



The Rising Cost of Human Capital

By Walter Weathers, Catalyst/Hall – Houston

At Catalyst/Hall we view human capital as one of the primary value components in a business. We place a premium on competent, trustworthy management teams, and we recognize that a key success factor for any company is the contributions made by non-management employees. A motivated, well-trained work force is essential to creating long-term shareholder value.

Over the last several years, the costs of attracting and maintaining highly qualified human capital has risen at an alarming rate, fueled primarily by rising health care costs. National health expenditures consumed 15.3% of GDP in 2003 versus just 8.8% in 1980, and health insurance premiums for a family of four have risen over 12% per annum over the last four years (according to a Kaiser Family Foundation survey). Consequently, employers are requiring that employees bear a higher share of the total health care cost, contributing to employee discontent as real wages are barely increasing, while the costs of living march upward. The two major issues related to health care costs appear to be: a) the runaway compound growth rates (which we do not attempt to address herein); and b) the sharing of these costs.

Federal and state governments, attempting to find a middle ground between employers and employees, are proposing a variety of initiatives. President Bush's State of the Union speech voiced support for enhanced tax breaks for Health Savings Accounts in order to reduce the impact of rising health care insurance premiums. Maryland's state legislature recently mandated that companies employing over 10,000 people spend at least 8% of their payroll on health care or pay the difference to the state. Time will tell if any legislative initiatives can help companies and employees deal with the rising costs of benefits, especially healthcare.

In this newsletter, we suggest that to reduce tension between management and the work force is education as to the complete cost of an employee benefits package. We witnessed the Employee Benefits Worksheet serve as an effective tool in educating employees as to employer cost, and hence, enhance employee's understanding of their total compensation. Employees are aided by seeing both sides of this subject.

Most insurance providers offer summarized employee-benefits overviews in the form of personalized profiles for employees. However, we recommend employers consider a customized, interactive approach by which the employee calculates the value of his or her benefits package. By design, this approach results in greater insight and hoped for "buy-in", under the theory that a self-calculated value is more convincing than management's presentation of data. Additionally, the exercise requires employees to focus on the calculation. Below, we have provided a cursory template complete with example data and a line-by-line explanation.

	<u>Hourly Rate</u>		<u>Annual Hours</u>	=	<u>Base Annual Earnings</u>	<u>As a % of BAE</u>
Base Annual Earnings ("BAE")	\$20.19	x	2080	=	\$41,995	
Plus:						
"A" Unemployment Insurance	(BAE x .01)		\$420			1.0%
FICA (Social Security)	(BAE x .0765)		\$3,213			7.6%
Workers Comp Insurance	(BAE x Factor) ⁽¹⁾		\$575			1.4%
Sub-Total			\$4,208			10.0%
"B" Medical Insurance (Employer Portion Only)			\$3,826			9.1%
<i>(Enter amount based upon coverage that you have in the table below)</i>						
Medical Insurance Cost Table						
		<u>\$500 Ded.</u>	<u>\$250 Ded.</u>			
Employee Only		\$2,325	\$2,802			
Employee + 1		\$3,826	\$4,098			
Employee + Family		\$6,379	\$6,834			
"C" Paid Holidays			\$1,454			3.5%
<i>(hourly rate x 72 hours, or 9 days)</i>						
"C" Paid Vacation			\$2,423			5.8%
<i>(use multiplier as shown below – assume 2 weeks)</i>						
Paid Vacation Cost Table						
Number of Weeks		<u>2</u>	<u>3</u>	<u>4</u>		
Hourly Rate x		80	120	160		
"C" Paid Sick Days			\$808			1.9%
<i>(hourly rate x hours taken – assume 5 days)</i>						
"D" Contribution to 401k			\$840			2.0%
<i>(BAE x .02)</i>						
"E" Safety Clothes, Shirts, etc.			\$150			0.4%
"F" Training & Education / Internal			\$250			0.6%
Total Benefits			\$13,958			33.2%
TOTAL COMPENSATION & BENEFITS PAID BY COMPANY			\$55,953			133.2%

Note: ⁽¹⁾ This factor is provided by the insurance company and fluctuates based upon occupation, claims history, etc.

- A. These contribution amounts are mandated by the federal or state government and, consequently, are non-negotiable. These amounts are included: i) because they are employee benefits, and ii) to allow the employee to see their “total cost” to the company.
- B. These amounts are from the insurance schedule and represent the amount of the medical insurance premiums paid by the employer in a variety of scenarios. For the example worksheet above, “Employee + 1 with a \$500 deductible” is the case selected.
- C. All of the costs for nonproductive time are annotated in the section – holidays, paid vacation and sick days. These items are broken out as benefits because the employer is paying the employee for nonproductive time.
- D. In this example, the Company is “matching” up to 2.0% of contributions to an employee’s 401k plan.
- E. The Company pays for safety glasses, uniforms, etc.
- F. The Company pays for internal education programs, such as annual safety and quality control training.

As managers and a majority of employed persons are aware, an employee’s comprehensive cost far exceeds his or her hourly or gross annual wage. It is important that each employee be reminded at least annually of their “total benefits” and, hence, their total costs to the organization. In light of the rising cost of benefits, and in particular employee-sponsored health care plans, the Employee Benefits Worksheet is a tool to aid management and employees develop enhanced visibility of these costs which are developing into complex economic and social issues.

Café Adobe

After a highly successful twelve-year relationship, Catalyst/Hall (“CH”) recently exited its investment in the Café Adobe restaurant chain with Café Adobe’s redemption of CH’s limited partnership interests. Dating back to the purchase of Café Adobe #1 in April 1994, CH’s collaboration with Café Adobe’s management and partners demonstrated how to successfully execute a “buy and build” strategy with capable partners who were focused on building long term enterprise value.

“C/H’s experience with the management team of Café Adobe illustrates a few aspects of our firm that we attempt to perpetuate – our willingness to form long term partnerships and our acceptance that some companies reach a point of maturity where the benefits of risk capital and our participation diminish. It’s all about forging “win-win” partnerships.” *Ron Nixon, Catalyst/Hall Principal*

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