

Labor Efficiency Ratio (LER)

How to Use LER to Manage Labor to Higher Profits

Slides at:
Simplenumbers.me/brightstar

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SIMPLE NUMBERS, STRAIGHT TALK, BIG PROFITS!

4 KEYS TO UNLOCK YOUR
BUSINESS POTENTIAL

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WITH BEVERLY BLAIR HARZOG

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Simple Numbers... Straight Talk... Big Profits

4 Keys to Unlock Your Business Potential

- Your data is lying! - Why how you deal with Owner's compensation is distorting your data
- Profit matters more than you think – How to set the right profit targets for your business
- **Labor Productivity drives you profit engine – How do measure it and improve it**
- 4 Forces of cash flow – Get the priorities right to set your business on a solid foundation

Labor Efficiency Ratio Defined

- **Direct Labor Efficiency**
 - Value Added Revenue divided by Caregiver wages (does not include taxes and benefits)
- **Management Labor Efficiency**
 - Gross Margin divided by Management wages (all non-caregiver wages)
- **Every labor dollar must be held accountable to output either as an individual or a group.**
- **FTE (full time equivalent) employee is a flawed measure because it does not account for the unique output of each person. Even hours is a flawed measure. Output per dollar of labor is the only fair measure.**

Why use LER?

- Expresses Labor as a multiplier, not a fraction
- Simplifies pricing and performance measurement because the multiplier covers all costs if volume is achieved
- Makes forecasting and scenario planning quick and easy.
- Makes customer profit analysis simple
- Targets can be measured with each payroll cycle

BrightStar P&L Examples	Company 1	Company 2	Company 3	Company 4	Company 5
Revenue	1,066,527	903,339	1,728,801	1,582,692	562,032
Cost of Goods Sold	4,176	15,240	21,168	21,375	6,945
Value Added Revenue	1,062,351	888,099	1,707,633	1,561,317	555,087
as a % of sales	100%	98%	99%	99%	99%
Direct labor	626,838	536,223	862,320	823,719	340,476
Direct Payroll Taxes & Benefits	95,040	115,947	121,488	273,111	66,897
as a % of sales	59%	59%	50%	52%	61%
Direct LER (VAR/DL)	1.69	1.66	1.98	1.90	1.63
Gross Margin	340,473.00	235,929.00	723,825.00	464,487.00	147,714.00
as a % of sales	32%	26%	42%	29%	26%
Operating expenses:					
Facilities	11,481	21,390	26,184	34,884	18,513
Royalty	61,989	44,262	83,541	78,513	25,917
Marketing	38,298	40,119	61,665	29,958	19,113
Management Labor	190,578	108,624	170,475	74,469	45,183
Payroll Tax and Benefit	43,095	8,646	23,088	39,504	5,319
Other Operating Expense	47,352	48,168	52,209	63,921	58,389
Total operating expenses	392,793	271,209	417,162	321,249	172,434
as a % of sales	37%	30%	24%	20%	31%
<i>Management LER (GM/Mgmt Labor)</i>	1.79	2.17	4.25	6.24	3.27
Net operating income	(52,320)	(35,280)	306,663	143,238	(24,720)
as a % of sales	-5%	-4%	18%	9%	-4%
Other income (expense):					
Interest expense	(10,401)	(5,979)	(9,105)	(10,989)	(2,283)
Depreciation	(843)	(1,122)	(5,370)	(23,730)	(8,709)
Total other income (expense)	(11,244)	(7,101)	(14,475)	(34,719)	(10,992)
Net income before Executive Expenses	(63,564)	(42,381)	292,188	108,519	(35,712)
as a % of sales	-6%	-5%	17%	7%	-6%
Executive Expenses	37,224	-	58,353	4,230	204
Net Income	(100,788)	(42,381)	233,835	104,289	(35,916)
as a % of sales	-9%	-5%	14%	7%	-6%

Key Factors					
Marketing (as % to sales)	4%	4%	4%	2%	3%
Payroll Taxes and Benefit - Direct Labor	15%	22%	14%	33%	20%
Payroll Taxes and Benefit - Management Labor	23%	8%	14%	53%	12%
Other Operating Expense (as % to sales)	4%	5%	3%	4%	10%
Gross Margin/Marketing\$	8.89	5.88	11.74	15.50	7.73
Direct LER	1.69	1.66	1.98	1.90	1.63
Management LER	1.79	2.17	4.25	6.24	3.27
Management Salary & Benefit Cap	21.91%	12.98%	11.20%	7.20%	8.99%
Net income %	-9%	-5%	14%	7%	-6%
Revenue \$	\$ 1,066,527	\$ 903,339	\$ 1,728,801	\$ 1,582,692	\$ 562,032

Factors Affecting LER

- Revenue too low for wage rate
- Paying too much for Caregivers
- Paying Caregivers for time not billed where no value was added
- Is the right skill level caregiver working on the right cases?
- Overtime premium
- Management Labor too high, thus requiring more gross margin to support it
- Beware of the Management LER multiplier! (8x)

NON-LER Factors Affecting Profit

- Direct Labor benefit structure too generous
- Management benefits too high
- Executive expenses too high for performance level

LER Makeover Examples

LER Analysis Process

- Evaluate what LER would need to be to achieve profit target
- Determine the cause (paying too much, paying for time not billed or not billing enough for wages paid)
- Evaluate other primary contributors (benefits too high, Management Labor not effective, Executive Benefits)