

Talent & Labor Based Compensation

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North American Chief Financial Officer, Leo Burnett Group

A handwritten signature in blue ink that reads "Leo Burnett".

Wednesday, February 15, 2012

Continuing the discussion of "getting paid what we are worth" through focusing on the unfortunate conversations we as an industry currently find ourselves having on the topic of Talent & Labor Based Compensation.

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Stonestreet Studios 1927



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91%

Source: AAAA's Hourly Billing Rate Survey

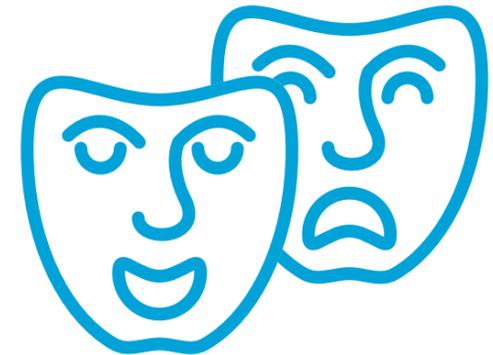
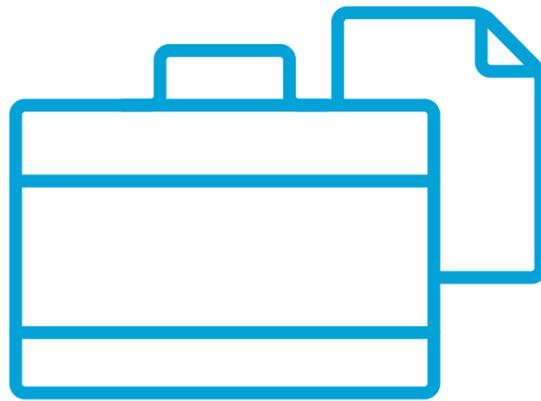
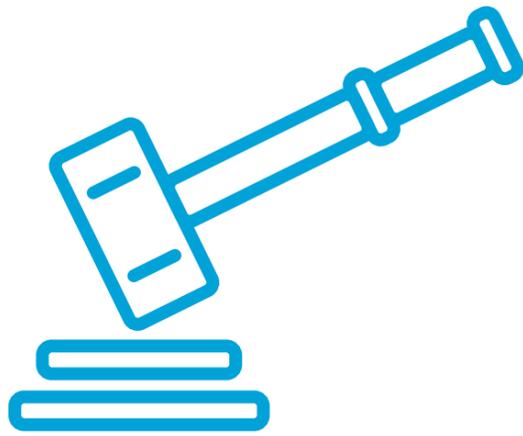
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Are we doing our very best to ensure we get paid, as agencies, for what we deliver to our clients.

As we look back it may seem silly that Walt Disney would ever be asked to sell his remarkable creativity based simply on the hours he spent creating Mickey Mouse, but the reality today is 9 out of 10 agency proposals 91% are prepared in exactly that way.

So we better be smart about the way we do it and devote as much talent to the process as we do any other client engagements we have in the agency...

Compared to others, agency costs are highly scrutinized



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There's another painful reality to our industry.

Compared to other similar industries - like accounting, legal, consulting and even scale talent - we as agencies are far less standardized in our approach to compensation and therefore more scrutinized.

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Increasingly, clients and consultants are forcing us into agency cost conversations at the "component" level.

This, in my humble opinion, is a real cause for concern that we need to more aggressively address.

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Thou shalt love thy Labour

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Now, there are several key components to cost. Overhead (or indirect cost as I like to call it) and Profit (which I just plain like!) are two very important components my colleagues will discuss later.

For the balance of my time up here, I'd like to focus on the other critical component to agency cost. Labour.

Perhaps the most important "cost component" in our business as it represents our most valued asset. PEOPLE.

So, we should love it every bit as much as the ideas that labour produces.

And, yes, it's spelled with a "u". I'm English!

The way they want
to pay for it is not
the way we want to
charge for it

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So, what's the first reality we need to understand about the cost of agency labour?

There seems to be a fundamental difference between the way clients want to pay for it and the way we feel we should charge for it.

The truth is, I loathe "FTE's, Hours and OH" discussions. I prefer to focus on scope, deliverables and the value we create.

However, today's reality is we have to manage the transition. So, let's prepare...and it starts with...

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We must control the conversation

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Controlling the conversation.

If we don't, the chances are you'll not get what you deserve.

Have your agency approach for compensation and specifically labour discussions, agreed and embraced by your agency.

Enter the first discussion clearly selling how you want to be paid.

Without a strong kick-off, the conversation with clients and consultants could be something like this...

CLICK

Source: Bill Connoly

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So to help you prepare your agency point of view...

[CLICK](#)



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So to help you prepare your agency point of view...

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3 Traps to Avoid

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Let's talk about what it takes to truly control the labour conversation and be assured you'll get what you deserve.

And I am going to summarise them down into 3 Traps to avoid and some final thoughts

1

Definition

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The first is simply choosing to define labour in the best possible way.

direct
salary

+

benefits

= labour

+

taxes

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It is my feeling that labour be defined as the sum total of direct salary, benefits and payroll taxes. That is, the true cost of agency employees.

In the world today, we'll see increased burden of benefit costs for employers such as healthcare and payroll taxes. So, making these components the cost of an employee keeps the conversation real and principled.

Why is this definition of labour critical to being paid what we deserve? Clients today are trying hard to define labour as simply direct salary. They want to separate benefits and payroll taxes from labour and consider that part of our overhead discussion...part of the compensation equation that is already over ratio'd

If we allow them to do that we lose on the multiplier effect I'll discuss in a moment. Suffice it so say, by not including benefits and payroll taxes in our labour cost we simply won't earn the profit we so rightly deserve.

As I mentioned earlier, this level of scrutiny seems to only be prevalent in our industry. I've yet to hear of an accounting, legal or consultancy firm being asked to break down their rates.

2

Multiplier

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The second recognizes the trend I'm seeing in compensation discussions. Ratios are being misused and misquoted to lower our compensation.

	Option A Salary Only	Option B Salary, Taxes & Benefits
Direct Labour	\$75,000	\$95,400
Multiplier	2.90	2.28
Revenue	\$217,882	\$217,882

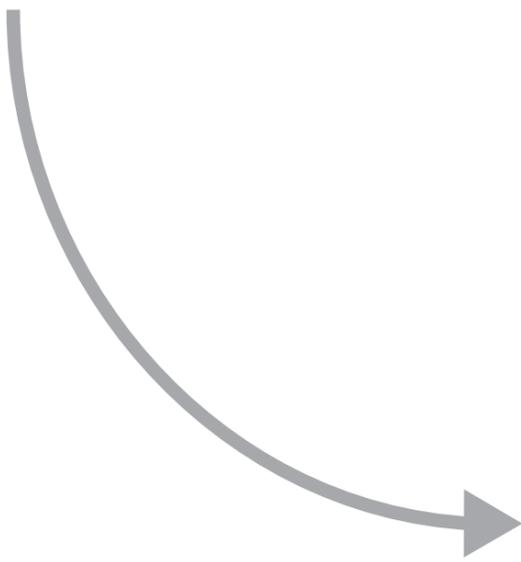
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Both A and B are selling the same employee with a base salary of \$75K. Both should yield us revenue of approximately \$218K. The only difference between A and B is the numerical articulation of what I share with you in Trap 1.

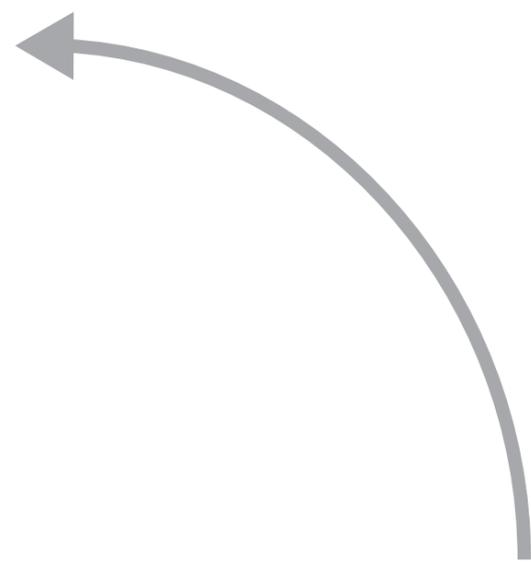
And what I know is certain is that one of these options is certainly easier to defend...why Indirect cost ratio is less than 100%

Then comes the multiplier effect. And this is purely the ratio of direct labour to revenue

\$75,000



**\$47K
Loss**



2.28

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So, here's what I've personally witnessed

Consultants picking the lower labour cost of option A and using the multiplier from option B to lower the revenue they pay us by \$47k...that is pure profit!

3

Utilisation

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The third trap, is quite frankly, us as employers, giving up control over our employee's hours.

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2,000

\$218K

Utilization Rate

1,550

1,800

2,000

Hourly Rate

\$141

\$121

\$109

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So first thing is in case you cannot tell...I don't support 2000 hours not only does it have the consequences we just discussed but it also just cheapens / devalues the hourly cost of our employees...and you all know how the value of our ideas and are not equated to cheaper hourly rates

my personal view is that 1550 hours should be the time we should expect to recover fully the appropriate revenues for every client direct employee

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So another trend and damaging demand being made of our industry is that every employee should working 2000 hours directly on client business....so what does this mean...

It means we need to ask / expect the following annual hours commitment from each and every client facing employee

So their standard year has to look something like this.....

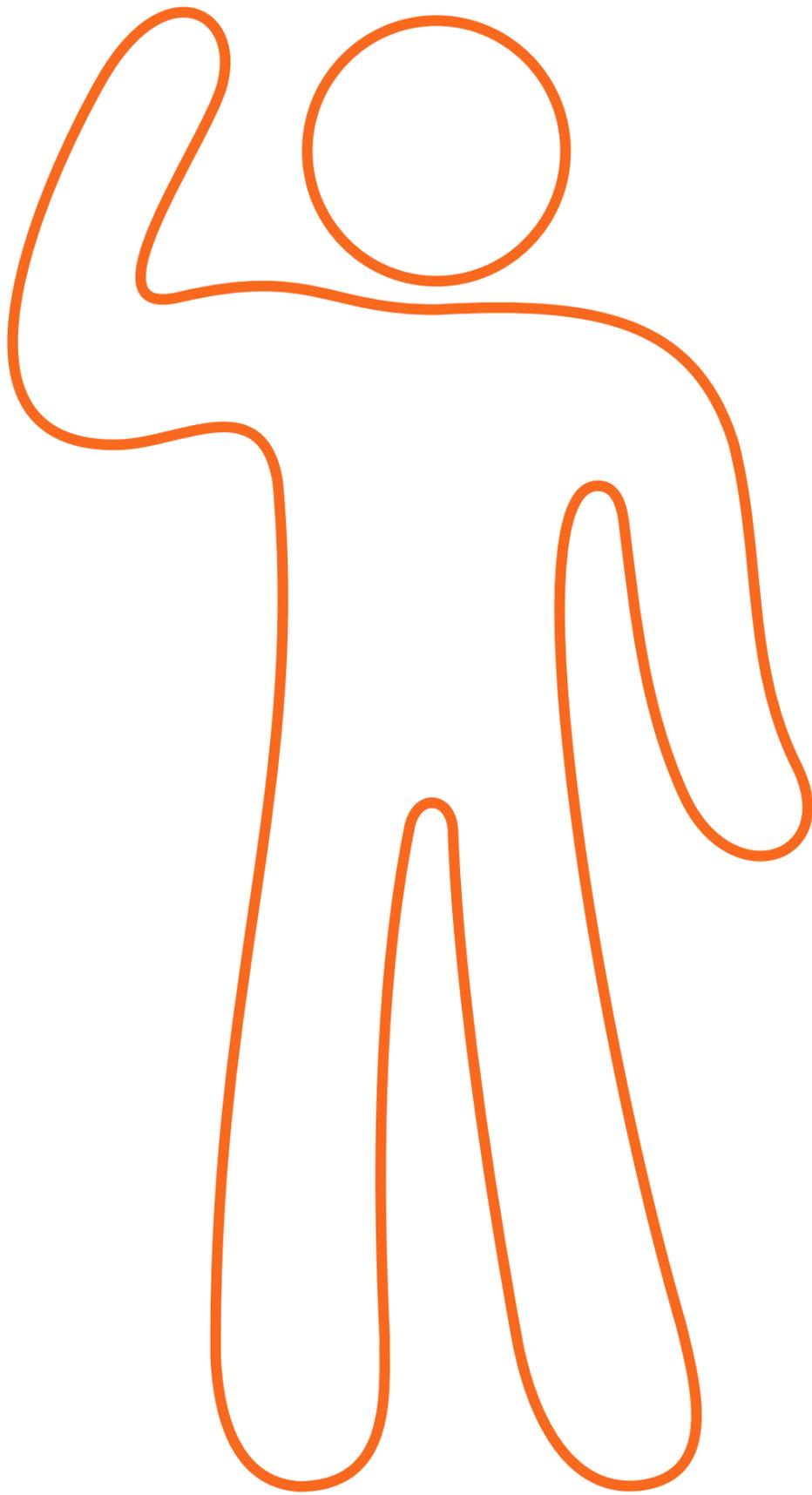
203 hours = holiday + vacation

35 hours = Sickness / Family leave

35 Hours = training

105 Hours = Agency Activities

2000 hours the client demand! giving a total of 2378 hours



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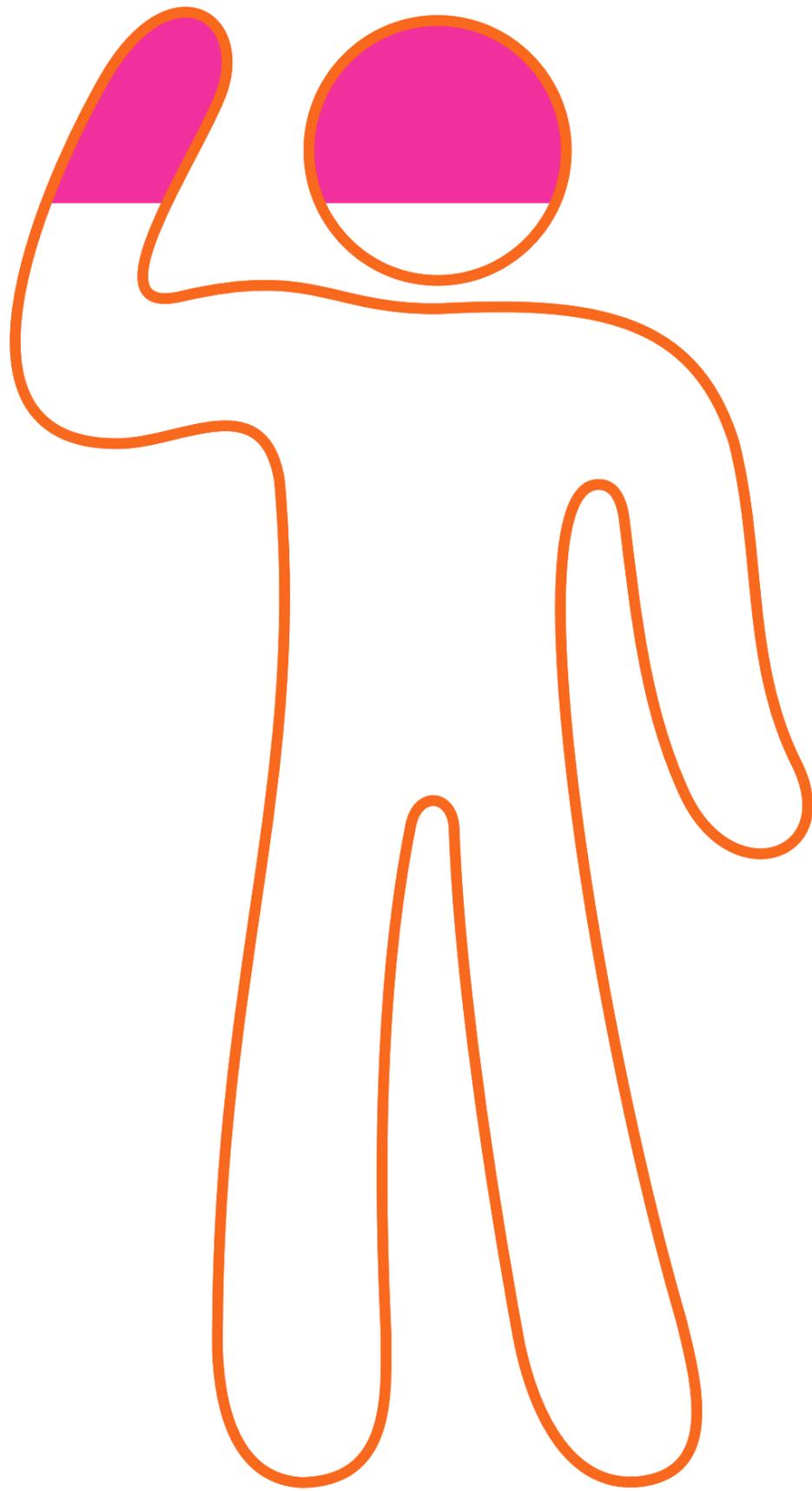
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Holidays and Vacation



203

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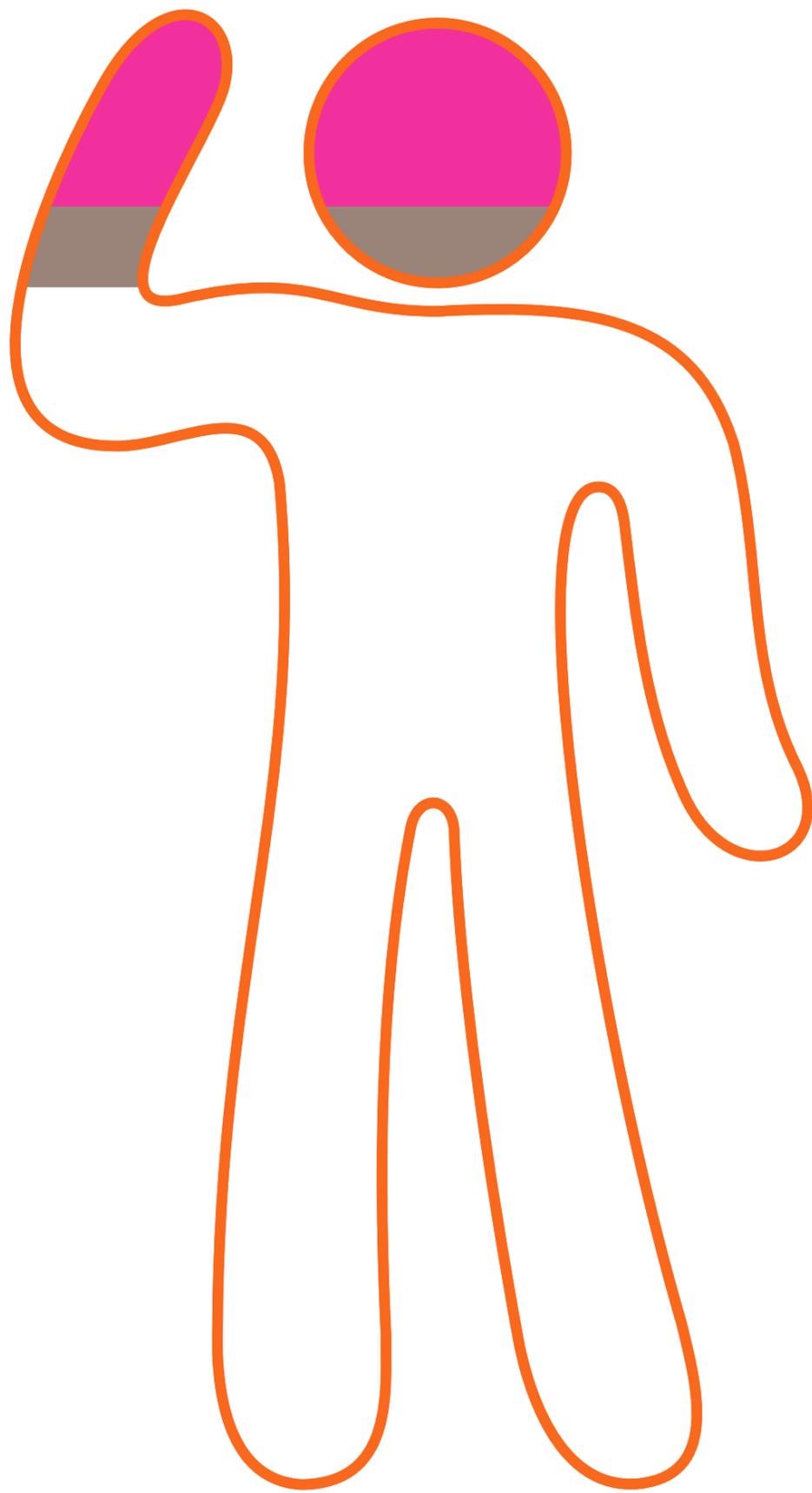
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Holidays and Vacation

Sickness and Family Leave

238

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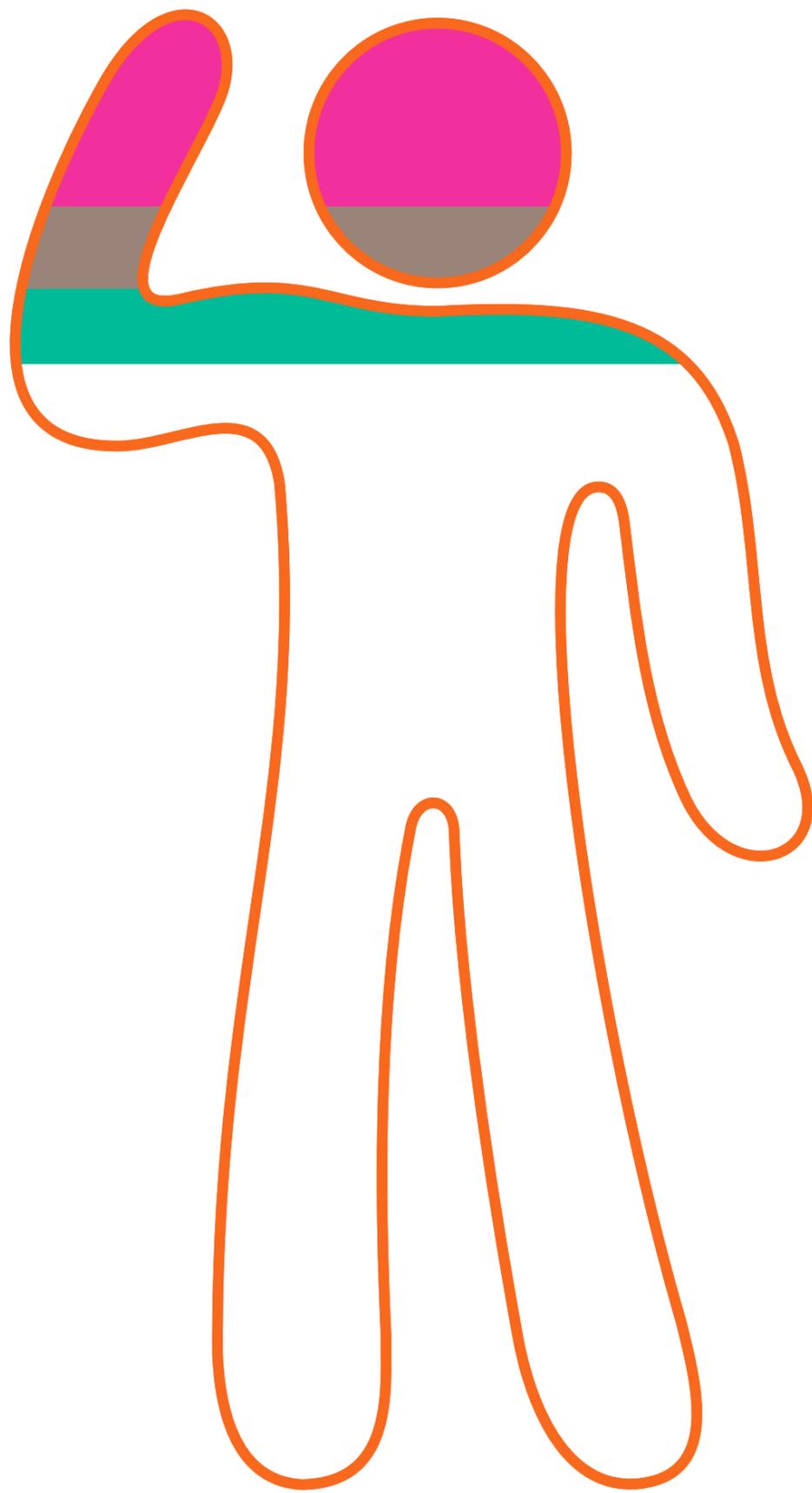
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Holidays and Vacation

Sickness and Family Leave

Training and Development

273

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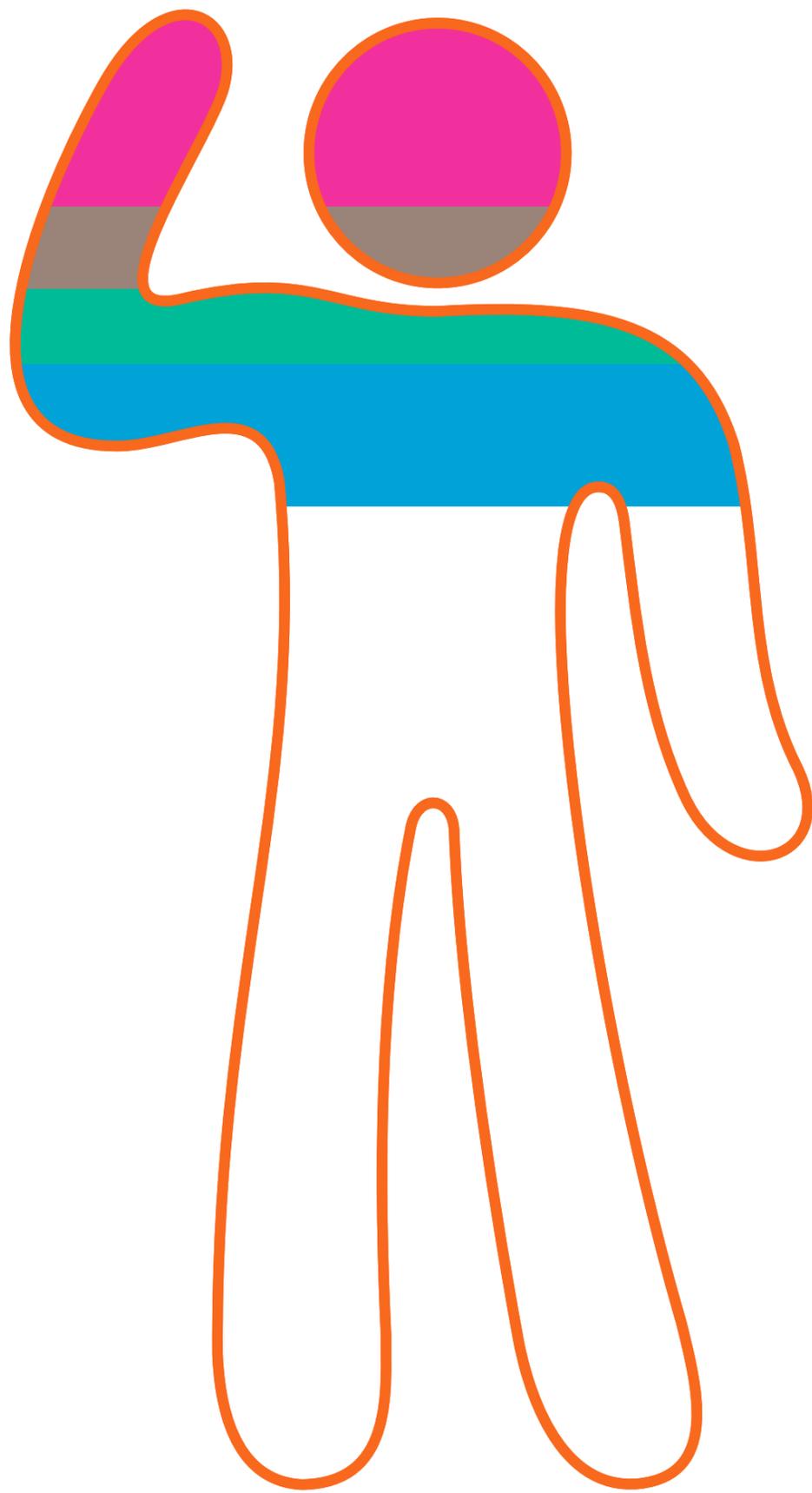
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Holidays and Vacation

Sickness and Family Leave

Training and Development

Agency Activities

378

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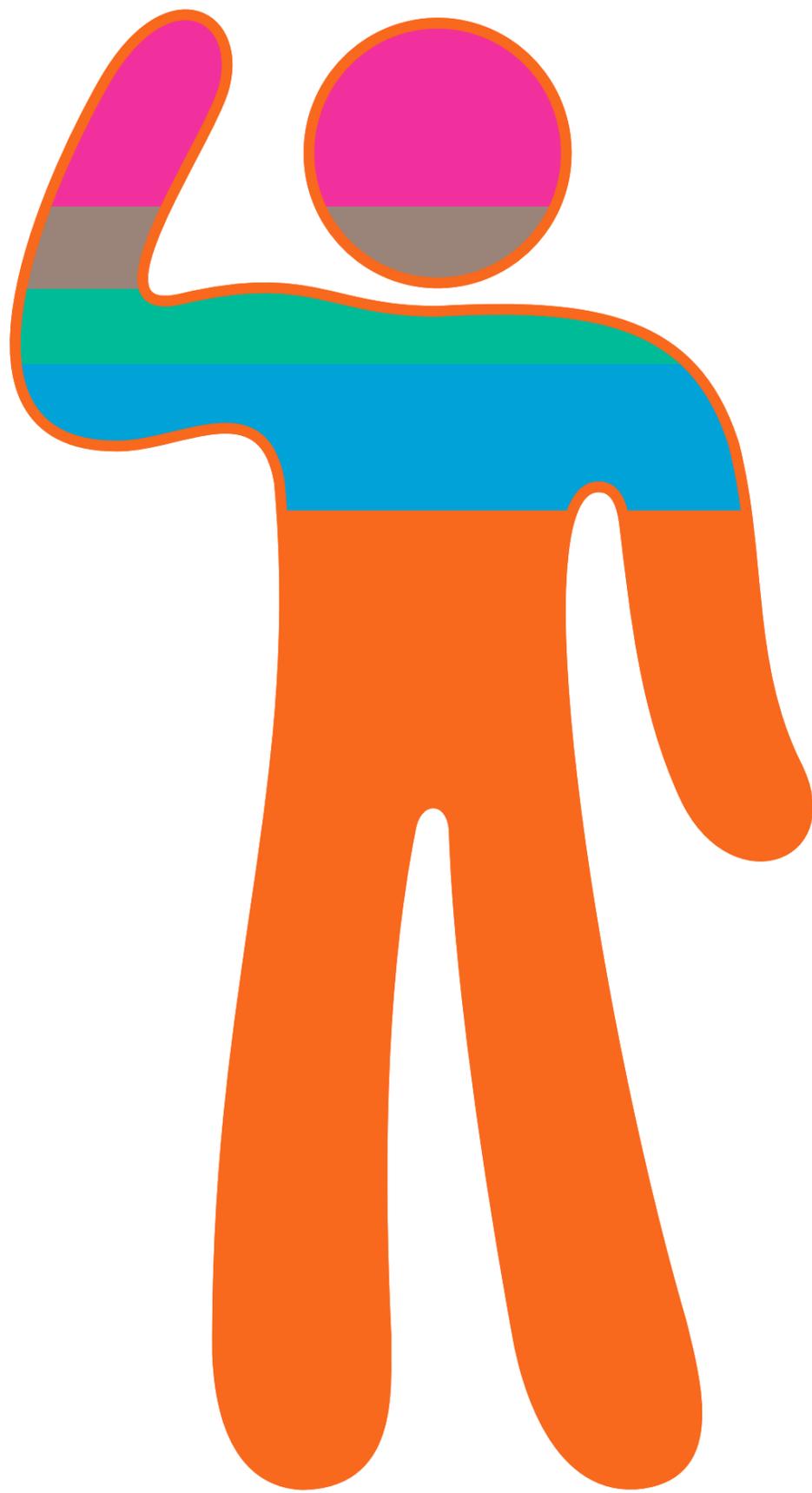
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Holidays and Vacation

Sickness and Family Leave

Training and Development

Agency Activities

Billed Hours

2,378

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In Summary

- 1. control the conversation**
- 2. the right talent to negotiate**
- 3. a consistent methodology & training**
- 4. labour defined before overhead rate**
- 5. less info is more**
- 6. focus on selling scope of work**

Thanks

Leo Burnett