How to Use Construction Accounting

to Protect Your Company

Accounting Can Mitigate Risk and Help Recession-Proof the Business

Part 02

Introduction

For most construction companies, the accounting department is seen simply as a box the company has to check. These folks balance the books and make sure the bills get paid, but they're rarely leveraged to their full potential.

You see, the accounting department is in a unique position. CFOs and top staff, with the right mindset, are able to see further down the financial road than other team members. They know where the company is and where it's heading, keeping a keen eye out for unnecessary risk. They also have the ability and knowledge to quickly identify regulatory issues and assess potential projects' financial viability.

In short, the accounting department could be full of real leaders who can help bring a company forward.

But they can only usher in that growth if they're empowered by the board and other decision-makers. Until now, that's been a tough goal to reach. But in this e-book, we'll mention some key actions that accounting personnel can take to earn the right to be part of the tough decisions, as they're often the folks best suited for the job.

To help us explain these concepts, we tapped some of the top accounting experts in the country to ask for their advice. Whether you're a CEO, a board member, a CFO, or a new accountant, these tips will help you push your company to its fullest potential.

We've divided this guide into three sections – you are reading Part 2.

To find the other two, or to download the entire guide, check out our Turbo-Charged Accounting resource center.

Identifying Risk

One of the greatest skills that the average accountant has is the ability to identify and assess risk. The construction industry is rife with them, and accounting pros who know how to mitigate them while still rolling the dice on profitable projects can steer their companies toward significant growth. Here's what you need to know.

How Construction Accounting Can **Be More Strategic and Mitigate Risk**

Let's be real. One of the accounting department's greatest skill sets is its ability to assess risk and avoid it. Construction accounting personnel are generally risk-averse despite working alongside the adventurers who push construction projects forward.

But, too often, construction accounting takes a backseat to the rest of the company. Rather than just balancing books and ensuring that payroll goes out, the accounting department could be more proactive and lean into what it does best: recognize and mitigate risks.

Construction Accounting Strategy and Risk Mitigation

We wanted to know what accounting departments could do to improve their companies' outlooks, especially in these wild times of high-interest rates and labor shortages. To get our answers, we tapped some of the top experts in leading accounting firms throughout the country. We spoke to experts from FORVIS, RSM US, and Crowe LLP.

These experts graciously answered our questions, provided insights, and gave opinions about the outlook of construction and its accounting function, as well as some advice for taking a more proactive role in today's construction industry. Here's what we found.

Nick Grandy,
RSM CPA

Increase Cash Reconciliation Frequency

One way that accounting divisions can be more proactive in reducing risk is to increase the frequency of cash reconciliation. Nick Grandy of RSM suggests that companies reconcile cash balances quickly every day. He says that companies should quickly check the balances, compare them against yesterday's amount, and look for any potential discrepancies to avoid fraud and take action.

Grandy told us:

"If your checking numbers are out there and somebody's printing checks and you don't have a positive pay solution set up, [daily reconciliation will] help you catch that earlier in the cycle. And if you catch it earlier, hopefully, you can take action to prevent either further issues or to help mitigate that risk.

Improve Forecasting (and Use It!)

Cash Flow forecasting is critical to making the best decisions with the money you have on hand and the money you expect to get in. It's important to have a true grasp of how it all works to avoid the risks associated with unpaid subcontractors and high-interest credit lines.

Grandy suggests using ERP software to create a rolling forecast that reaches at least 13 weeks out. This will allow companies to analyze when their invoices are typically paid by project owners or general contractors.

If they know their invoices are usually paid 93 days out with a particular project owner, they can better account for the subcontractor invoices that roll in every 30 to 60 days throughout the 13 weeks and potentially avoid lines of credit or contractor liens.

Promote the Right Projects

Choosing the right projects can go a long way to reducing risk, and the accounting department is in a prime position to educate the rest of the board. For example, the projects the government is funding through money earmarked by legislation are largely unaffected by high-interest rates or materials costs. These are reliable projects that are sure to come to fruition.

According to Grandy, "The government's not going to typically cancel a highway project because interest rates are up or material prices are up. The highway still needs to be built, so we're going to go build it."

Brent Kirkpatrick of Crowe LLP says, "That's government money that is earmarked, it's going to be spent, it already is being spent. If you look at the industries that are projected to grow the most in the next four to five years, it's the road builders, the heavy highway, heavy civil type projects."

Kirkpatrick also added that data centers will continue to be a big push, and potential safe projects for CFOs to lobby for: "15 years ago, we didn't view fiber optics in data as maybe infrastructure, but the reality is today, it's infrastructure."

Not every contracting firm has the ability to dive into roadbuilding or data center projects, but taking note of where safe money is being spent is a great way for accounting firms to reduce risk.

Start Succession Planning

There are few things as risky as uncertainty, and unfortunately, the construction industry is full of it. People will be retiring from the industry in droves over the next few years, and that can cause concern for not only the actual labor force but also the executives and back office team members who make sure to keep the fires burning.

Internally, it's a good idea for the accounting department to start preparing for the future. But it's more than simply choosing the next longest-tenured employee. The brightest minds leaving universities today want to work for cutting-edge companies that employ AI and the latest technology. If the accounting department is stodgy and stuck in the same ways for 40 years, the industry will hardly have a chance at attracting these young people, perpetuating the problem for another generation and creating long-term risks companies can't afford.

Understand State Border-Crossing Taxes

The largest and potentially most lucrative projects currently underway have a serious problem. According to Kirkpatrick, the manpower required to build them simply does not exist. This means that companies from all over the country will be able to backfill local labor forces, sending crews into other states for extended periods of time.

This creates a tax risk that only construction accounting firms are equipped to handle.

“If a contractor who’s not based in Ohio, for example, is working on the [Ohio] Intel site and they are bringing workers in from all over the US to make sure they have the right team on staff, those people are going to be in Ohio for a significant amount of time. There’s going to be some sort of payroll tax and income tax ramification to those workers that the accounting team would 100% need to be on top of,” according to Kirkpatrick.

His suggestion? Investing the $400 to $500 that the CFMA’s guide to state and local taxes cost to help the accounting department better understand payroll for these employees.

Promote Service-Based and Recurring Revenue Projects

Another practical option for reducing risk is to implement serviced-based divisions and recurring revenue or subscription-based services. Whether it's a repair division, seasonal services, restoration emergency services, or even home inspections, these divisions diversify revenue streams, providing cash flow stability and seasonal balance.

This also makes the company more attractive to private equity investors. According to Mike Trammel of FORVIS, "They're getting into construction not because they love construction risk, but because they want recurring revenue."

Trammell also added, "Private equity tends to place a greater value on that because that's recurring billing. You probably don't need to work very hard to win that client and win that work, and there probably isn't a huge amount of risk. So that work tends to be more favorable."

Lean on Technology for Real-Time Data

Looking forward is helpful, but sometimes, the best decisions (and least risky) are made with the data we have right now. Real-time data helps companies understand exactly what's going on in the moment, and it can only be truly real-time with the use of technology.

Jamie Tancos of FORVIS told us that real-time data can help fix mistakes as well as avoid them. She says, "You need to right the ship because this job's going to go south if you don't or you're bidding way too skinny, or whatever the case. " She continued, "We've got this other job here that's exactly like what we're bidding right now, and it was a catastrophe and this is why."

Having that data on hand, whether it's through an ERP or a CRM, creates a "lessons learned library, " as Jamie described it. That's something that can only be achieved with technology that stretches far beyond the capabilities of Excel, helping contractors avoid major risks.

Also, legal risks associated with contract language can also be avoided with technology (to a degree). Brent Kirkpatrick told us that Crowe LLP is rolling out software, Pro Contract Manager for Construction, that uses AI to read and dissect contracts, comparing them to industry and company standards to ensure everything is assessed for risk. While this might be outside the realm of the accounting division, it could be a tool that the division uses to better understand what contracts entail.

Jamie Tancos,
FORVIS

Streamline Your Tech Stack

As new technologies and software come along, construction companies tend to gather them into a tangled mess of implementation. Kathryn Schneider of FORVIS believes this is an area where accounting divisions can help mitigate risk by simplifying the tech stack.

“I think another common theme moving forward is how do I reduce my tech stack? I'm now on a best of suite or best of platform and now take advantage of cloud and APIs to just really minimize that burden and the risk of having a very disconnected technology stack, ” Schneider says. “So, that's another risk mitigation strategy that I see contractors taking. Let me get out of this best-of-breed world and find a common platform that we can all make everyone happy on.”

Accounting divisions and CFOs should advocate for modern ERPs, CRMs, cloud tech, and APIs that fully integrate with one another. Data can be shared across these platforms without duplication and re-entry, reducing the margin for error and creating better, more complete data sets that companies can actually use the way they were intended.

But, just peeling back the layers of the old software and data systems can be convoluted, too. It involves complicated software subscriptions, license keys, and data reconciliation to make happen—all risks in their own right.

Consider Cash Reserve Investment

Instead of mitigating risks, construction accounting divisions may have a chance to make a calculated one—investing.

Many construction companies are sitting on large cash reserves as they're waiting for delayed projects to start. But the benefit of this high-interest world we're living in is that short-term investment vehicles are turning 5% yields, and construction accounting divisions may want to suggest these investments.

Brent Kirkpatrick tells us, "It's been forever since you could get 5% on a CD, a short-term duration investment vehicle, or making sure you're using some treasury ladders. You can do short duration 3-, 6-, 9-, 11-month treasury ladders to earn 5, 6% on your balance." He continued, "Nothing's a hundred percent risk-free, but fairly high risk-free returns on to help maybe weather some of these short lulls that they may have with projects being pushed."

And no one in a construction division is better-suited to spearhead this move than the accounting division.

Advocate for SDI

Finally, construction accounting divisions should be advocating for general contractors to carry SDI policies. Subcontractor Default Insurance protects the prime contractor against subcontractors failing to hold up their contractual obligations.

Brent Kirkpatrick tells us why SDI insurance is necessary: “Subcontractors right now are finding it tougher and tougher.” He adds, “They’ve taken on a lot of work, probably more work than they should have in a lot of cases. And so I think a lot of subs are actually struggling right now to get work done and get it done with high quality and to meet schedules.”

Accounting Firms Can Step Up and Take on a New Role

We mentioned that accounting personnel are typically good at recognizing and mitigating risk. With the approaches mentioned in this article, construction accounting divisions can step up into a stronger, more influential role at their companies while also reducing the chances of risks impacting the bottom line. And there's no one better suited for the job.

Find more tools to help you be a change-maker in your company at the Turbo-Charged Accounting Resource Center.

Recession-Proofing Your Business

If you plan on making a real career out of the construction industry, you're going to deal with your fair share of recessions. These economic downturns are cyclical, occurring every 5 to 10 years. But if you build your business wisely and prepare for these challenges, you can recession-proof your business to withstand times when money is more expensive, projects are harder to find, and other companies are closing their doors. Here's how.

Let's not dispute whether or not a recession is coming—the ifs and buts about it aren't worth the time. What we know, however, is that recessions come along once every 5 to 10 years. They're hardly the Halley's Comet of economic events, so it makes sense to prepare for a recession regardless of whether one is lurking around the corner in the near future or not.

Recessions happen. They're part of the economic cycle. Recession-proofing your business just ensures you're prepared for the next one, regardless of when it happens. This guide will explain some of the best ways to shore up your bottom line in the event of a recession.

Why You Need to Recession-Proof Your Business

Recession-proofing your construction business isn't doomsday prepping or shuttling your executive board into a bunker. It's a solid business practice that ensures your company is structurally sound any time the broader economy takes a few steps back.

Recessions typically last 12 to 24 months, and typically include a bear market in stocks. In the U.S., only the National Bureau of Economic Research (NBER) can call a recession—and only in hindsight. Prior to the short-lived Covid recession in Q2 of 2020, The Great Recession was our most recent "normal" recession, beginning at the end of 2007 and continuing through mid-2009 (though the impacts on the construction industry have lasted much longer). Many industries were impacted, but construction especially took a brutal blow. The housing market collapsed, demand for new construction projects flattened, and finding financing became a needle-in-a-very-crowded-haystack situation.

A report from the NAHB stated that the number of residential builders alone dropped 50% from 2007 to 2012.

Housing still hasn't fully recovered, despite the ongoing demand and persistent supply shortages that have underlined the current growth in home prices. And while the impact of The Great Recession is something of an outlier—its was wider-reaching than most other recessions, from a historical perspective—it's still a cautionary tale from recent history, and there are still reverberations throughout the industry. Companies need to protect their bottom lines and not forget that the right combination of circumstances can become a tinderbox that can burn unprepared construction companies to the ground. Preparing for these situations is the best way to survive them.

7 Keys to Recession-Proofing Your Business

Many companies think that the only practical response to a recession is cutting costs and praying for the best. But rather than the reactive approach, prepare for a potential recession and minimize its impact on your business with the following tips.

01 Assess Your Financials

You have to understand how much money is going out each month before you can put a plan together for recession-proofing your business. Sit down with your accountant or team and discuss everything from accounts payable to overhead to incidental costs and other expenses you pay out each month. The goal is to identify where the money is going and how much of it is leaving.

The time to find and plug the holes is when business is good, when it's "extra cash" and not blood money. Being proactive now about any unnecessary spending or expenses ensures that the company can save money and also survive reduced cash flow for longer. Waiting until there isn't enough money to make payroll is simply too late.

02 Build Cash Stores

It might not seem like rocket science, but there's actually a lot of value to unpack from this tip.

Building up your cash stores is one of the best ways to prepare for an economic downturn. Companies with a healthy stockpile will be able to weather situations better than those relying on credit and loans to get through. Cash is almost always a safer bet than the expensive interest rate-bearing loans available in recessions.

But cash isn't just for keeping the lights on and funding projects. Recessions can also present incredible investment opportunities. Whether it's purchasing another company, buying equipment at a reduced rate, or even providing short-term funding to other contractors, cash can make it happen.

The trick about building cash stores, however, is being proactive about cash flow. Contractors need to stay on top of their accounts receivable, minimize frivolous spending, and set a goal to save each month. It's important to have a proactive but realistic plan for saving.

03 Diversify Your Customer Base

Construction companies that put too many eggs in too few customer baskets rarely do well during a recession. Even companies with a finely-tuned recession game plan will lose customers during a downturn. Whether it's because of financing drying up or because companies are simply going out of business, some will fail.

The key to ensuring that losing one customer doesn't crush business is having a portfolio of other customers to work with. Increase your outreach and marketing efforts, and encourage salespeople with additional incentives for landing a certain amount of new clients each month. This allows you to continue serving your current customers while still expanding your reach.

04 Focus on a Backlog, but Don't Bank on It

A company's backlog can be a sign of its health during strong times, but it can be a false sense of security during downturns. Backlogs can quickly dry up, with projects being canceled or put on pause until money is cheaper. For this reason, it's important to focus on your backlog, but don't take it for granted.

Try to keep your sales funnel as full as possible. This is easier said than done, but starting new outreach campaigns, expanding your service area, and offering new services can help attract more clients, keeping the sales funnel and backlog brimming. Don't rest on your laurels, though. Concerted sales efforts are still critical to keeping the backlog full enough.

05 Add Recurring Revenue Models

Recurring revenue is all the rage now, and it could be a key component to making it through a recession. Construction companies that start repair or service arms with subscription-based fees that keep the money rolling in each month will have an easier time maintaining positive cash flow when things get difficult.

Some business models to consider include:

- **Repair services:** Clients pay monthly for access to a repair team whenever they need them.
- **Emergency services:** Businesses pay each month to have a trusted team on call for emergencies.
- **Property maintenance services:** Monthly subscription payments entitle the property owner to a set amount of days for clean-up.

Companies will receive small payments from these customers each month in exchange for a service. The recurring revenue increases the company's valuation, builds customer relationships, improves cash flow, and allows companies to retain workers they might otherwise consider letting go during tough times. Plus, upselling additional services to existing subscription customers is relatively straightforward and doesn't require a robust sales team.

06 Rely on Data

Every decision made during a recession is more critical than those made in boon times. Companies need to make better decisions with more certainty because more is on the line, and recovering from a stumble is a lot harder in a recession. The best way to make great decisions is by relying on real, up-to-date data.

Companies that utilize modern project management software can make the most of the available data. These programs provide customers with overviews of project statuses, available resources, budgets, timelines, and more. Most are cloud-based, so when changes are made, the entire system reflects the change across as many line items or contracts as necessary.

These programs can also generate valuable reports instantly. When big decisions are on the table and teams need real-time data, they'll have instant access to the latest information, allowing them to make the best decision possible.

07 Choose the Right Projects

If there's one area where companies can improve their chances of growth and success ahead of a recession, it's project selection. Choosing the right projects with the best clients and the safest funding stabilizes the backlog and allows companies to breathe, even when others are closing their doors.

First, go where the money is. Today, that would mean focusing on projects like data centers, chip manufacturing plants, EV battery and manufacturing plants, and similar projects funded by the CHIPS Act and Inflation Reduction Act. Also, infrastructure projects funded by the Infrastructure Investment and Jobs Act should also be considered safer than private projects. The government has earmarked billions of dollars to fund these programs, making them a better bet in the long run.

Also, be selective about your clients. Reviewing data regarding payment and credit history allows companies to determine how risky a potential partnership could be. If a customer has a history of defaulting, canceling projects, or not paying its contractors, they're worth avoiding in good times, let alone when things are getting difficult.

Start Your Recession-Proofing Before You Need It

It's not a matter of if a recession happens, but when. These challenging times are cyclical and we're never more than a few years removed or away from one. Construction companies need to make hay while the sun shines rather than taking positive cash flow and lengthy backlogs for granted. The tips mentioned above will help companies narrow their focus to surviving these challenging times so they can grow at a time when others are struggling to survive.
Get started recession-proofing your business today.

Conclusion

The tips we discussed can help your internal accounting experts move toward becoming vital members of the decision-making team. They'll be able to bring better insight, better risk assessment, and a better financial outlook to the table than anyone else on the team—and that's where their value really lies.

But it takes more than reading these tips to get the job done. CFOs and accounting staff have to put these ideas into action.

Trimble's suite of tools and software can also be the catalyst to getting there faster. If you're interested in changing the way you interact with your project management team, executive board, and other company decision-makers, let Trimble show you how we can help.

Find more tools to help you be a change-maker in your company at the Turbo-Charged Accounting Resource Center.