

SETTING UP QuickBooks Pro FOR CONSTRUCTION

QuickBooks was originally developed as a general, small-business accounting package. It was only after large numbers of construction companies began using the software that Intuit upgraded the

by Judith Miller

A step-by-step guide to getting this popular accounting software up and running

program to include basic job-costing features, and called it QuickBooks Pro (QBP). Setting up the software has always required rudimentary understanding of general accounting principles, but setting up the latest release (version 5) to take full advantage of job-cost reporting can be frustrating, especially for new users.

Part of the confusion stems from the fact that QBP uses two very different methods — one called *Items*, the other *Classes* — to organize data for job-cost reports.

Each method has its strengths and weaknesses. Which method you choose will depend on how much detail you want to track and on the kind of reports you want to generate (see “*Items vs. Classes*”).

If set up correctly, QBP v.5 provides all the necessary tax information you'll need, two standard accounting reports — a balance sheet and an income statement — plus a Job-Cost Estimate to Actual report. QBP will produce many other reports, but these three are most important to construction companies. In this article, I'll help you steer clear of trouble by presenting a step-by-step tour of the

QBP setup procedure that will enable you to produce these three reports. Because time is your greatest investment in working with QBP, I suggest you read this entire article before you sit at the computer to begin the setup.

The Easy Step Interview

After installing QBP on your hard disk, the first setup screen instructs you to *select New from the File Menu*, which brings up the *Easy Step Interview* (see Figure 1). The *Easy Step Interview (ESI)* is a series of questions about your chart of accounts, customers and jobs, and vendors and employees. In what follows, I'll walk you through those parts of the interview where the choice I recommend is different from the QBP default. Remember that you can always change your answers later; if making a change will be particularly difficult, the program will warn you with a large yellow triangle symbol.

Welcome

To get started, click the *General* tab, click *Welcome*, and select *No, I'm not upgrading*, even if you already use QuickBooks.

QuickBooks. It's easier to start with a clean slate.

Company Info

The second tab is where you enter *Company Info*. When you're asked to *Select your type of business*, highlight *Construction/contracting*. Under the next heading, *QuickBooks and your industry*, you can view or print a report that will tell you more about Intuit's point of view on setting up QBP for construction. Although some of my recommendations will differ from those in this report, reading the report now is optional. Click *Next*, and the program creates your data subdirectory using the company name you entered.

When you're asked about *Your income and expense accounts*, click on *No, I'd like to create my own*. The chart of accounts for construction provided by QBP mingles direct job costs, such as building materials, with overhead, such as office supplies. Reliable gross profit margin reports can't be produced from this arrangement, so you need to create your own chart of accounts. (I'll show you how later.)

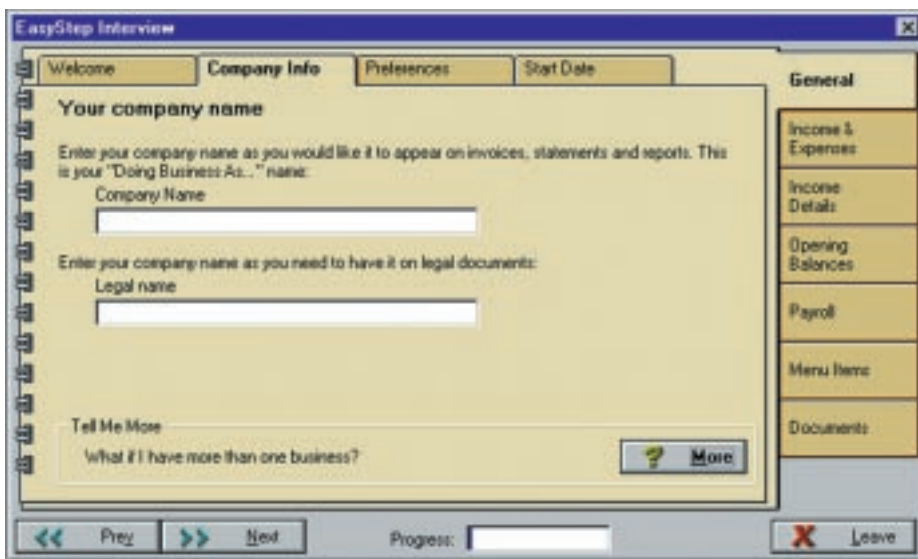


Figure 1. The Easy Step Interview is the best way to set up QuickBooks Pro initially, because its question-answer format ensures that all necessary information is entered. Changes can be made later, however, using drop-down menus.

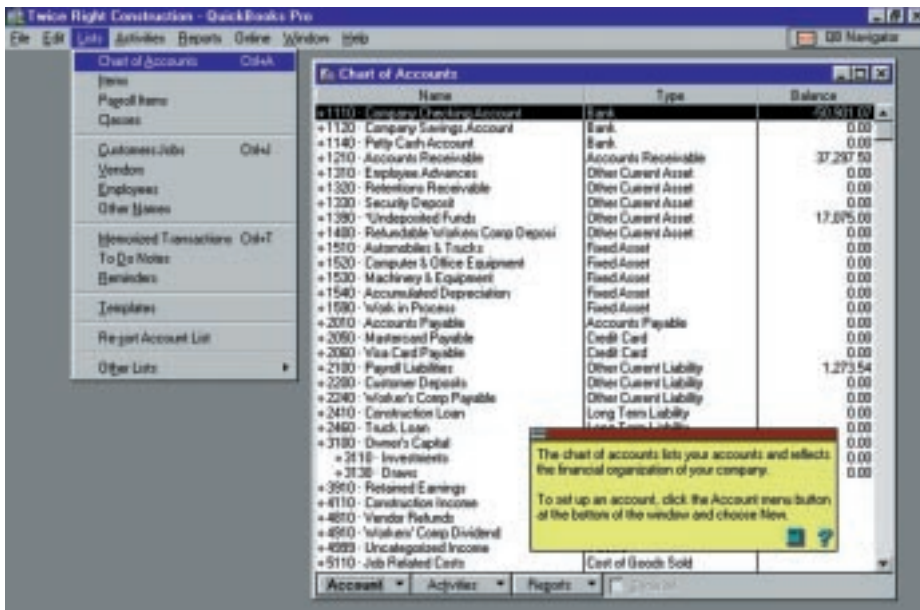


Figure 2. The author recommends using the *Lists* menu to set up your own chart of accounts instead of accepting the one provided with the software. This involves leaving the *Easy Step Interview*, but you can return later to complete it.

Preferences

From the *Preferences* tab, you will establish how the desktop looks and make choices that affect how the program treats your company. When you're asked *How many employees do you have on your payroll?* enter the correct number only if you will be using the QBP Payroll feature, and click *Yes* under *Using QuickBooks Pro for Payroll*. The Payroll feature provides burdened labor reports, including

employer payroll taxes, workers comp, health benefits, and small tool allocation.

Estimates. Your decision to use *Items* or *Classes* affects the choices you make under the *Estimates* heading. If you have decided to use *Classes*, click *No*. If you have decided to use *Items*, click *Yes*, and at the *Progress Invoicing* screen, click *Yes* again when asked *Do you ever issue more than one invoice for one estimate?* Using *Items* will enable you to produce simple

invoices based on job progress.

Transactions. Under *Classifying Transactions*, choose *Yes*. Whether you use *Items* or *Classes*, you will have to classify your transactions if you want to produce job-cost and other reports.

Bills & payments. Your choices under *Two ways to handle bills and payments* don't significantly affect the reports you will be able to get. Which way you handle bills and payments, however, depends entirely on whether you select accrual or cash-based reporting. To get the most up-to-date reporting, use accrual accounting, and choose *Enter the bills first*. (Before you answer the question about billing and payments, read the next section on accrual and cash reporting.)

Accrual vs. cash. The choice you make under *Accrual- or cash-based reporting* is crucial to the accuracy of your financial reports. If you choose cash reporting, you will be able to delay recording expenses until you actually write the check; similarly, you will not record income until the money is deposited in the bank. Cash reports are simple to produce, but they miss any outstanding material and subcontractor bills you might owe on a job, as well as any payments due from clients.

If you choose accrual reporting, you will be required to enter expenses when they are incurred, regardless of when you pay them; income must be recorded when the invoice is sent, regardless of when payment is received. Accrual reporting gets tricky at tax time, because you may have to pay tax on income that you have not yet received. But accrual reporting gives you a much more accurate picture of your company's finances, because the money you owe and the money owed to you are both accounted for.

Fortunately, QBP gives you the best of both worlds. Small companies can use accrual reporting for ongoing financial statements, but switch to cash reporting at year end for tax purposes.

Start Date

The last tab on the *General* screen asks for a *Start Date*. If possible, begin your company as of the first day of your fiscal

Items vs. Classes

QBP provides two ways, *Items* and *Classes*, to organize the data that goes into job-cost reports. Before deciding which to use, review this list of the advantages and disadvantages of each.

Remember, though, that whichever method you use, you must maintain consistent office procedures to ensure that income and expenses are assigned to the proper accounts, and that data from one job are not mixed with data from another.

Items:

- 10 variables in setup
- Attached to specific accounts
- Data entry flow: Item to Job to Class

Items take longer to set up because each Item must be assigned initially to a financial account and account type. This ensures that data are consistently posted to the proper account, but it makes setup more complex and makes it more difficult to change an Item later. Classes are not linked to accounts until the data are entered, so Classes are much easier to set up and change.

After setup, however, Item data entry is easier and more accurate, because selecting an Item automatically links the data to the proper financial and job-cost account. By contrast, during data entry for Classes, accounts may be assigned incorrectly or inconsistently from one job or invoice to the next.

With Items, financial reports are simple to produce, but lack detail because there is only one Income and one Expense account. With Classes, financial reports provide greater detail, but accuracy will suffer unless you employ strict office procedures to make sure accounts are assigned consistently. Items produce more detailed job-cost reports, however, than Classes.

Classes:

- 2 variables in setup
- Can be assigned to any account during data entry
- Data entry flow: Accounting to Job to Class

Items:

- Produce estimate summaries
- Produce progress billing

Neither Items nor Classes can be used to produce a detailed estimate — you will have to do this by hand or with a spreadsheet or dedicated estimating software. Items can, however, be assigned a subtotal from an estimate, which makes it possible to produce an invoice keyed to job progress simply by entering a percent complete for each Item.

Classes work with “budgets,” not “estimates,” but budgets are tied to a monthly calendar and provide no way to create an invoice based on job progress. Plus, you have to enter budgets as negative amounts to counteract the positive amounts you post to financial accounts.

Classes:

- Cannot produce estimates
- Cannot produce progress billing

Items:

- 9 Standard reports

Using Items gives you access to more standard reports than does using Classes. Unlike Items, Classes cannot be used to track time unless you set up a Service Item type. Doing so, however, would create two sets of overlapping lists that relate to the same information, and using the program would become more complicated and confusing.

Classes:

- 6 Standard reports

year; otherwise, begin with a new quarter. QBP explains the choices and the results.

Chart of Accounts

Because earlier you answered *No, I'd like to create my own* when asked about *Your Income & Expenses*, the next step is to click *Leave* to exit the *ESI*. We will return to the *ESI* later to set up *Customers: Jobs* and *Vendors*.

To set up a chart of accounts, go to the

Lists menu and click on *Chart of Accounts* (Figure 2). This is where you will create all of the various “shoe boxes” into which your expenses and income will be grouped. QBP controls financial reports using the account type you assign to each account. Account types define the order of individual accounts according to a rigid standard called Generally Accepted Accounting Principles (GAAP).

To make financial reports easier to

read, use uppercase for main headings, and lowercase for subaccounts. Use a simple alpha/numeric system that follows GAAP (see “Sample Chart of Accounts”). To avoid mistakes, draw up a working chart of accounts in advance and have your accountant review it. Make any changes on the working version before making entries into QBP.

Direct expenses. Pay particular attention to the account type *Cost of Goods*

Sample Chart of Accounts for Construction

Use this sample chart of accounts as a guide to designing your own, then have it reviewed by an accountant before making entries in QuickBooks Pro. Note that the only difference between the version used with Items and

that used with Classes is that the latter has sub-accounts under income account 400 – CONSTRUCTION INCOME and under expense account 500 – DIRECT JOB COSTS (see inset).

Account Name and Number	Type
100 - BANK ACCOUNTS	Bank
Bank One - Checking	
Petty Cash	
120 - ACCOUNTS RECEIVABLE	Accounts Receivable
125 - PAYROLL ADVANCES	Other Current
130 - WORK IN PROGRESS	Other Current
140 - PREPAID ASSETS	Other Current
G/L Deposits	
Security Deposit	
Workers Comp Deposit	
150 - FIXED ASSETS	Fixed Asset
Vehicles	
Office Equipment	
Tools & Equipment	
200 - ACCOUNTS PAYABLE	Accounts Payable
210 - CREDIT CARDS PAYABLE	Credit Card
American Express	
220 - PAYROLL TAX LIABILITIES	Other Current
FICA/FIT Payable	
SIT/SDI Payable	
State Unemployment Payable	
FUTA Payable	
230 - OTHER PAYROLL LIABILITY	Other Current
Employee Benefits Payable	
G/L Insurance Payable	
Workers Compensation Payable	
250 - LOANS PAYABLE	Long Term Liability
300 - EQUITY	Equity
Paid in Capital	
Add'l Paid in Capital	
Owner's Drawing	
310 - RETAINED EARNINGS	Equity
400 - CONSTRUCTION INCOME	Income
440 - OTHER INCOME	Income
500 - DIRECT JOB COSTS	Cost of Goods

Account Name and Number	Type
600 - OVERHEAD EXPENSE	Expense
Advertising	
Bank Charges	
Communications Expense	
Depreciation Expense	
Dues, Subscriptions & Trading	
Interest Expense	
Office Supplies	
Professional Fees	
Rent	
Repair & Maintenance	
Small Tools	
Tax & License	
Travel & Entertainment	
Utilities	
Vehicle	

Alternate accounts for use with Classes

400 - CONSTRUCTION INCOME	Income
Other Misc. Income	
Remodel Income	
Change Orders	
New Construction Income	
Change Orders	
T&M Income	
500 - DIRECT JOB COSTS	Cost of Goods
Direct Labor	
G/L Insurance	
D/L Benefits	
D/L PR Taxes	
D/L Workers Comp Insurance	
Other Direct Expense	
Equipment rental	
Subcontractors	
Materials	
Officer Wages	Expense

Sold (COGS). It is essential to accurately reporting of gross profit margin that this account type be used only for direct costs. Select account type *Cost of Goods Sold* and set up one account called “500 - DIRECT JOB COSTS” — use uppercase, because this is a main heading (Figure 3). If you decide to use Items, this will be your only COGS account; if you decide to use Classes, you will need to set up subaccounts for material, subcontracts, equipment, and other direct

expenses.

Overhead. Choose *Expense* from the account type list and name the main account “600 - OVERHEAD EXPENSE.” Create sub-accounts for all overhead expenses, listed alphabetically under the main account and assigned *Expense* types.

Don’t enter any beginning balances now. Later on, I’ll tell you how to enter these amounts using a *Journal Entry*.

Job Cost Setup

Next, we will set up the job codes QBP will use to compare estimated costs to actual costs. Stay in the Lists menu, and enter either *Items* or *Classes*.

Items. If you decided to use *Items* for job-costing, setup the QBP *Item* codes to match the work codes you use when you prepare an estimate. Many builders use the Construction Specifications Institute’s 16-division system; others use HomeTech’s 27 categories. Whatever

system you use, be consistent and concise.

Like the accounts in the chart of accounts, *Items* are ordered by type. Always select the type *Service* so that every *Item* will appear in the payroll time sheet. Ignore other *Item* types, because they will only complicate your setup, data entry, and reporting. Assign each *Item* a number; enter main headings in uppercase and sub-items in lowercase.

Click on *This service is performed by a subcontractor*. (This will allow you to track subcontractor hours and to include on employee time sheets any hours your crew spends doing work normally performed by a sub.) Two windows will open in the *Item* setup, one for expenses and the other for income (Figure 4). For the expense account, enter the 500 - DIRECT JOB COSTS account you set up previously in the chart of accounts; for the income account, enter "400 - CONSTRUCTION INCOME." To simplify the use of *Items*, these will be your only income and expense accounts.

Click *Next* to maintain the layout for subsequent entries. Later, after you've set up *Vendors*, you can come back to enter your most commonly used vendor in the *Preferred Vendor* field for each *Item*.

Classes. If you decided to use *Classes* for job-costing, set them up to match your estimating work codes. Again, use the alpha/numeric system to name and organize the *Classes*.

Even if you have decided to use *Classes*, you must enter a few *Items* so you can produce invoices for your customers. For example, if you typically invoice three times during a job, your *Items* might be *Draw 1*, *Draw 2*, and *Draw 3* (Figure 5). For these *Items*, do not click on *This service is performed by a subcontractor*, and enter only "400 - CONSTRUCTION INCOME" in the account field.

Back to the Easy-Step Interview

Now that you've set up the two most important lists — a chart of accounts for financial information and *Items* or *Classes* for job-cost information — you

Figure 3. Whether you use *Items* or *Classes*, set up an account labeled "500 - DIRECT JOB COSTS" and assign it the account type *Cost of Goods Sold*. If you use *Items*, this account will hold all direct costs; if you use *Classes*, setup subaccounts to hold amounts for different kinds of direct costs (materials, subcontracts, equipment, etc.)

Figure 4. To simplify the way QuickBooks Pro operates with *Items*, create only one income account (400 - CONSTRUCTION INCOME) and one expense account (500 - DIRECT JOB COSTS).

can go back and finish the *Easy Step Interview*. (You can either leave the *Lists* window open or hit the Escape key to close it.) From the *File* menu, click on *Easy Step Interview*, then click on the *Opening Balances* tab.

Customers:Jobs. Click on the tab *Customers*. The first screen asks *Do you have any customers who owed you money on your start date to add?* Click *Yes*. On the *Customer* job tracking screen, click *Yes* when asked *Do you want to track jobs (projects) for any of your customers?* On the next screen, for each customer name you enter, click *has multiple jobs*. These

choices will allow you to use QBP to track separate individual projects for the same client. A year after you do a kitchen for the Smith family, for example, you may build a deck for them. Answering *Yes* here will allow those two jobs to be set up separately.

Click on *Next*, and enter current job information, including beginning balances (payments owed to you) for each job. When you've done this for all customers, proof these balances by viewing the *A/R Reports/Customer Balance Summary* under the *Reports* menu.

Vendors. At the tab for *Vendors*, enter

Figure 5. The *Classes* method of tracking job-cost data does not include the ability to create invoices. You can, however, create a few *Items* specifically for this purpose, even when using *Classes*. This screen shows an *Item* called “Draw 1” being set up as a subaccount of 400 - CONSTRUCTION INCOME.

Account	Debit	Credit	Memo	Name	Class
1110 - Company Check					

Figure 6. To make it easier to double-check beginning balances, enter amounts as *Journal* entries instead of during setup of the chart of accounts. Labeling each entry “BB-1” (for “Beginning Balance #1”) or something similar will keep the amounts separate from other *Journal* entries and make them easier to proof.

all suppliers, subcontractors, and any individuals who are paid on a regular basis and who require a 1099. Enter opening balances (in this case, amounts you owe), and proof the balances by viewing *A/P Reports/Vendor Balance Summary* under the Reports menu.

Accounts. Because you set up the chart of accounts earlier, you can skip this portion of the *ESI*. If you’re confused about something in the chart of accounts, however, you can review the definitions contained in the *Accounts* section by clicking on *Next*, and reading the definitions and *Tell Me More* screens.

Payroll. Standard payroll setup is simple in the *ESI*. Click through the questions and QBP will do the work.

Budgets. Click the *Activities* tab on *Menu Items*. When you are asked *Do you want to use QuickBooks to help with budgeting?* click *Yes*. This will enable you to

assign estimated costs to a budget for job-cost reports for both *Classes* and *Items*. You will also be able to assign budgets for business plan reports.

Documents. To complete the *ESI*, click through *Documents*, the last tab on the *ESI* menu. Remember that you can go back into the *ESI* at any time to change your responses. But once your system is up and running, you will probably prefer to use the *Preferences*, *Lists*, and *Activities* menus to make changes.

Final Steps

Only two more sections remain before you can begin entering your transactions: beginning balances and customizing lists.

Beginning balances. QBP suggests that you enter balances when you enter the chart of accounts. I recommend, however, that you enter beginning bal-

ances as a journal entry. This will provide a complete audit trail for your entries, and will also allow you to proof the transaction so that you can enter your Retained Earnings manually instead of having the program calculate it for you.

To enter beginning balances, click *Activities* on the menu bar at the top of the screen, then click on *Make Journal Entry*. (Any beginning balances previously entered for *Customers:Jobs* and *Vendors* will already be in the corresponding A/R and A/P accounts.) In the date field, enter your start date. For *Entry No.* enter something like “BB-1,” which is my shorthand for “Beginning Balances Entry #1” (Figure 6). Doing it this way will keep your beginning balance entry separate from other journal entries.

Now enter the amounts from your balance sheet as of your start date. If you start at year end, you will enter only assets, liabilities, and equity; if you start in the middle of your fiscal year, you will need to enter income and expense balances to date as well.

Customizing lists. If you want to be able to generate reports about specific kinds of jobs or customers, you’ll have to enter several different *types* for customers and jobs. In the *Other Lists* option on the menu bar at the top of the screen, use *Customer Types*, such as “commercial” or “residential,” to represent your typical client; use *Job Types* to classify specific kinds of projects, such as “kitchen” or “bath.” Use *Other Names* for one-time payees to whom checks are written directly and whose payment does not go through Accounts Payable Bills or Credit Cards. Assign *Vendor Types*, such as “M-Lumber” to designate a lumber materials supplier, or “S-Plumbing” to designate a plumbing sub.

QBP is now set up and ready to roll. In future articles, I’ll show you how to enter data, print reports, and enter payroll. 

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