



Construction Labor Costs

101

How to Calculate and
Manage Construction
Labor Costs

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Construction Labor Costs 101

When it comes to job costing, the most apparent construction project expense to calculate (aside from materials) is labor. Like material pricing, labor costs have been on a dramatic uptick. Some businesses have reported that they're spending the same amount of money for site maintenance workers as they are for seasoned professionals. With almost half of project expenses going to labor (sometimes upwards of 50 to 60%), a clear and accurate picture of your labor costs is crucial to maximizing productivity and future revenue.

However, labor costs are about more than just hourly and salary rates, and with a sustainable method for managing them, it's much easier to bid profitably and avoid overrun.

By implementing reliable processes and tools for managing labor costs, construction firms can:

- Achieve sustainable growth
- Master compliance and regulation
- Submit profitable and competitive bids



This guide will show you how to accurately calculate labor costs (regardless of the size or style of the project) and includes tips, strategies, and tool recommendations that take the guesswork out of labor cost analysis, estimation, and management.



What to Include with Construction Labor Costs Calculations

Operating a construction company contains many moving parts, all of which are made more challenging by restrictive regulations and taxation demands. To make compliance management more accurate and consistent, you must clearly understand labor costs' three main categories.



Direct Labor Costs are the most straightforward expenses, encompassing:

- The wages and salaries you pay workers directly
- The benefits and insurance policies woven into workers' hourly or salaried rates
- The inevitable overtime, and premium pay, necessary to keep projects on schedule



Indirect Labor Costs are tertiary costs in the form of:

- Payroll taxes and workers' compensation
- Training and development
- Travel and per diem expenses



Overhead Costs are sometimes overlooked when calculating labor costs, but they're integral to having a true grasp on cost. They include:

- Administrative and management salaries.
- Equipment and facility costs.
- Technology and software expenses.



4 Common Challenges in Managing Labor Costs in Construction

Tracking labor costs is complicated enough in any industry, but there are variables (many unique to this industry) that add a lot of extra work, result in many additional expenses, and create unnecessary headaches for your team.

1. Inaccurate Time Tracking

One of the most problematic and expensive issues is the use of inaccurate timesheets. A single construction company juggles multiple job sites at any given time, so the same employee or subcontractor (and the equipment/tools they use) could visit multiple sites per day. If the employee is particularly busy (and let's be honest, there's a reason construction is as mentally exhausting as it is physically), they may:

- Forget to log their time at all, only realizing it once they get a paycheck that needs correcting
- Forget to turn in their timesheet, especially if they're dealing with old-fashioned paper
- Add the wrong times or wrong job codes to the timesheet

All of these issues can lead to your payroll specialist spending extra hours correcting mistakes and chasing down missing timesheets when processing weekly payroll (leading to them manually entering timesheets, trying to get approval, depositing or mailing out checks, etc.)



2. Labor Shortages and High Turnover

Across the board, business owners everywhere are struggling to hire and keep skilled workers. With the cost of living escalating at a steady click, workers need higher wages to compensate. This problem increases the labor costs of construction businesses trying to stay competitive both as employers and service providers.

The U.S. Bureau of Statistics revealed that private construction workers' salaries and wages have increased by 20% since 2018. But why?



3. Compliance with Labor Laws

One of the construction industry's biggest barriers to entry is the strict (and continuously evolving) compliance restrictions. These play an especially large role in labor cost management because many of these laws are directly tied to variables like:

- OSHA (Occupational Health and Safety Administration).
- Adhering to Union Agreements.
- Wage laws (such as—but not limited to—the Davis-Bacon Act).

This means it isn't just about getting the most out of every dollar. Accuracy, consistency, and organization are crucial to avoiding fees or civil suits. For example, in 2023, the IRS uncovered more than \$4 MILLION worth of cases in civil employment tax penalties, which equaled penalty payments (nationally) exceeding \$1.5 billion.



4. Project Complexity and Variability

With the US construction industry alone reaching over \$2 BILLION in 2023, the average construction company juggles multiple projects on any given day. Each of these projects requires specific skill sets, equipment, and workers to complete. Add the near inevitability of adjusting to changes in project scope and timelines, and keeping track of labor costs becomes an even greater hurdle without the right tools and approach.

Because there are fewer qualified professionals to go around, construction businesses have to pay more for workers. They also struggle to get workers to show up consistently. This complication causes disruptions in project timelines due to fewer hands on-deck, and when new hires are brought on board, the projects can take longer due to their lack of experience.



How to Calculate Construction Labor Costs

Calculating labor costs accurately is essential for construction companies to maintain profitability and keep projects on budget.

Here's a step-by-step guide to help you calculate labor costs effectively:

1. Determine the Hourly Wage

Start by identifying the hourly wage of each worker or crew member. This includes both base wages and any fringe benefits like health insurance, retirement contributions, or paid time off.

For example, if a worker earns \$25 per hour and receives \$5 per hour in benefits, their total hourly wage is \$30.

2. Calculate Labor Burden

Next, calculate the labor burden, which includes additional costs like payroll taxes, workers' compensation, and insurance. Labor burden typically ranges from 20% to 40% of the total hourly wage.

Formula:

Hourly Wage x Labor Burden % = Labor Burden
For instance, if the labor burden is 30% and the hourly wage is \$30, the labor burden adds \$9.

3. Add Overtime

If workers exceed standard working hours, include overtime pay. Overtime is usually 1.5 times the regular wage.

For example, if a worker earns \$30 per hour, their overtime rate would be \$45.

Make sure to track and include any overtime hours worked to ensure labor cost calculations are accurate.

4. Factor in Productivity Rates

Not all workers operate at the same productivity level. Consider how much work each employee can complete in a given time. This is called the productivity rate.

For example, if an employee takes 8 hours to complete a task that's expected to take 6 hours, the labor cost increases due to lower productivity.

5. Calculate Total Labor Cost per Employee

Now, you can calculate the total labor cost per employee by summing the hourly wage, labor burden, and any overtime or productivity adjustments.

Formula:

$$\text{(Hourly Wage + Labor Burden + Overtime Adjustment)}$$
$$\times$$
$$\text{Hours Worked}$$

$$= \text{Total Labor Cost per Employee}$$

7. Review and Adjust Regularly

Labor costs can fluctuate due to changes in wages, overtime, or labor laws. Regularly review and adjust your calculations to ensure accuracy. By following these steps, you can accurately calculate labor costs, which is essential for managing project budgets and ensuring profitability.

6. Estimate Labor for the Entire Project

Once you know the labor cost per employee, multiply it by the total number of employees and hours worked over the entire project to estimate the total labor cost.

For example, if 10 workers are on-site for 40 hours a week for 4 weeks, multiply their individual costs by the total hours.



Pro Tip: Using software to track hours worked, productivity, and payroll data can simplify this process and help avoid errors, keeping your labor costs in check.



Top Tips to Managing Labor Costs Long-Term

IBISWorld reports that, as of 2023, there are over 3.9 Million Construction businesses in the US (growing by 3.4% since 2022). To position your construction business for growth, adaptability, and with an eye to the future, try the following practices that can help you achieve consistent growth and competitive advantage:



Continuous Monitoring and Improvement

Even if you put a solid labor cost management system in place, it's not a "one-and-done" solution. Regularly audit labor cost data and monitor performance metrics so you can adjust strategies based on project outcomes and feedback. By doing this, your business can act proactively, which means more financial flexibility.

- Define core values that your company culture can build upon, and make sure everyone on the team keeps them in mind to ensure consistent messaging and execution.
- Clearly and consistently communicate expectations, goals, and appreciation for everyone's contribution.
- Work with your Human Resources Manager to prioritize diversity and inclusion, so everyone on your team feels valued, welcome, and confident in what they bring to your organization.
- Enforce clear policies on conduct to ensure everyone not only feels safe at work but also feels safe in bringing an issue up to their supervisor if one arises.



Building a Sustainable Workforce

Businesses across the spectrum are struggling with hiring and retention, so it's crucial to prioritize employee satisfaction and engagement. Here are a few strategies that you can use to nurture a positive work culture:



Providing Training and Development Resources

No matter what route you choose for your labor cost management, it's important to support your team with training and professional development opportunities. Continuous education and upskilling promote productivity and confidence to keep you at the forefront of industry developments and regulation.



Leveraging Technology and Automation

While the construction industry is synonymous with hard-working, human hands, it's also one of the first places technological innovation influences. But that isn't just regarding "in the field" tech (like drones, mobile tablets—or even augmented reality (AR) tools for development).



Staying Updated with Industry Trends

Regardless of how large (or how many) teams you're leading, it can be easy to only focus on immediate priorities and deadlines. However, one of the best ways to stay competitive is by staying ahead of what's happening in your industry.

From monitoring changes in labor laws and regulations to watching for innovations in machinery and technology, keeping your finger on the pulse keeps you ahead of the game.

Your back office benefits greatly from advances in automation and digitization because they save countless hours of labor, practically eliminate the risk of human error, and optimize the accounting process for accuracy and compliance. Regardless of the size of your construction business, integrating payroll and project management systems can boost productivity and drive revenue.



Industry Best Practices for Effective Labor Cost Management

Many construction businesses approach labor cost management (and a majority of their administrative processes) manually.

\$5 for Each HR Manual Tasks

To illustrate this point, a Clutch report revealed a staggering 25% of small businesses still use old-fashioned pen and paper to track their finances — and that adds up quickly. According to an Ernst & Young study, each "by-hand" HR task (like payroll entry) costs US businesses almost \$5.

However, one of the biggest problems with manual data entry is the risk of human error. And, frankly, calling it a risk may be an understatement as it's more so an inevitability.

Daily Data Entry Errors

According to a 2024 Gartner survey, 18% of accountants admit to making data-entry (financial) errors on a daily basis, while nearly 60% knew they'd made multiple errors per month. And that's just the mistakes they caught.

Essential Automation

One of the most valuable ROI strategies you can implement to improve and reduce labor costs is automation software



Why Automation is Essential



Helps Audit Current Processes

Work with your team to understand exactly how your current processes function — and the biggest issues they cause. By doing this, you can identify the areas that need the most immediate attention and find software specifically designed to solve them.



Optimizes Scheduling

The right technology can help you analyze and streamline your scheduling process, making sure everyone is exactly where they need to be when they need to be there. Streamlining your scheduling processes can help avoid overlaps that could mean less productivity or unnecessary overtime costs.



Makes It Easier to Log Time from Anywhere

Making time sheets easy and accessible on mobile devices makes it simpler for workers to log their time, and automation helps keep things organized by accurately connecting the entered hours under the appropriate job code.



Keeps Critical Information in One Place

Digitizing the process and centralizing it on one platform makes it exponentially faster to process payroll, keep bookkeeping clean, and make getting approval a breeze.

Even if the initial cost of a digital time tracking system may seem high, the money it saves (via time and resources saved) yields an undeniable ROI almost immediately.

That doesn't even include the boost to morale with peace of mind, less stress, and a more pleasant working experience.



How To Find the Right Time Tracking Software for Construction

Even if you're ready for automation to improve labor cost management, not just any tool will do. Construction demands key features because of:

- Intensive compliance regulations
- Complex job site juggling
- The many types of labor involved (W2 employees, subcontractors, or even your friend's nephew looking to make some quick cash)

Here's what construction companies should look for in time tracking and payroll software:

- **Industry-specific tools:** The construction industry's intense regulations and complicated job coding make it critical to choose software built by construction professionals for construction professionals.
- **A comprehensive suite of tools:** The time tracking system you choose should be all-in-one. Whether it be job coding and time tracking, document scanning, or even workflow automation, it should be able to handle all aspects of your time-tracking flow.
- **User-friendly and easy to implement:** Everyone on your team should feel confident using the tool. It should also offer a reliable and attentive customer support experience.
- **Seamless integration:** Even if you aren't handling everything manually, the right payroll software should seamlessly integrate and complement any current ERP software (like Sage, Autodesk, or CMiC) you have. For example, hh2 back-office cloud platform unifies your stack and helps eliminate information silos and bottlenecks.
- **Real-time data synchronization:** Executing accurate payroll and managing labor costs depends on having up-to-date data, so your software needs to offer real-time analytics for accurate labor tracking.

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A Comparison of the Top Tools and Resources for Labor Cost Management

With an oversaturated market, varying product reviews, and trying to figure out what tools are going to help you grow versus those that are just eating away at your bottom line, it can be tough to choose a tool to help. Rest assured, the following list shares some of the top-rated construction labor management and payroll software we believe are worth investigating.



QuickBooks Time

One of the most established digital accounting software options around, QuickBooks Time is a great solution for construction companies already using and enjoying QuickBooks. With a variety of plan options, users can take advantage of everything from basic tracking features (like the timecard app) to advanced tools like geofencing and expense tracking.



Buddy Punch

iOS, Android, and web compatible, Buddy Punch optimizes scheduling, payroll processing, time tracking, and beyond. Its portability makes it great for clocking in and out on the go. While it doesn't offer a free trial, its price point is very affordable.



Clockify

For those who aren't ready to make large upfront investments, Clockify is an excellent solution. Free for unlimited users, user-friendly, and offering convenient features like PTO management and GPS tracking, it also integrates with accounting and productivity apps like QuickBooks and Trello.



hh2's Time Tracking

hh2 cloud-based construction platform was built by contractors for contractors. Powering over 3,500 construction sites, hh2 connects the field and office seamlessly, eliminating the frustration and costly errors associated with manual payroll. Fast and flexible, it captures, codes, routes, and approves time without complicated spreadsheets and messy paperwork.



The ROI of Labor Cost Management Solutions

With a short list of software solutions to investigate and the top features to look for, we'll close out this deep dive with a summary of the ROI that labor cost management software yields:

- **Enhanced budget control and cost management.** The first, and most obvious, benefit of accurate labor tracking is the improved clarity and control over costs, which makes it easier for your projects to stay on budget.
- **Invaluable software integration.** Integrating labor tracking software centralizes all labor tracking data into one digital location, creating the most accurate picture of your financial status on each project.
- **Better able to maintain compliance with enhanced accuracy.** Aside from making the most out of every dollar, accurate labor tracking protects your business when it comes to compliance and regulation (such as observing labor laws, union agreements, and safety regulations).
- **Avoid cost overruns with real-time monitoring.** When you have reliable labor tracking processes in place, you can monitor how costs are adding up. Doing this gives you a better chance of preventing cost overruns and finding ways to save on future products.
- **Improved scheduling:** Labor tracking also gives more insight into how each job is progressing, enabling you to more effectively schedule timelines to make sure your resources and employees aren't spread too thin.
- **Increased productivity due to reduced idle time.** Labor tracking helps decrease idle time because it's much easier to allocate equipment and workforce numbers effectively. A digital platform makes it easier for job site managers to update asset availability, regardless of their location or time, so your team always has up-to-date information.



There's never a wrong time to optimize any component of your back-end processes. From payroll and job costing to field reporting and enhancing the interconnectivity of your current stack, every step you take toward efficiency means more revenue in your pocket — and less stress on your team.

Master Your Construction Labor Costs with hh2

*Want more information on the top construction payroll software built **for**
construction business owners **by** construction business owners?*

**Book your demo today to speak with one of our experts to find out how
hh2 can help you master your construction labor cost management.**

BOOK NOW!