

## LABOR COSTS - DIRECT-INDIRECT

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The terms wages and salaries are frequently used as though their meanings were clear and concise. Wage rates, salaries, real wages, take home pay, earnings, labor costs, income and net pay are used frequently as though they were interchangeable. The term wages is frequently used to refer to payments for labor services. Wages are usually paid to individuals who work by the hour whereas salaries are paid on a weekly or monthly basis. Wage rates are payments based on time units, i.e., working hours. Earnings include wages, overtime and bonuses. Take home pay is gross pay less deductions. Take home pay is of paramount importance because in many instances the workers can recall their take home pay but not their gross pay.

Labor costs generally apply to the total labor bill, sometimes divided between direct labor costs, wages and other payments and indirect costs which apply throughout the firm, shop or plant but which may not be specifically allocated. Labor costs are related to wage rates or earnings but are not the same thing. Only if wages are paid as piece rates will an adjustment presumably affect labor costs in the same manner and amount. Labor costs can be realistically calculated only on a unit of output basis. If the rate of output changes, the variation will influence labor costs. For example, if wage rates are increased 10 percent while output remains the same, the direct labor costs will increase in approximately the same proportion. If, however, output increases 20 percent in the same period labor costs are likely to fall. If wage rates remain the same and output falls, direct labor costs may actually increase.

A significant factor in the total wage bill is fringe benefits - or employee benefits. One definition of a fringe benefit is a payment received by a worker in addition to wages. They are not direct wage payments. The list of fringe benefits includes paid holidays, paid vacations, paid rest periods, pensions, life insurance, hospitalization and surgical insurance, dental plans, contributions to workmen's compensation, unemployment insurance and social security.

The table below presents a listing of employee benefits which are very prevalent in American business and industry.

1. Legally required payments (employer's share only)
  - (a) Old Age, Survivors, Disability and Health Insurance (Social Security)
  - (b) Unemployment Insurance
  - (c) Workmen's Compensation
2. Pensions and other agreed upon payments (Employers share only)
  - (a) Pension
  - (b) Life Insurance
  - (c) Hospitalization and Medical Insurance
  - (d) Sickness and Accident
3. Paid rest periods, lunch periods, wash up time, travel time, get ready time
4. Payments for not worked
  - (a) Paid Vacations
  - (b) Paid Holidays
  - (c) Paid Sick Leave
  - (d) Payments for National or State Guard duty, jury duty, payment for time lost due to death in family and other personal reasons

## 5. Other Items

- (a) Providing Work Clothes or Cleaning of Work Clothes
- (b) Christmas Bonus
- (c) Special Employee Parties

In discussions with a sod farmer and a superintendent of a golf course, there are other employee benefits which are included and for which there are costs. The farmer stated that he provides his employees with a house with electricity and heat. The estimated annual cost is \$3600. The superintendent of the golf course stated that the employees who come in say on Saturday or Sunday and who work for three hours will be paid for four hours. In addition, employees can use the facilities and course without payment of fees. Moreover, in this instance and it is not an isolated employee benefit, the employees can use the tools and equipment available to work on their personal vehicles.

While data on the costs of employee benefits for employees involved with turf-grass are not available, there are data available for American business and industry. These data are collected by the Chamber of Commerce of the United States.

There are three primary ways to express the value or cost of a fringe benefit.

- (1) total annual cost of the benefit per employee
- (2) cost of the benefit in cents per payroll hour
- (3) cost of the benefit as a percent of payroll

Table I below presents U.S. Chamber of Commerce data for 1973 on the costs of employee benefits. The employee benefits as a percent of payroll for all industries was 32.7 percent. Employment benefits as cents per payroll hour was 154.1 cents or \$1.54 per payroll hours. The total cost of the employee benefits per year per employee was \$3230.

Table II shows a comparison of 1953-73 Employee Benefits for 155 companies. These data reveal the significant increases in the costs of employee benefits over the two decades. The cost of employee benefits as a percent of payroll increased from 21.6 percent in 1955 to 36.3 percent in 1973. The cost as cents per hour rose from 40.6 cents to 180.6 cents or 4.5 times the 1955 cost. Employee benefits in dollars per year per employee rose from \$842 in 1955 to \$3802 in 1973, a whopping gain of 350 percent in twenty years.

There are several explanations for these significant increases in the cost of employee benefits. Like everything else, the cost of employee benefits are affected by inflation. Government actions have contributed to the increasing cost of employee benefits. The Social Security tax is a case in point.

The cost of Federal Social Security program to the employer and employee increased as of January 1, 1975. The tax rate prior to January 1, 1975, was 5.85 percent on the first \$13,200 of wages and salaries. The tax rate remains the same but the taxable wage base is now \$14,100. This means that the employer's tax contribution has risen from \$772.20 a year to \$824.85, an increase of \$52.65. This represents an increase of 6.8 percent in the employer's tax contribution.

The insurance carriers have also increased their rates. One brief example will suffice. Prior to December 1, 1974, in Michigan the Workmen's Compensation rate for sod farmers was \$3.32 per \$100 of payroll. The new rate of \$3.56 per \$100 of payroll became effective December 1, 1974. The rate increase from \$3.32 to \$3.56 per \$100 of payroll represents an increased cost of doing business for one employee benefit item of 7.2 percent.

Aside from the factor of inflation, another factor which helps to explain the growth of employee benefits in recent years is the tax advantage. Employers can make improvements either through collective bargaining and/or unilaterally and can deduct their costs as a cost of doing business. If money is given to employees to purchase such benefits, the employee's income would be taxed. Thus it is cheaper for the

employer to provide employee benefits because of the tax laws.

Perhaps the most significant factor affecting the expansion and growth of employee benefits is the employee's fear of insecurity. This is particularly true in a job economy where 90 percent of the nation's labor force are employees. The employees, therefore, seek protection against those hazards of life which affect income. These include unemployment, disability, illness, old age and death. The chart below points out the risks or hazards of living and the responses or approaches for their mitigation. Over the years, a complex set of efforts have been developed to provide protection for the employees and their families. These efforts include a combination of individual, employer and government actions.

It is safe to predict that employee benefits will be expanded and will become more costly. These items are no longer a fringe; nor are they a hidden cost of employment. As was indicated earlier, the cost of employee benefits represent 32 percent of total payroll in American business and industry in 1973. It will increase not only for business, industry and government, but for agricultural full time workers.

There is another cost of doing business which is becoming increasingly burdensome. Absenteeism was formerly considered a hidden cost but with the growth of employee benefits it has become primarily a fixed cost. If an employee is absent, the cost of pensions, insurance vacations and holidays is not affected. The benefits accrue during his/her absence. There are other costs involved when an employee is absent. For example, the postponing of work may entail a cost, the unused equipment is a cost factor, the loss of production during the employee's absence is a cost factor. Employers need to give careful analyses to the cost of absenteeism. Moreover, if absenteeism is excessive, steps should be taken to control it. Absenteeism is an important cost consideration which has increased in importance in recent years.

In summary, the wage bill and the cost of doing business are being significantly and dramatically affected by the increased costs of employee benefits - those legally required and those granted by employers unilaterally or through collective bargaining. The trend of more benefits for employees will continue and will increase the cost of doing business. In addition, increased absenteeism has increased the costs of doing business for many firms and it must be considered in the cost structure.

FEARS OF INSECURITY AND APPROACHES TO MITIGATION

<u>RISKS</u>	<u>APPROACHES FOR MITIGATION</u>		
	<u>Individual</u>	<u>Group</u>	<u>Government</u>
1. Illness	1. savings 2. insurance 3. relatives/family	1. group, health insurance 2. sick leave	
2. Injury on the job	1. savings 2. insurance 3. relatives/family	1. sickness/accident insurance	1. Federal: disability benefits under Social Security 2. State: workmen's compensation
3. Unemployment	1. train himself 2. move to another employer and/or another city 3. savings 4. relatives/family	1. retraining 2. relocation allowances 3. severance pay 4. supplemental unemployment benefits	1. State: unemployment insurance 2. Federal Manpower Programs
4. Old Age (with income)	1. savings 2. annuity 3. relatives/family	1. pension	1. Federal: old age benefits
5. Old Age (without income)	1. family/relatives	1. private welfare	1. Federal: old age assistance (supplemental security income)
6. Disability (with income)	1. savings 2. insurance	1. disability insurance	1. Federal: disability benefits under Social Security
7. Disability (without income)	1. relatives/family	1. private welfare	1. Federal: supplemental security income (APTD)
8. Death	1. savings 2. insurance 3. relatives/family	1. life insurance	1. Federal: Survivors benefits
9. No income	1. relatives/family	1. private welfare	1. State/County Welfare Programs 2. Food Stamps

Observations:

1. individual, group and governments are involved
2. mixture of contributory and non-contributory
3. public and private efforts
4. complex system of efforts

TABLE I. COMPARISON OF 1953-73 EMPLOYEE BENEFITS FOR 155 COMPANIES

Item	1953	1955	1957	1959	1961	1963	1965	1967	1969	1971	1973
<u>All industries (155 companies)</u>											
1. As percent of payroll, total . . . . .	21.6	23.5	25.0	25.6	26.9	28.0	28.0	30.2	31.8	34.2	36.3
a. Legally required payments (employer's share only). . . . .	2.8	2.9	3.1	3.5	3.9	4.5	4.1	4.9	5.3	5.5	6.7
b. Pension and other agreed-upon payments (employer's share only) . . . . .	7.4	8.3	8.7	9.2	9.3	9.5	9.8	10.3	10.7	12.4	13.0
c. Paid rest periods, lunch periods, etc. . . . .	2.0	2.2	2.3	2.1	2.5	2.6	2.6	3.0	3.2	3.2	3.3
d. Payments for time not worked. . . . .	7.4	7.9	8.8	8.9	9.4	9.6	9.7	10.0	10.6	11.1	11.3
e. Profit-sharing payments, bonuses, etc. . . . .	2.0	2.2	2.1	1.9	1.8	1.8	1.8	2.0	2.0	2.0	2.0
2. As cents per payroll hour. . . . .	40.6	48.4	55.8	63.0	71.4	80.8	87.8	102.9	120.8	146.4	180.6
3. As dollars per year per employee . . . . .	842	1011	1160	1311	1483	1683	1836	2133	2516	3033	3802
<u>All manufacturing (62 companies)</u>											
1. As per cent of payroll, total. . . . .	20.1	22.2	24.1	24.4	25.8	27.0	27.4	29.7	32.0	24.6	36.8
2. As cents per payroll hour. . . . .	37.9	45.2	52.7	59.8	67.3	75.3	83.3	96.6	114.4	142.5	177.2
3. As dollars per year per employee . . . . .	803	958	1105	1247	1409	1589	1777	2048	2444	3017	3803
<u>All nonmanufacturing (93 companies)</u>											
1. As per cent of payroll, total. . . . .	22.5	24.4	25.5	26.4	27.6	28.7	28.5	30.4	31.7	33.9	35.9
2. As cents per payroll hour. . . . .	42.4	50.6	57.9	65.1	74.1	84.4	90.8	107.0	125.1	149.0	182.9
3. As dollars per year per employee . . . . .	868	1046	1197	1353	1533	1746	1875	2190	2564	3044	3802

Source: United States Chamber of Commerce

TABLE II. EMPLOYEE BENEFITS IN INDUSTRY, 1973

Type of benefit	Employee benefits as per cent of payroll	Employee benefits as cents per payroll hour	Employee benefits as dollars per year per employee
Total employee benefits as per cent of payroll. . . . .	32.7	154.1	3230
1. Legally required payments (employer's share only) . . . . .	7.5	35.6	746
a. Old-Age, Survivors, Disability and Health Insurance. . . . .	5.3	25.1	527
b. Unemployment Compensation. . . . .	1.2	5.6	117
c. Workmen's compensation (including estimated cost of self-insured) . . . . .	0.9	4.4	92
d. Railroad Retirement Tax, Railroad Unemployment and Cash Sickness Insurance, state sickness benefits insurance, etc. . . . .	0.1	0.5	10
2. Pension and other agreed-upon payments (employer's share only) . . . . .	10.5	49.1	1032
a. Pension plan premiums and pension payments not covered by insurance type plant (net) . . . . .	5.1	24.0	503
b. Life insurance premiums, death benefits, sickness, accident and medicare insurance premiums, hospitalization insurance, etc. (net) . . . . .	4.6	21.8	457
c. Contributions to privately financed unemployment benefit funds . . . . .	***	0.1	3
d. Separation or termination pay allowances . . . . .	0.1	0.3	6
e. Discounts on goods and services purchased from company by employees. . . . .	0.2	0.2	15
f. Employee meals furnished by company. . . . .	0.2	1.0	22
g. Miscellaneous payments (compensation payments in excess of legal requirements, disability insurance, moving expenses, etc.) . . . . .	0.3	1.2	26
3. Paid rest periods, lunch periods, wash-up time, travel time, clothes-change time, get-ready time, ect. . . . .	3.5	16.3	341
4. Payments for time not worked . . . . .	9.2	43.7	914
a. Paid vacations and payments in lieu of vacation. . . . .	4.7	22.2	466
b. Payments for holidays not worked . . . . .	3.0	14.1	295
c. Paid sick leave. . . . .	1.1	5.3	110
d. Payments for State or National Guard duty, jury, wit- ness and voting pay allowances, payments for time lost due to death in family or other personal reasons, etc. . . . .	0.4	2.1	43

TABLE II., Cont'd.

Type of benefit	Employee benefits as per cent of payroll	Employee benefits as cents per payroll hour	Employee benefits as dollars per year per employee
5. Other items. . . . .	2.0	9.4	197
a. Profit-sharing payments. . . . .	1.1	5.3	112
b. Contributions to employee thrift plans . . . . .	0.2	1.1	22
c. Christmas or other special bonuses, service awards, suggestion awards, etc. . . . .	0.4	1.8	37
d. Employee education expenditures (tuition refunds, etc. . . . .	0.1	0.4	8
e. Special wage payments ordered by courts, payments to union stewards, etc . . . . .	0.2	0.8	18

\*\*\* Less than 0.05%

Source: United States Chamber of Commerce