

IS LABOR FREE?

NOT AT YOUR SHOP. THEN WHY ARE YOU EFFECTIVELY GIVING YOUR LABOR AWAY?

BY CHRIS “CHUBBY” FREDERICK | CONTRIBUTOR

IN MY 40-plus years of helping shop owners become more profitable, typically the biggest pricing problem is labor margin. If you want to stay the best shop in your market, you have to be profitable enough to deliver the best experience today's customers desire, and that takes money. I was listening to Mike Bennett, a successful shop owner in Pennsylvania and an ATI coach, teach a class on solving the effective labor rate problem. He even created a work sheet you can use to understand how to accomplish it.

Bennett began by saying, “You have done the proper math. You have looked at the labor costs associated with the hourly rate you pay your techs. You've calculated in the appropriate tax and benefit load (matching taxes, workers' compensation insurance, health care costs, holidays, vacations, sick days, uniforms, training, etc.), needed labor margin and, of course, the productivity factor. You know the exact hourly shop rate you need to charge to make sure you can make the needed labor margin and a decent profit on your labor model. So, why is it that you never seem to get ahead?”

You are built for profit; you charge the hourly rate you should — or do you?

Calculating Effective Labor Rate

Let's look at it. Your hourly shop rate or “door rate” might be what you base your prices on, but your effective labor rate represents the actual or “effective” labor rate that you collect based on the hours your technicians produced.

A great example of this labor rate black hole could be an oil and filter service. Let's assume you collect \$14 for



labor as part of your \$34.95 oil-change service. Let's also assume you pay your technician a half-hour for the oil change service because “that's the time it realistically takes to perform the oil change as I want it done.” Well, if you are going to pay the tech 0.5 hour to do the LOF and \$14 is the labor dollars you collect for the service, then effectively your labor rate on the oil and filter change service is \$28 an hour.

Now, we all know that an oil and filter change service is a necessary evil, a “lost leader” if you will. You try to minimize the damage by putting your less skilled and lower cost techs on the job. They don't cost you \$14 a half-hour, so you're not necessarily losing money. The fact remains that the poor labor markup or low effective labor rate is still part of your total profit model.

The simple math to calculate effective labor rate is labor dollars collected divided by the labor hours turned. Perform enough of these low effective

labor rate services in a given week, even when combined with all the jobs you collect your full labor rate on, and your overall effective labor rate certainly will be lower than your “door labor rate.” The same can apply for state inspections, a smog check or any job that has “a special labor rate for some maintenance-related jobs that I need to be competitive on.”

Another huge black hole in your effective labor rate bucket is diagnostic time. Do you “waive” the diagnostic charge if the customer approves the repairs? Well, you have labor time that was associated with the diagnostics. Certainly your flat-rate tech isn't going to waive his billed time involved with the diagnostics, and you can't miraculously make the time your hourly tech invested in the job disappear. You can make the charge disappear, but not the time investment. This is a huge blow to your overall effective labor rate. Even for that hourly technician

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“WHAT IS THE BENCHMARK FOR EFFECTIVE LABOR RATE? THE KEY PERFORMANCE INDICATOR WE USE SHOULD BE NO MORE THAN A 10 PERCENT SLIP FROM YOUR DOOR RATE.”

CHRIS “CHUBBY” FREDERICK [ATI CEO]

you have to consider the opportunity cost. If you are giving away their time, but you figure it's not costing you anything extra, how many dollars in labor could they have produced if they worked on a job you can charge your rate for?

The ATI benchmark for effective labor rate (ELR) is no more than a 10 percent slip from your door labor rate. This is a critical Key Performance Indicator (KPI) for measuring the effectiveness of your labor model, which would include all of your canned and menu services as well as all your estimated mechanical services and diagnostics. Like anything in your business, if you can measure it, you can manage it.

In an effort to measure this critical KPI accurately, it would make sense to track your actual billed hours. Do not just calculate billed hours by dividing labor sales dollars by your advertised door labor rate. This would end up with false numbers for the labor hours turned and for how productive your techs were for the course of the day.

Most management systems have the capability to track and report billed hours as long as your service advisor is assigning a technician and the billed time for each job to a labor line. Consult with your management system rep if you need assistance on the proper way to enter technician labor per labor line.

Tools to Correct Effective Labor Rate

Now that we have properly defined effective labor rate, discussed how to calculate it, discussed why it is so important to track it and what affects it, we probably should discuss the tools you can use to correct it. You will have some jobs that you just won't be able to collect 100 percent of your shop rate on. As discussed, oil services and inspection/smog services are examples. The trick though is to minimize the negative impact of these jobs as much as possible. If we make sure that we collect properly on diag-



nostic and labor-only sales, we have a good start. Another tool we can use is a labor matrix that should be used on all estimated jobs. The theory with a labor matrix is to add a small percent increase to your labor charge for each 10th above an hour of billed time.

These are just a couple of the tools you should use to make up for the holes in your labor-rate bucket. Also, make sure your service advisors are estimating all labor available including the “adds” provided by the labor time guides. Make sure you have a hard diagnostic policy that includes an accountability tool for controlling diagnostic time.

How often have you said, “We can't charge the customer for all the time we have in this job. Just charge (fill in any number here) and we will make it up somewhere else.” We know that “somewhere else” is really at the end of the yellow brick road. In other words, someplace you will never get. Your advisor should be getting approval for diagnostic services, and you should have an accountability tool that makes sure the tech doesn't get caught up in taking longer than the allotted time.

In lieu of an automated program or shop flow system, I would suggest the simplistic egg-timer method. The service advisor should have two egg timers. When he or she dispatches the job back to the tech for diagnostics, the service advisor would set both to 55 minutes. The instructions are simple: “When the egg timer goes off, I (service advisor) either need a report of what the suggested repair will be or I need a report of what you have been able to check, what you have been able to determine and exactly what more you will need approval to do to complete your diagnostic evaluation.”


This is one of the most basic yet effective methods I have seen to control “diagnostic run-on.”

Periodically Review Canned and Menu Services

Next, you should periodically review your canned and menu services. Parts slip is a huge issue that just sneaks up on you and will have a huge negative impact on your effective labor rate.

Think about it, when was the last time you raised the price on your transmission service? How many price increases have you had on the chemical additives or the transmission fluid since? Parts costs go up, so to maintain your parts margin the parts sales dollars have to go up. The problem is the service sale price remains the same, so something has to give. The end result is the labor dollars available have to go down. If labor sales dollars go down and the tech time or billed hours remain the same, effective labor rate must go down.

A Tool for Building Fixed Priced Jobs

I have a great “building profitable flushes” tool that can assist in properly pricing any of your fixed-price jobs. If you wish to receive the tool on building profitable flushes to protect your effective labor rate, for a limited time you can simply go to www.ationlinetraining.com/2015-01. 



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Chris “Chubby” Frederick is the CEO and founder of the Automotive Training Institute. ATI's 108 associates train and coach more than 1,150 shop owners every week across North America to drive profits and dreams home to their families. Our associates love helping shop owners who are having the same struggle as many of them have had, and who are looking for the same answers — and in some cases looking for a lifeline. This month's article was written with the help of Mike Bennett, a shop owner in Pennsylvania and an ATI Coach.

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