

Labor Burden & Profits – Part I: What Do Your Employees Really Cost?

Whether you're a contractor, supplier, remodeler, builder, service provider, consultant, or other business professional, if you have employees, you owe it to yourself to understand exactly what each person on your payroll really costs, and how he or she can make an appropriate contribution to your bottom line.



We all know that employees are an expensive, but necessary, component of doing business. We count on them to deliver an honest day's work for an honest day's pay, and if they are "direct labor" employees, we try to charge our clients appropriately so that we can make a profit on the services that they deliver. In the case of staff employees, we may not be able to directly charge for their time, but we still expect excellent service and value in return for their compensation.

Employee payroll, and employee-related costs, comprise an extremely large portion of most business entities' non-refundable cash outlay. And the potential for labor-over-runs can be the riskiest element of any project undertaken. Yet, over our years of working with clients, we've found that most businesses (and business owners) have never actually taken the time to compute the true, total expenses associated with each employee. As a result, those businesses have not been able to take advantage of the many beneficial ways in which they could use that information.

So, this series of articles is designed to explore the variety of different ways that you can:

1. Compute and understand the full, true cost of employee labor.
2. Compute what you should really be charging for direct labor employees to meet your profit goals.
3. Creatively use employee cost (and income) information to positively impact your bottom line.
4. Measure the cost of lost and/or wasted time.
5. Be certain that you are achieving an excellent return on your investment in each employee.
6. Compare and contrast the cost of employees vs. subcontractors or outsourced services.

What is Labor Burden and How Does it Impact My Business?

You are probably in fairly close touch with each employee's hourly wage or salary, and may have a good idea of approximately what payroll taxes cost. But you may not have taken the time to research and compute all of the additional "hidden" costs associated with each individual, including (but not limited to):

- Paid time off
- Health insurance
- Worker's compensation insurance
- Uniforms or special work clothes
- Training
- Usage of equipment and vehicles
- Workspace (e.g., office or floor space) costs



So how do we refer to these extra employee-related costs (including taxes)? Here are some of the terms (and calculations) frequently used by businesses who closely track employee costs:

Labor Burden: The costs – **above and beyond gross compensation** – that you incur in order for an employee to perform the work that you hired them to do.

Labor Burden Cost per Production Hour (or Fully-burdened Cost):

(Labor Burden Cost + gross payroll labor cost) ÷ the number of actual work (production) hours.

Labor Burden Rate per Production Hour (%): The additional total labor burden cost, expressed as a percent, above and beyond regular hourly payroll. I.e., Labor Burden Cost per hour ÷ hourly payroll cost.

After you compute an employee's fully burdened labor cost and then divide it by the number of hours that employee actually works on projects, businesses often find that workers typically cost the company from 50% to 150% (or more), above and beyond their gross hourly labor rate. Getting in touch with, and carefully managing, employment-related costs can be the critical difference between staying in (or needing to get out of) business. Let's review a fairly simple example.

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How Much, in Total, Does it Cost for Pat to Perform His/Her Job?

We'll start with an employee ("Pat"), whose hourly compensation is \$17, or \$35,360 gross annual payroll. As Pat's employer, you do your research and find out that Pat has a variety of additional annualized costs "attached" to this position:

- \$3,005 for payroll taxes (based on 2.7% state unemployment on the first \$9,000, and no other state disability taxes).
- \$3,536 for workers' compensation insurance (at \$10 per \$100).
- \$4,200 for health insurance (\$350 per month).
- \$1,060 for retirement benefits (3% of compensation).
- \$720 for cell, telephone and/or Internet costs (\$60 per month).
- \$150 in uniforms (e.g., 4 company shirts at \$25, 1 jacket at \$50) or for office workers an equivalent amount in coffee(!).
- \$6,000 in company vehicle usage (depreciation, gas and oil, maintenance, license, insurance, etc.), or for office workers an equivalent amount in equipment usage and maintenance. and office space.
- \$300 in small tools and equipment usage (at \$25 per month) or for office workers an equivalent amount in office supplies.
- \$708 estimated annual bonus (2% of wages).
- \$100 employer-paid snacks, meals, parties, entertainment.
- \$250 in training fees, seminars, etc.



Total additional costs: \$20,029.

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How Many Hours Is Pat Actually Available for Work?



Next, let's determine how many hours Pat is potentially available for company work. Start with 52 weeks/year x 40 hours/week = 2,080 hours.

Then subtract Pat's non-project paid time for the year:

- Six holidays.
- 10 vacation days.
- Six sick or personal days.
- Two days of training seminars.

This equals 24 days (192 hours), leaving 1,888 available working hours.

You'll then subtract an estimate of two hours from the 47 remaining work weeks for miscellaneous administrative meetings, timekeeping, general problem-solving or prep time and so forth (breaks are assigned to jobs or projects). This reduces the available production time by another 94 hours.

Total time available for production/project work: 1,794 hours.

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The Final Results for Pat's "Numbers"?

First, Pat's additional Labor Burden Costs total just over **\$20,000**. This brings Pat's annual cost to **\$55,389**.

Therefore Labor Burden Cost per Production Hour (or Fully-burdened Cost) to your company is **\$30.87** per production/project hour ($\$55,389 \div 1,794$ hours) or **\$0.51** per minute.

To compute Pat's Labor Burden Rate (%) per Production (work) hour, subtract Pat's hourly rate from his/her fully burdened cost ($\$30.87 - \$17.00 = \$13.87$) and divide the excess by the base hourly rate. We see that our additional cost to have Pat "on the job", when computed as a percentage, adds **82%** to Pat's base hourly rate.

The bottom line: Pat is a truly **costly and valuable asset** whose time should be carefully assigned. And his/her related costs (and resulting contribution) should be closely measured and monitored!

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Next,...

**Labor Burden & Profits – Part II:
Exactly What Should Your Employees Contribute to the Bottom Line?**

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*She is the developer of the **Qlean\$tart Worksheet: Labor Burden Calculator**, an Excel spreadsheet that automatically performs comprehensive labor burden and billing rate calculations for up to 40 or up to 100 individual employees. To view an on-line demo please go to <http://www.infoplusacct.com/productdemo.html>. Contact Gilson via email at help@InfoPlusAcct.com or contact her at 734-544-7620.*