

MUHLENKAMP Methods

Answers to questions you may not even know you have.

WHEN WE CHANGE THE RULES A LITTLE...

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One of our favorite maxims is, “When we change the rules a little, we change the game a lot.” We find this maxim applies in many areas of life, from games—different versions of pinochle—to sports—no helmet contact—to economics.

We’ve maintained for the last three years that employers were reluctant to invest and hire because “no one knows what the rules are.” This has been particularly true since the Patient Protection and Affordable Care Act (Obamacare) was enacted into law. Even after enactment, it was challenged legally before the Supreme Court, and politically in last year’s election.

Frankly, I think the mindset in Washington discourages businesses from growing and hiring. For example, while it has since been removed, the Patient Protection and Affordable Care Act originally contained a provision that outlined 2012 tax guidelines for businesses. All businesses would need to issue a 1099 to any vendor to whom it paid \$600. Think about that from a personal level. Suppose you had to report to the IRS every business with which you spent \$600—every grocery store, every gas station, every utility, (cable TV, telephone, gas to heat the house...). Wouldn’t that change what you do? Every plumber, every carpenter, and every electrician—people who hate bookkeeping—thought so, and demanded the proposed burden be removed!

The point being, government officials wouldn’t dare do this to households because such legislation would also be thrown out! Somehow, however, businesses are treated differently than individuals—even though half of the commerce in this country is small businesses: hairdressers, barbers, plumbers, and electricians...

Meanwhile, the American consuming public, faced with higher unemployment and declines in market prices of both homes and equity investments in the 2007-09 recession, chose to save more and spend less. The resulting slow economic recovery (GDP growth of 2%-3% since 2009) allowed businesses to fill their needs primarily through gains in productivity. They’ve been able to postpone buying capital goods and hiring people. As a consequence, four years after the economy bottomed in 2009, neither capital spending nor employment has returned to the levels of 2007. Recently—particularly with the elections—the rules have been clarified. The net effect: it will be even more expensive to employ people.

After three years of deferring decisions to buy equipment and hire people, employers now see increased costs for hiring. As an employer, after each yearend, we issue a W-2 form to our employees showing the deductions that were taken from their gross pay. Years ago, I realized that my employees weren’t aware of the amounts paid by the company (me) on their behalf. In particular, they were not aware of the amount paid for their health insurance which was growing faster than the other parts of their compensation. So we now provide the data shown on the following table:



Employment Costs 2013 (W-2 Filing: Married, Two Children)

Employee's Deductions		Employer's Costs	
Gross Wage	\$ 45,000.00	Gross Wage	\$ 45,000.00
FICA • Social Security (6.2%) • Medicare (1.45%)	\$ 3,442.50	FICA • Social Security (6.2%) • Medicare (1.45%)	\$ 3,442.50
Federal Withholding (4 exemptions)	\$ 2900.00	Health Insurance	\$ 21,430.80
PA State Withholding	\$ 1,381.50	PA State Unemployment	\$ 542.00
PA State Unemployment	\$ 32.00	Federal Unemployment	\$ 42.00
Local Services Tax	\$ 52.00		
Local Earned Income Tax	\$ 450.00		
Employee's Take-Home Pay	\$ 36,742.00	Employee's Cost to Company	\$ 70,457.30
		Pension/Profit Sharing Contribution ¹	\$ 11,250.00
		Employee's Cost to Company, including Pension/Profit Sharing	\$ 81,707.30

¹ Based on the maximum allowable contribution by the law: 25% of gross wages.

As you can see, for my employee to take home \$37k, it costs me \$70k—or \$82k, if I am able to fund profit sharing to the maximum. The new rules will add complexity and costs to employing people.

Under the new rules, some regulations kick in at the 50-employee level; other regulations apply to employees who work over 30 hours per week, but not to employees who work less than 30 hours per week. And, of course, regulations chew up time for both the consumer/employee and the business/employer. Have you noticed that government, at all levels, is willing to waste our time?

And on it goes...just as consumers/employees respond to incentives, so will businesses/employers. After three years of deferring decisions to buy equipment and hire people, we expect the number of employees to increase, but many of them will work less than 30 hours per week.

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