



Finding Hidden Employment Costs

The Complete Guide for
Business Owners

A free resource from



As any company grows, it becomes more difficult to handle all of the employment costs involved. Here are just a few facts about small business owners that might turn your hair grey:

Almost **50% work more than 40 hours a week.**

Around **40% take less than 1 week of vacation per year.**

Nearly **20% say that regulations on small businesses are their greatest source of stress.**

These worries only worsen over time as your business expands. Managing all of these challenges well is incredibly difficult and leaves no time for thinking about cost management. **Although many factors place cost burden on a small business, this piece addresses cost management through 3 lenses:**

- 1. Hidden HR Administrative Costs**
- 2. Insurance and Benefits Management**
- 3. Vendor Consolidation**

In each of the sections below we will examine some of the most critical cost issues affecting small businesses and propose solutions offered for eliminating headaches and reducing risk related to each issue. Overall, our goal is to help illuminate otherwise hidden or unknown costs for those running small businesses, and to offer helpful strategies and solutions for improvement.

HR Administrative Costs

Small business owners know firsthand that the axiom “you don’t know what you don’t know” is more than a clever saying. Managing costs efficiently and proactively requires business owners or other responsible personnel to have the following throughout their organization:

- 1. Visibility into costs**
- 2. Time to monitor costs**
- 3. Methods of analysis to measure opportunity cost against current investments**
- 4. Strategic planning and foresight**

Unfortunately, even meeting the criteria above does not ensure that hidden costs will be discovered. While it is relatively easy to track payroll and employer-sponsored benefits costs, it can be hard to determine the total cost of employment, including vendors, taxes, fees, premiums and the time internal resources spend doing Human Resource-related tasks. Some of these hidden costs might be intentionally kept from view by vendors, or they might be incurred unintentionally through inefficient processes or regulatory burdens. Thankfully, a trusted partner can help present a transparent view of all costs and advise where spend can be redirected to improve productivity and the bottom line. Let’s take a closer look at how hidden costs can be camouflaged within small businesses.

How Are Costs Hidden From View?

Additional Fees

Most payroll services charge for W2s, garnishments, custom reports, W2s, and ACA reporting, making it difficult to know the total costs annually. These services might all be “in addition” to the standard fees charged by providers, quickly racking up bills.

Inefficient Processes

Having internal resources do HR is often inefficient, despite good intentions. Do any of these sound familiar?

- Reconciling and keying time data into the payroll system or payroll data into the General Ledger
- Tracking attendance and paid-time-off balances
- Updating benefit carriers and other vendors
- Submitting state unemployment filings
- Allocating employee costs across departments



Insurance Commissions

Commissions for insurance agents are embedded in insurance premiums, making it hard to ascertain the actual cost of benefits administration. It is especially important to keep track of these costs as insurance benefit expenses continue to rise. This will be discussed further in a later section.

Workers' Comp

Worker's Compensation, if not tightly managed, usually results in a catch-up payment in the annual audit. Injuries and compensation can practically drown owners and managers in paperwork.

Unemployment Taxes

Unemployment tax rates are communicated in December, often through a payroll service, and then paid quarterly. These taxes are very easy to forget.



Now that we know the most common problem areas of HR-related cost management for small businesses, we should talk about solutions. Each of the key problems listed above are addressed in a corresponding section below.

Transparent Pricing On Administration Fees

Large vendors can try to sneak costs past with you with ambiguous wording or by failing to disclose which services are not included. Look for vendors with a transparent pricing strategy. The goal is to eliminate hidden fees, and separate insurance and tax fees from administration fees.

Streamline Accounting for HR Expenses

Predictable Expenses

A predictable billing structure prevents unwanted surprises. Budgeting and forecasting is simple and cash flow is easier to manage when employment expenses are clear and well-known.

Streamlined Cost Allocation

Connecting full employment costs to payroll simplifies the accounting burden of ensuring the 'benefits load' follow the staff in various departments or parts of an organization. Good payroll cost reports show the full costs of employees. If there are shared or split resources, those full costs can be shared or split as a consistent rule, or can vary each payroll. These options allow you to control reporting for complete transparency

HR and Accounting Integration

Set-up custom reporting that feeds payroll cost reporting directly into your general ledger.

Time & Labor

An integrated timeclock or timesheet import feature can be used to automate time reporting for hourly employees into payroll. This feature reduces errors and the duration spent conducting reconciliation and proofing.

Benefits: Reduce errors and the amount of work required to reconcile benefits bills by using automated file feeds to all benefits carriers. Find a vendor who can proactively provide open enrollment and new hire benefit elections, terminations, and other updates so that billing remains accurate.

Managing Rising Insurance Costs

Although insurance commissions were specifically mentioned earlier as an unknown cost, there are several other aspects to handling insurance expenses that should be explored in more detail. Like the problems, the solutions to mitigating rising insurance costs are multi-faceted.

It's no secret that increasing insurance costs have presented businesses with a difficult problem. To visualize this problem, consider the following question: what is the best way to handle a 15% increase from a health insurance carrier? At first glance, there may be 3 apparent options: increase employee's cost, decrease benefits, or absorb the increased cost as the plan sponsor.

Unfortunately, the first two choices impact an employee's perception of what they receive in total compensation, encouraging them to look elsewhere for more competitive options. However, the last option listed above erodes the bottom line. In fact, for a \$5MM small business with 10% earnings, choosing to absorb medical increases over a period of seven years actually results in a loss. This example even accounts for 4% revenue growth!

To make matters worse, medical plans are expected to increase 7-9% in 2018. This trending increase is higher than 2017 and driven more by price inflation than increased utilization, though Rx price increases are also a significant contributing factor.

Strategies To Employ

The following strategies have grown in prevalence and proven effectiveness:

- Shift to (or secondary offer), a QHDP and pre-fund Health Savings Accounts.
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- Move to self-funding, shared funding, or similar alternative to fully-insured.
- Medical cost “layering” using indemnity plans.
- Extra-contractual benefits to incentivize employee’s consumerism, including direct negotiations with providers.

Each of these strategies are effective when properly implemented, and we’ve seen dramatic results in excess of 20% YOY savings. However, three of the five strategies have catastrophic (close the doors) implications if managed improperly.

There are four essential questions to ask when considering each strategy mentioned above:

- **Will my employee’s perceive this change to be a benefit enhancement, or reduction?**
- **What impact will this change have on my organizational budget?**
- **What additional risk is my company taking?**
- **What additional out-of-pocket risk are my employee’s absorbing with this change?**

Now, let’s examine one of the recommended strategies using these four questions...

Qualified High Deductible Plans (QHDP) with HSA funding:

Employee Perception

If this is a new concept to your employees, it's possible that they've been living under a rock. However, enrolling in an HSA plan for someone accustomed to a traditional health plan (especially low deductible plans) can be intimidating. What should be presented, is the total annual household exposure and cash flow. The HSA will always, always, win this argument. Whether the employee is a non-user or chronic user, the HSA wins. However, the employer must contribute something to each enrollee's health savings account for at least the first year. A good broker will present these options, educate the employer's group, and calculate all associated costs.

Organizational Budget

The insurance premium for a QHDP will be less than a comparable deductible traditional plan.

Therefore, as employees are encouraged to enroll in the QHDP the company saves premium that can be used to fund HSA accounts, or a portion of the savings can be passed to the employee in the form of reduced payroll deductions for the chosen HSA plan. This approach works well for the short term.

Long-term, when HSA account balances grow over time, higher deductible options can be added (even as secondary options) at a lower premium. Ultimately, when properly implemented, a QHDP with deductible equal to maximum out-of-pocket (\$7,350/\$14,700) with 100% coverage thereafter should be a plan on the benefits menu. If "company A" currently offers an "average" traditional plan with a \$1500 single deductible, transitioning to a \$7350 HSA would cut their insurance premiums in half.

Additional Company Risk

None.

Additional Out-of-Pocket for Employees

None. It might seem like increasing an employee's deductible seems would increase out-of-pocket expenses. In reality, most ACA-compliant plans offered today have a maximum out-of-pocket limit equal to IRS guidelines (\$7,350/single for 2018). Furthermore, if the average deductible is \$1,500/single, the only reduction in benefit when moving to a similar deductible QHDP is flat-dollar copays. Consider that paying an office visit copay at \$30 with after-tax money actually costs about \$40 in wages. Now consider paying for that office visit at \$100 (retail) with pre-tax HSA dollars. This costs \$60 more but only when used. If an employer matches HSA deposits \$1 for \$1 (up to a limit), now an office visit costs \$30 and reduces future deductible! Another win! Although we have only looked at one example, remember that this four-question framework should be applied to all of the aforementioned strategies to help mitigate potential issues.

Managing Unemployment Costs

Flexible Staffing

If a business has seasonal cycles, a great way of managing unemployment exposure is to use a temporary service instead of laying off each year during down times. By identifying patterns, you can build a flexible staffing plan to reduce exposure AND still meet staffing needs.

Involuntary Termination

Unemployment claims are won before the claim even starts with effective support throughout the involuntary termination process. Preparing key documentation and avoiding common missteps is critical for putting yourself in a good position to contest any future claim.

Claims Management

Do you know the best (and worst) ways to contest a claim? A solid claims process includes: manager documentation review, timely claims documentation and form submission, and unemployment hearing representation. Ensure that claims are managed in an integrated fashion across all absence programs, whether pay replacement or job protection related: Paid Time Off, FMLA, ADA, short-term disability, long-term disability, and Worker's Compensation. When an employee has a health or family issue it is common for multiple programs to overlap. It takes careful coordination to ensure that the proper tracking and compliance is in place, and that there is no 'double dipping' regarding pay replacement.

Return to Work Program

Helping injured or ill employees return to work is critical to assisting their recovery. You can use a variety of tools to encourage a return to the workplace, including:

- Personalized case management
- Light duty placements
- Employee assistance program
- Occupational therapy and clinical experts

A proactive approach to getting employees back to work will benefit employers in two ways. First, it will optimize disability and workers' compensation experience, translating to minimized premium increases. Second, pro-activeness will also help workers get healthy faster. Saving costs and promoting health are both solid business outcomes regardless of the company size or industry



Vendor Consolidation

To recap, so far we have discussed how specific vendors can cloak costs through a variety of methods (e.g. charging for additional necessary services or disguising commission fees). What we have not discussed is how using numerous vendors can quickly multiply unknown or unforeseen costs. Consolidating vendors is a crucial strategy for ALL business owners to help eliminate redundancies, improve processes and lower administrative expenses (and headaches). Another way to state this is: vendor consolidation can help you sleep better at night and get more enjoyment out of those rare vacations. Why not let the professionals handle problems?



Vendor Selection Doesn't Get Enough Attention

Most small business owners spend each day making hundreds of decisions regarding the operation of their business. Each decision determines whether that day, week or year is profitable. Making critical decisions typically involves numerous vendors that interact with the business owner – daily, weekly, monthly, quarterly and annually. This interaction isn't always fun; often it is just necessary. It can be surprising how quickly vendors takeover one specific workflow, even if they don't work well with other programs or providers.

Vendors are found through recommendations, hopeful Google searches, prior experience or even relatives or contacts in a particular industry. While the decision to choose one vendor over another is often made in an effort to become more efficient, the final decision is often reached with too little information. Sometimes there is no rhyme or reason to a decision that is made out of necessity or convenience because other issues are more pressing.

Additionally, once a vendor selection is made business owners often try to not disrupt the relationship no matter how dysfunctional some of them may become. For many business owners, their ability to choose the right vendor diminishes proportionately according to their own knowledge about that industry. For example, a technology company can select the best software solution, but they might not understand how to provide a competitive insurance package for their employees.

Get Perspective On The Cost

The best way to get started with vendor consolidation is simply by stepping back from the business to review vendor relationships. As perspective is gained, there are two ways that business owners should think about cost that can help them become more efficient, competitive and profitable.

Direct Cost

Direct cost savings (often easily measured) are derived from lowering the actual daily cost of doing business. An example of direct cost savings would be finding a less expensive provider or implementing a new method to save time on operational tasks.

It might be helpful to consider the following direct cost savings strategies with your vendors:

- 1. Can money be saved by simply changing to the direct competitor of a current vendor?**
- 2. Can one vendor handle tasks or operations that two or more currently manage?**
- 3. Does a new vendor offer clear competitive advantages in their marketplace?**
- 4. Is it worth completely outsourcing an operation that is currently managed in-house using a vendor solution?**

Vendors can handle nearly any operation within a business, but here is a list of the most popular vendor functions, some of which were mentioned earlier:

- Payroll
- Tax compliance
- Workers compensation insurance and related claims management
- Accounting services
- Unemployment claims filing and management
- Health insurance for yourself and your employees
- Retirement planning and services
- HR tasks such as running open position ads, interviewing, hiring and all related paperwork and personnel files
- All other insurances and claims activities
- Lawsuits



Opportunity Costs

The second method of cost savings is through lowering the opportunity costs of running a company. We have had countless discussions with small business owners where they admit to not having enough time or energy to manage non-core tasks of the company.

It is tempting to dismiss national research showing that task-oriented inefficiencies cost small business owners thousands of dollars per year as “irrelevant” or only for the “other guys.” However, after nearly 30 years in the West Michigan community, we can say with certainty that these statistics are not only accurate, they are understated.

1. HR at 70% of small businesses is handled by an owner or someone with other primary responsibilities
2. These tasks can absorb more than 13 hours a week in total.
3. 30% of small business owners spend more than six hours a week on payroll tax administration alone.

A quick calculation using these figures reveals that business owners and other crucial staff members spend up to 30% of their time EVERY week on HR-related tasks. The opportunity cost here is staggering as small business owners could use this time and energy to focus on:

1. Sales growth
2. Innovation/Market Disruption
3. Training/Relationship Development
4. Thought Leadership/Conferences
5. Employee Management
6. Strategy Development
7. Vendor Review
8. Golf!

The impact that 30% of a small business owner’s time can make when dedicated to growing and sustaining their company is enormous.

Conclusion

Hidden costs can reside in any part of a company, but knowing where to look is crucial. While there are many ways to reduce hidden costs, the most important thing is to get started. A trusted partner can guide you through this process and offer help as your business grows and adapts in a dynamic marketplace and thriving community.



**If you need HR expertise to
help you identify and manage
the costs of running a
business, we're here to help.**



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