Managing multiple projects, each with its own budget, contracts, and compliance requirements, demands a specialized approach. That's where RealNet comes in, delivering strategic solutions tailored to construction firms.

Why Construction Accounting Requires a Different Approach?

At RealNet Accounting, we recognize that construction accounting differs significantly from regular accounting. Here's why:

1. **Project-Based Focus:** Construction accounting revolves around individual projects, each treated as its own cost center. Tracking labor, materials, and overhead on a project-by-project basis ensures that the financial picture is clear and accurate. Unlike regular accounting, which looks at departments or functions, we make sure your projects stay on budget and profitable.
2. **Precision in Job Costing:** Job costing is at the core of every construction project. Our approach ensures that every cost—from materials to labor to equipment—is allocated precisely to the right job. This level of detail helps you monitor profitability in real-time, allowing for better decision-making and project performance.
3. **Revenue Recognition:** In construction, recognizing revenue is more complex. RealNet Accounting helps implement percentage-of-completion accounting, ensuring that revenue reflects project progress. This contrasts with regular accounting, where revenue recognition methods are simpler and not project based.

4. **Compliance and Reporting:** We know construction firms face stringent compliance issues, from certified payroll to lien waivers and bonding. Our services ensure that your firm stays compliant with all local and federal regulations. Unlike general accounting, where compliance is more standardized, the construction industry requires specific attention to detail that our firm specializes in.
5. **Managing Subcontractors:** Handling subcontractor agreements, tracking payments, and managing change orders are critical to staying on track and within budget. RealNet streamlines this process to ensure that you maintain control over subcontractor relationships and performance.
6. **Strategic Cash Flow Management:** Long project timelines can make cash flow management tricky. We provide real-time cash flow projections tied to your project schedules, so you always know where your cash stands. This is essential for keeping projects moving and preventing cash shortages.

The RealNet Advantage: Strategy Meets Experience



With over two decades of experience, RealNet Accounting understands how to leverage key financial data to maximize your project's success. Here's what we bring to the table for construction firms:

- **Increased Financial Visibility:** We provide you with the financial insights needed to manage costs, track progress, and adjust courses where necessary.
- **Enhanced Financial Control:** Our detailed reporting allows for greater control over your finances, ensuring each project contributes positively to your bottom line.

- **Compliance with Confidence:** We handle construction compliance, so you don't have to worry about costly penalties.

Strategic Approach

In construction accounting, a strategic approach means going beyond just tracking income and expenses. It involves analyzing financial data to make proactive decisions that enhance profitability, manage risks, improve cash flow, and ensure project success.

Instead of just recording costs, a strategic approach would involve:

- **Forecasting** future costs based on current data to avoid overruns.
- **Optimizing cash flow** by aligning payment schedules with project milestones.
- **Ensuring compliance** by proactively managing payroll and regulatory requirements.
- **Monitoring project KPIs.** Here are some best practices to effectively monitor KPIs:

1. Define **Clear and Relevant KPIs**

Some key Operational construction KPIs include:

• Project Schedule Variance	Planned vs. Actual progress
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<ul style="list-style-type: none"> • Cost Performance Index (CPI) 	Cost efficiency of project
<ul style="list-style-type: none"> • Earned Value (EV) 	Work completed vs. budget spent
<ul style="list-style-type: none"> • Labor Productivity Rate 	Output per labor hour
<ul style="list-style-type: none"> • Safety Incidents 	Number of accidents or violations
<ul style="list-style-type: none"> • Quality Control 	Defects or rework rates

Tip: Make sure the KPIs are actionable and specific to the type of project, like residential, commercial, or infrastructure.

2. Set Baselines and **Targets**

Establish performance benchmarks before the project starts to measure actual performance against targets. Use historical data from similar projects to inform baseline estimates.

Example: For a construction company building homes, set baseline KPIs such as average construction time per home, labor cost per square foot, and a maximum defect rate of 2%.

3. Utilize Real-Time Data Collection Tools

Adopt digital tools like project management software or mobile apps that allow real-time tracking and updates of KPIs. Example: Procore helps automate reporting and visualize project status.

Tip: Integrate accounting and budgeting tools to keep financial KPIs up to date.

4. Conduct Regular **Reviews** and Updates

Schedule consistent KPI reviews—Every Monday, or Tuesday or monthly depending on project size and scope. Adjust targets as the project progresses based on real-time data and unexpected changes.

Tip: For large-scale projects, consider milestone-based reviews rather than only periodic ones.

5. Establish **Accountability**

Assign responsibility for each KPI to relevant stakeholders (project managers, site supervisors, or subcontractors). Ensure they understand how to track, interpret, and respond to KPI data.

Example: Have the project manager monitor the schedule variance, while a site supervisor tracks safety metrics.

6. Use Dashboards and Reports for **Visualization**

Use dashboards to visualize KPI trends, making it easier for teams to spot issues early. Automated reporting systems can generate insights that help track progress and inform decisions.

If you need a Dashboard to visualize your KPI, call RealNet Accounting team.

Tip: Use color-coded systems (green for on track, yellow for warning, and red for issues) to quickly interpret performance.

7. Focus on **Leading** Indicators

Leading KPIs (workforce productivity, equipment downtime, and material availability) help predict potential problems before they impact the project. Tracking these indicators helps you prevent delays or cost overruns.

8. Ensure Team **Communication**

Share KPI results transparently with all team members to ensure everyone is aligned with project goals. Open communication ensures quick responses to KPI red flags.

9. Review and Learn **Post-Project**

Conduct a post-project review to assess whether KPIs were met. Analyze areas of success and where improvements can be made for future projects.

Key Financial Performance Indicators per Project

In the construction industry, financial Key Performance Indicators (KPIs) are crucial for ensuring that projects stay on budget, are profitable, and maintain a healthy cash flow.

Below are some of the most important financial KPIs for construction projects:

1. **Gross Profit Margin**

What it measures: The percentage of revenue left after subtracting the cost of goods sold (COGS), such as labor, materials, and equipment.

Why it's important: This KPI helps you understand how much profit is made from each dollar of revenue before overhead expenses are considered. A high gross profit margin indicates efficient cost management in delivering the project.

Formula:

$$\text{Gross Profit Margin} = \frac{(\text{Revenue} - \text{COGS})}{\text{Revenue}} \times 100$$

2. **Net Profit Margin**

What it measures: The percentage of profit remaining after all expenses, including overhead, taxes, and interest, are deducted from total revenue.

Why it's important: This KPI indicates the overall profitability of the project, giving a clear picture of how well the project is performing financially.

Formula:

$$\text{Net Profit Margin} = \frac{(\text{Net Income})}{\text{Revenue}} \times 100$$

3. Cash Flow

What it measures: The amount of cash moving in and out of the project over a given period.

Why it's important: Positive cash flow ensures that the project has enough liquidity to pay bills, wages, and suppliers on time, reducing the need for external financing.

Tip: Track both operating cash flow (cash generated from project activities) and net cash flow (total cash after all activities).

Want examples? Visit [Resources | RealNet Accounting LLC](#)

4. Cost Variance (CV)

What it measures: The difference between the budgeted cost and the actual cost of a project at any given point.

Why it's important: Cost variance helps project managers identify whether the project is over or under budget, enabling adjustments before significant financial issues arise.

- Formula:

$$\text{Cost Variance} = \text{Budgeted Cost} - \text{Actual Cost}$$

5. Schedule Variance (SV)

What it measures: The difference between the planned value of the work that should have been completed and the actual value of work completed.

Why it's important: A delay in the schedule can lead to increased costs due to overtime, penalties, or extended use of equipment and labor. Monitoring this ensures timely completion of the project.

- Formula:

$$\text{Schedule Variance} = \text{Earned Value} - \text{Planned Value}$$

6. Working Capital

What it measures: The liquidity available to meet short-term obligations, calculated as the difference between current assets and current liabilities.

Why it's important: Adequate working capital ensures that the company can cover day-to-day operations without financial strain.

- Formula:

$$\text{Working Capital} = \text{Current Assets} - \text{Current Liabilities}$$

7. Cost Performance Index (CPI)

What it measures: The cost efficiency of the project by comparing the earned value (EV) to the actual cost (AC).

Why it's important: A CPI greater than 1 indicates the project is under budget, while a CPI less than 1 signals that it's over budget.

- Formula:

$$\text{CPI} = \frac{\text{Earned Value (EV)}}{\text{Actual Cost (AC)}}$$

8. Return on Investment (ROI)

What it measures: The profitability of a project in relation to the costs invested in it.

Why it's important: ROI helps assess whether the financial benefits of the project outweigh the costs, giving a snapshot of overall project success.

- Formula:

$$\text{ROI} = \frac{\text{Net Profit}}{\text{Total Investment}} \times 100$$

9. Change Order Impact

What it measures: The financial effect of change orders on the project's budget and schedule.

Why it's important: Change orders can dramatically impact costs and timelines. Tracking how much they add to the budget or delay the schedule helps keep the project profitable.

Tip: Keep a close eye on the frequency and financial impact of change orders to avoid excessive cost overruns.

10. Committed Costs

What it measures: Costs that have been committed to but not yet incurred, such as purchase orders or subcontractor agreements.

Why it's important: Committed costs help anticipate future cash outflows, giving a more accurate picture of the financial health of the project.

Tip: Monitor committed costs to ensure they do not exceed the project's budget allocations.

11. Overhead Costs

What it measures: The indirect costs that aren't directly tied to a specific project but are necessary for running the business (e.g., office expenses, administration, utilities).

Why it's important: Keeping overhead costs in check ensures profitability, as excessive overhead can eat into project profits.

Tip: Regularly review overhead allocation to ensure it aligns with project scale and duration.

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CASH FLOW Details:

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Best Practices for Managing Cash Flow in Construction:

1. Accurate Cash Flow Forecasting

- Tip: Regularly update your cash flow forecast throughout the project. Include all expected payments, material purchases, labor costs, and overhead.
- Best Practice: Use historical data from previous projects to predict future cash needs and account for seasonal variations in construction work (example: weather-related slowdowns, new regulations).

2. Track Expenses and Receivables in Real-Time

- Tip: Use accounting software like QuickBooks or Sage to track expenses and payments daily.
- Best Practice: Automate invoicing to ensure clients are billed on time. Use integrated systems that track both project progress and invoicing, so you're billing as milestones are met.

3. Negotiate Payment Terms Favorably

- Tip: Structure payment schedules to receive cash before making large expenditures. For example, negotiate to receive a deposit or payment in stages (mobilization, project milestones).
- Best Practice: Push for shorter payment cycles (maybe 30 days) from clients and offer small incentives for early payment. This ensures you have cash on hand for ongoing expenses.

4. Manage Overhead Costs Efficiently

- Tip: Track fixed and variable overhead costs separately. Identify areas where you can cut costs (example: leasing vs. purchasing equipment).
- Best Practice: Set limits on project overhead costs (administrative expenses, rent, and utilities) and monitor regularly. Keep these costs proportionate to the project's size and revenue.

5. Project Profitability

- Tip: Regularly compare actual project costs against the project budget.
- Best Practice: Adjust cash flow projections as soon as cost overruns or delays are identified, and act quickly to either negotiate more favorable terms or reduce spending.

6. Establish an Emergency Fund or Line of Credit.

- Tip: Set aside a portion of profits as a contingency fund to cover unexpected expenses or project delays.

- Best Practice: Plan for cash shortages by maintaining access to a line of credit or reserve funds, especially for large or long-term projects. Avoid using Credit cards with high interest rates that will eat up your profit.

CHANGE ORDERS Issues:

Best Practices for Handling Change Orders:

1. Establish Clear Contract Terms for Change Orders

- Tip: Ensure the contract clearly defines what constitutes a change order, how it will be processed, and the timeline for approvals.
- Best Practice: Always include clauses in contracts that outline how change orders are to be submitted, approved, and paid. This prevents disputes and delays.

2. Require Written Approvals Before Starting Work

- Tip: Never begin work on a change order without written approval from the client.

Best Practice: Create a standard change order form that includes a description of the change, associated costs, and how it will affect the project's schedule. Use digital signatures to streamline approvals

3. Track Change Orders in Real-Time

- Tip: Use construction management software to document change orders as they happen.
- Best Practice: Have a centralized process for submitting and approving change orders. This ensures transparency and tracks how they affect timelines and budgets.

4. Price Change Orders Fairly and Quickly

- Tip: Price out change orders as soon as they are requested to avoid delays and disputes later.
- Best Practice: Include both labor time and material costs in change orders (you don't need to breakdown line by line), and update cash flow projections accordingly. Be proactive by notifying clients immediately if the change significantly impacts the timeline or budget.

5. Communicate the Impact of Change Orders

- Tip: Always provide clients with updated project timelines and financial forecasts once a change order is approved.
- Best Practice: Use change orders as an opportunity to reset expectations. Document how the change order will affect the project and keep all stakeholders informed.

6. Review Change Orders Regularly

- Tip: At regular intervals (suggestion: every Tuesday at the regular meeting), review all outstanding change orders to ensure nothing is overlooked.

- **Best Practice:** Build in a buffer for change orders in your project budget, especially for larger or more complex projects. This reduces the financial strain caused by frequent changes.

5 Tips to improve Cash Flow & Change Orders:

1. **Create a Cash Flow Calendar:** Map out your expected payments and receivables to know exactly when cash will be available.
2. **Keep Detailed Records:** For both cash flow and change orders, document everything. Use cloud storage to back up all contracts, invoices, and approvals.
3. **Stay Proactive:** Anticipate cash shortfalls or potential change orders by staying in regular contact with clients, subcontractors, and suppliers.
4. **Integrate Systems:** Use integrated construction and accounting software to streamline both cash flow monitoring and change order processing.
5. **Communicate Frequently:** Keep your team and clients informed about the financial and timeline impact of change orders or cash flow issues.

Take Control of Your Construction Finances Today

At RealNet Accounting, we are committed to helping construction firms gain the financial clarity they need to thrive. Let our 20 years of experience work for you, providing the strategic accounting

solutions that drive project profitability, ensure compliance, and streamline operations. Call us today!

Download this document and learn how RealNet Accounting can help your firm master the unique challenges of the construction industry.