

# Payroll Tribune

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## Budget for 2011

**There is a lot of uncertainty in the air.** The headlines don't help: unemployment, the effects of deleveraging (foreclosures, troubles with mortgage backed securities, lots of liquidity but little demand for loans, currency and trade battles). Fewer companies, fewer employees, fewer checks, lower interest rates, that's enough to take the fun out of payroll and H/R services!

**BUT,**

The rest of the story is that GDP will grow 2% and the private sector will continue to product more jobs. Interest rates will remain low and banks will continue to increase fees and seek to decrease risk (meaning that some will get out of doing ACH processing for payroll service bureaus).

**SO,**

Bureaus need to **get more efficient**, have the courage to **press through modest price increases**, and get very serious about **adding new sources of revenue** to their product offering.

Every year I get the question, "**why should I create a budget?**" Each year my answer is the same: Pogo and self-interest. Or, if you don't know where you are going, then any road will take you there. And, whether it is your domestic partner or a potential buyer, they are not just interested in what you did, they are actually interested in seeing if you did what you said you were going to do. Budgets are roadmaps. They tell the world what you planned and whether you could execute your plan. In times of uncertainty, they help tell you that you need to change your behavior, and help you test alternatives.

In times of uncertainty, it helps to diversify. Our bureau survey this year showed that the major players now got just 75% of their revenues from payroll services, and 25% from H/R services, insurance products, and retirement plan administration. They got more revenue per current customer by selling that customer more services that the customer wanted. The vast majority of independent service bureaus got more than 95% of their revenues from payroll services alone, and that interest income was down more than 65% over the last two years.

**Consider the following in budgeting for 2010:** **1.** Compare your operating ratios to industry standards, **2.** **Double the percentage of your revenue which comes from non-payroll sources.** In general, the first will help you manage your costs more effectively, and the second will help you grow and diversify your revenue. **3.** Plan a 10% increase in your check volume. You should plan on increasing your sales efforts to both new customers and to existing customers. **4.** You should review the risks that you are running in your operation. You can control some of them, others are beyond your control, but you still must react to them. The first include: the status of your internal controls, your reliance on certain employees, and the security around customer transactions. The second include: reliance on suppliers and customer concentrations, and the effects of regulatory changes.

We will post some key operating ratios on our website at [www.henshawvierra.com](http://www.henshawvierra.com) . I am happy to talk to anyone about these budget guidelines. E-mail me at [guy@henshawvierra.com](mailto:guy@henshawvierra.com). Let's see if together we can help you grow your business in a difficult, but by no means dead economy.

## How can you build value in your service bureau?

The good news is that recessions affect companies that provide necessary key business services less than they affect other businesses. More good news is that in a slow or deflationary environment, businesses which produce annuity style cash flow remain in demand.

Payroll service bureaus with a loyal customer base and a broad service offering remain valuable assets, even in this market.

**The value of a service bureau comes from two general sources:** the discounted present value of a predictable cash flow, and the value of the customer list assigned by the buyer. In many cases the buyer looks at the cost of acquisition versus their cost of gathering the same number of customers by their sales efforts and factors in something for the value of having the customers on the books now versus waiting to acquire them internally.

**What are some practical things that you can do to increase the value of your company?** Here are five things you can start with:

1. **Do your company no harm**
2. **Build long term relationships with your customers**
3. **Keep pricing simple**
4. **Show consistent revenue growth and increasing margins**
5. **Create and use a budget**

*You harm your company when you take unnecessary risks* like: not managing your fiduciary obligations through tight controls and daily balancing to the customer level; under pricing your services for short term competitive gains; poor training of your staff in payroll and customer relations.

*Building long term relationships is what independent payroll companies do well,* and larger firms have difficulty with. Long term relationships result in long term demonstrated cash flows. The half life of a stream of cash from a customer base with an attrition rate of 20% is just over 3 years. The half life of a stream of cash from a customer base with an attrition rate of 5% is just over 13 years. Look hard at the attrition rate of a buyer. They will impute their rate into their offer. It is worth the effort to find the right buyers.

*Keep pricing simple.* Many bureaus use too many pricing tables. Some have 50 or more. Two or three will allow you to verify the average price a buyer can expect to apply to your customer base.

Part of your job as a seller is to be able to *convince a buyer that what they see is what they get.* A steady growth in sales shows that your company competes well in your marketplace. Long term relationships show that your level of service is good. Keeping pricing simple helps demonstrate that customers are paying what you are asking. Together they go a long way to showing predictable cash flows, and an increasing customer list.

*Finally, create and use a budget.* Running your company by looking in the rearview mirror (comparing this year to last) is not an effective way to convince a buyer that you know where your customer base and cash flows are going. Having and using a budget over multiple years, managing the variance between actual performance and budget show that you can plan, you can manage, and you can do what you say you can do.

## HENSHAW / VIERRA MANAGEMENT COUNSEL LLC

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Let our experience in payroll and in banking help you plan for credit risk reduction, security risk reviews, and possible regulation of payroll.

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