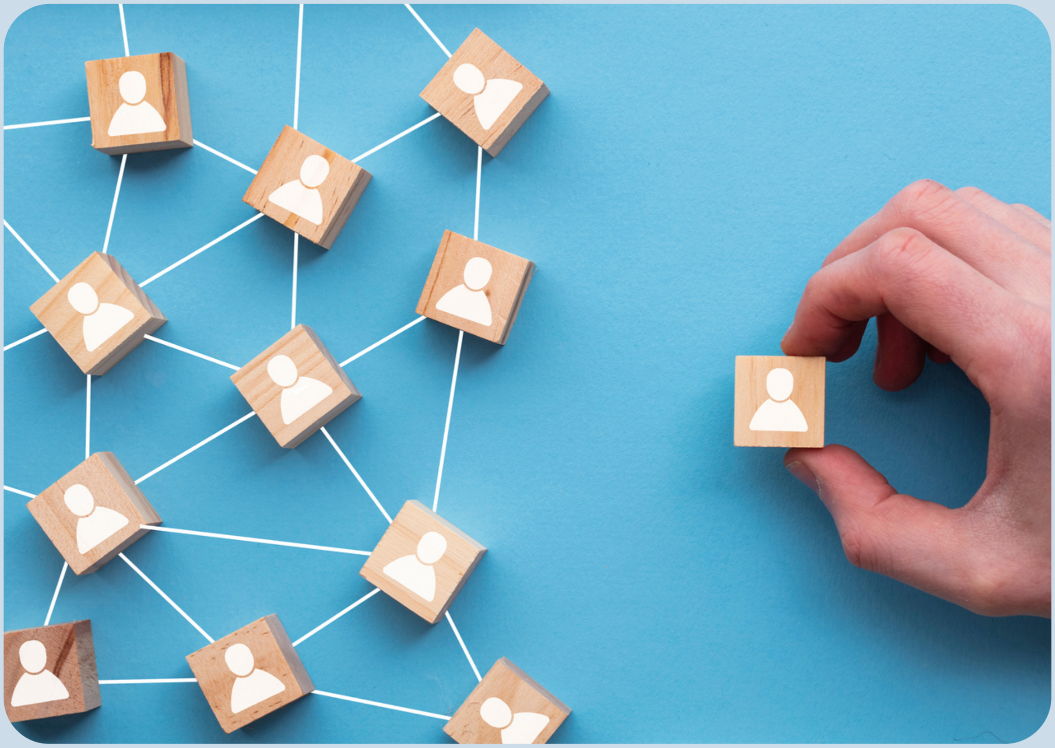
How to Afford Your First Hire

A 5 Step Worksheet to Organize Your Finances



Introduction

Pricing is all about making sure you can afford your overhead while still turning a profit. To plan for future growth, you need to have enough profit (or enough savings) to hire someone before they start bringing income to your company. In this worksheet, we're going to look at the cost of bringing on different types of staff.

Note: This worksheet is designed to help you determine a baseline cost for hiring an individual employee. It does not cover company-wide expenses such as a payroll company or changes to your insurance. Since these expenses can vary widely, you should always talk to a financial professional about any questions you have regarding your budget and hiring plans.

Terms

Revenue

The total amount of money you made during this period.

Profit

The amount of money left over after all expenses, including wages and cost of sales.

Gross Profit

Your revenue minus any expenses that occur on the job site.

Net Proft

The amount of money you make in a given period after you have paid all of your overhead expenses.

Overhead Expenses

Expenses that you have to pay whether or not you do any jobs. They often include things like rent, insurance, and software subscriptions.

If you're a small business owner, you may be paying yourself out of your profits, or you might have hired yourself as a W-2 employee. However you pay yourself, make sure that you're subtracting that amount from your revenue numbers.

Type of Hires

Hire Type 1

People who contribute ***directly*** to your revenue through

- Work that is billed directly to a client
- Work that brings in new clients

Examples of this might include hourly staff who work on a job site or an additional salesperson.

Hire Type 2

People who contribute ***indirectly*** to your revenue through

- Work that is not billed directly to a client
- Work that increases your efficiency
- Work that increases the number of clients your company can handle

Examples of this might include an office person who handles administrative work or builds the schedule.

This worksheet will help set your pricing to afford both types of hires.

Step 1: Determining Your Profits

Start by pulling up your recent sales, and list your revenue for the following periods. If you aren't sure, add up your invoices for that period, or check your accounting software if you use one. If you haven't been in business for a year, use whatever length of time you've been in business.

	Last Week	**Last Month**	**Last Year**
Total Sales and Revenue			

List your ***gross profit*** for the same periods. If you're not sure how to find this, look at your invoice for the period, and subtract the amount you spent on each job from the amount you made on each job. This gives you your gross profit per job. Add all jobs together to get your total for a given period.

	Last Week	**Last Month**	**Last Year**
Total Gross Profit			

Last, let's list your ***net profit***. Subtract your overhead expenses from your gross profits for an accurate picture of how much money you have to spend on a potential hire.

	Last Week	**Last Month**	**Last Year**
Total Net Profit			

Note: If you're a small business owner, you may be paying yourself out of your profits, or you might have hired yourself as a W-2 employee. However you pay yourself, make sure that you're subtracting that amount from your revenue numbers.

Also, make sure that you're accounting for expenses that may not come every month, such as quarterly taxes or insurance premiums.

Step 2: Determining Potential Pay Rates

Now let's think about what positions you might want to hire for. List them below, along with local pay rate and whether they're directly or indirectly contributing to your revenue. We'll walk through both types of positions in this worksheet, so don't worry if you have more than one type.

Position	Pay Rate	Time Period	Direct/Indirect
Example: Office Assistant	\$12-\$15	Per Hour	Indirect
Example: Project Manager	\$50,000	Per Year	Direct

Note: If you're not sure how much a given position pays, you can check your local industry job board for similar positions. If there's a wide range, pick the average. At this point, we're not looking to budget for specific positions. You are just getting a feel for your finances.

Step 3: Employee Payroll Costs

For this section, we're assuming that you are hiring an employee. Skip to the next section if you're hiring a 1099 contractor.

If you're hiring an employee, there are also some non-payroll costs to consider. The two biggest expenses are:

- Employer's share of Medicare/Medicaid and Social Security taxes
- Workers' Compensation Insurance

We'll start with ***taxes***. As of April, 2023, the employer rate for Medicare and Social Security taxes is 7.5%. Add this cost in by multiplying your pay ranges by .075. This will give you the amount you'll need to pay to the federal government for these taxes.

Position	**Pay Rate**		**Tax Rate**
Example: Office Assistant	\$12-\$15	X .075	\$0.90 - \$1.13
Example: Project Manager	\$50,000	X .075	\$3,750
		X .075	

Next, let's think about ***insurance***. For many companies, Workers' Compensation is their most expensive form of insurance. Not all states require Workers' Compensation Insurance, but many do. Even if your state doesn't, consider purchasing it anyway. If an employee is hurt on a job site and you don't have insurance, you could be paying their medical bills out of pocket.

Workers' Comp is usually calculated as a percentage of payroll, so the cost depends on how much you pay and what type of work the employee is doing. Every industry is different, and you'll have to check with your specific insurance company or broker to see what your costs will be.

For the sake of simplicity, use the following numbers:

- Add 1% for any office, retail, or non-specialized work. (Multiply pay rate by 0.01)
- Add 5% for any food service, food prep, or work regularly involving outdoor work or hand tools. (Multiply pay rate by 0.05)
- Add 12% for any work involving regular use of power tools or heavy machinery. (Multiply pay rate by 0.12)

Let's find your estimated Workers' Compensation Rates

Position	Pay Rate	X WC Rate	WC Cost
Example: Office Assistant	$12-$15	X .01	$0.12 - $0.15
Example: Project Manager	$50,000	X .05	$2,500

Great! Let's add it all together.

Position	Pay Rate	Tax Rate	WC Rate	Total
Example: Office Assistant	$12 - $15	$0.90 - $1.13	$0.12 - $0.15	$13.02 - $16.28
Example: Project Manager	$50,000	$3,750	$2,500	$56,250

So the total cost for hiring an office assistant who makes $12 - $15 per hour is $13.02 - $16.28. The total cost for a project manager is $56,250 per year. These are the numbers you want to use for calculating your hiring budget.

Step 4: Determining Hiring Cost Per Month

Now that we know how much each employee will cost, we want to see how that fits into your budget. If you're hiring a 1099 contractor, you'll use the original pay rates you wrote down in Step 2. If you're hiring a W-2 employee, you'll use the Adjusted Pay Rates you created in Step 3.

For each position listed above, create a monthly pay rate. If someone is being paid hourly, how many hours per week would you expect them to work? Multiply this number by 4.35, the average number of weeks per month. If it's a salaried position, divide your yearly salary by 12 to get the monthly rate.

Hourly Positions

Position	Total Pay Rate	X Hours Per Week	x4.35	Total Monthly Pay
Example: Office Assistant	$13.02 - $16.28	10	x4.35	$566.37 - $708.18
			x4.35	
			x4.35	

Salaried Positions

Position	Annual Salary	÷12	Total Monthly Pay
Example: Project Manager	$56,250	÷12	$4687.50
		÷12	
		÷12	

Step 5: Putting it All Together

Now let's see if you can afford to hire. Let's look at your profit for last month. Subtract your total monthly pay from your profits. If you are hiring an employee who **DIRECTLY** contributes to revenue, you want to look at your **GROSS** profit numbers. If you are hiring an employee who **INDIRECTLY** contributes to revenue, you want to look at your **NET** profit numbers.

This is because if an employee is directly increasing your revenue, they're covering their own paycheck, plus extra for overhead expenses. If an employee is not directly contributing to revenue, you'll have to pay for their work as part of your overhead expenses.

Note: If you are a seasonal employer completing this worksheet in the off-season, you can use a different month that makes more sense for you.

In this example, we're going to assume that the same company is hiring both an office manager and a project manager, so we'll use the Net Profit number from the above table to determine whether we can afford the office assistant.

Staff Directly Contributing to Revenue

Position	Gross Profit for Month	Monthly Pay Rate	Net Profit Remaining
Example: Project Manager	$10,000	$4687.50	$5312.50

Staff Indirectly Contributing to Revenue

Position	Gross Profit for Month	Monthly Pay Rate	Net Profit Remaining
Example: Office Assistant	$5312.50	$708.18	$4604.32

So...Can you hire?

Look at your remaining net profit in the last step. Is this number positive? If your net profit is a positive number, and you can cover any expenses that weren't accounted for in this table, then
YES! Congrats!

But what if the net profit number is negative?

Generally, if this number is negative, you can't afford to hire yet. In that case, think about some ways that you can increase your sales or reduce expenses to be able to afford that person. So how can you get there?

Let's go back to the numbers. If you hired a person who could contribute directly to your sales, how much more revenue would you need to make in order to cover their paycheck and your payroll expenses? If you wanted to hire someone who indirectly contributed to your revenue through greater efficiency, how much additional revenue would you need? Once you know these answers, you can make a plan for how to achieve those goals.

The only exception to this rule is if you have savings or outside investment that can cover the cost of your new hire as your business grows. In that case, you're gambling that by the time your savings run out or your investment loan comes due, you'll be making enough money to cover your expenses. If you're thinking about going this route, be sure to consult with a financial advisor or business mentor to make sure that you'll be able to meet your future goals.

Thank you for downloading our How to Afford Your First Hire Worksheet!

This worksheet is not a fool-proof pricing plan, and you should always consult with a qualified accounting professional if you have questions about your business finances. For more detailed activities and courses, go to www.outgrowyourgarage.com for current offerings.

A downloadable spreadsheet of this worksheet is available as part of our Hiring Staff and Contractors Course.

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