

# KNOWING YOUR COSTS

**The rumor is, we have a lot of good Well Drillers and Pump Technicians in our industry but only a handful of good business operators.**

**MWWDA wants to change that Image!  
Here is one way to help you become more aware of your costs and a better business operator.**

- There are many ways to figure costs
- Cost per hour
- Cost per day
- Cost per foot ( drilling industry )
- Cost per Person
- Cost per Job??
- Cost Per Rig/unit

**What's Involved**

- Cost by the hour/per man is the way we are going to figure today!
- Costs are on 12 months / 2080 hours per year minimum but its better to do total Hours worked by all direct labor (previous year)
- Most companies pay employees by the hour
- If you pay by Salary you just can re-calculate for hourly rate
- Salary is weekly gross times 52 divided by 2080= hourly rate

**Cost BY the Hour**

- Labor Expenses
- Direct payroll- employees doing \$\$ making work
- These are Labor expenses
- Overhead Expense's
- Indirect labor Secretary, Yard/shop help/ Mechanic ( if you have one) Yourself if you're not actively doing billable work
- Insurance expenses– Medical, work comp, Liability, auto, property and all other insurance expenses
- Fuel, taxes (not payroll) all utilities including cleaning services, advertising, Accounting Expense's, office supplies etc.

**Calculating Costs/Overhead ?**

- FICA, State Employment Taxes, Federal Employment Taxes.
- for a total of 7.65 % on employee's gross pay up to \$132000.00 per year
- Capitol Expenses- Rig payment/ truck payment's (principal comes from profit; interest is figured into cost but for this demonstration we are going to combine them.)
- Tooling, Maintenance, Tires and all other on-going expenses
- Retirement 401K or IRA Employer Contributions, Bonus's
- Depreciation & Amortization IS an expense!!!!

**Calculating Costs/Overhead ?**

- Total of all expenses (excluding Material and Direct Labor) and Divide by total man hours of direct labor worked plus average hourly paid wage will give you cost per hour
- So \$1,000,000.00 of Total expenses divided by 20,000 total worked hours by direct labor = \$50.00 hour plus average hour wage (\$25.00) = 75.00 per man per hour.

## The Correct Calculation

- With a COST of \$75.00 per hour with a 30% profit its just over 107.00 per hour
- Now that said, in our industry we don't bill for every hour and have to account for shop time, warranty, jobs we all make mistakes on etc..
- To purchase capitol equipment such as rigs, tankers, service trucks, backhoes, and unforeseen large repairs that all comes from the profit.
- There is 2080 hours in a year at 40 hrs. per week. Not many companies in our industry can say they billed 40 hours for each man each week
- If you had 4 men with a total billed hours of 1200 you would have a potential profit of \$153,600.00 . Possible but not probable!
- When you know your costs you can adjust your labor rates to account for down time etc. When you don't your shooting from the hip and it may be too late before you figure it out.

**Cost is not PROFIT**

- One thing we haven't covered yet is materials and cost/profit!
- Material profit is the cushion we all depend on for the really unknowns in business!
- Insurance costs rising from last year, lost revenue from down equipment and repairs.
- A whole basket full of issues that come up that's too long of a list to go over.

## **Material Costs and Profit.**



Let's say we are drilling a 300' unscreened drift well!

So at a cost at \$75.00 per man, a 2-man crew=\$150.00 per hour on a rig /or \$1,500.00 for a 10-hour day, let's say with travel, drill and development it's 3 days, that's \$4,500.00 in overhead and labor.

Remember all your overhead is in that above figure, fuel and all.

Materials; 6" steel casing, 280' at \$17.00 per foot, \$180.00 in Grouting material, \$100.00 in Misc. materials = \$4,860.00

For at total cost of \$9,360.00

## Sample Well Cost

- S & P 500 2018 average operating profit was 11% last year!
- Revenue is the top line on a company's income statement. Revenue, which is sometimes referred to as net sales, reflects the total amount of income generated by the sale of products or services. Revenue refers only to the positive cash flow directly attributable to primary operations.
- Operating profit sits further down the income statement and is derived from its predecessor, gross profit. Gross profit is revenue minus all the expenses associated with the production of items for sale, called cost of goods sold (COGS). Since gross profit is a rather simplistic view of a company's profitability, operating profit takes it one step further by subtracting all overhead, administrative and operational expenses from gross profit. Any expense necessary to keep a business running is included, such as rent, utilities, payroll, employee benefits, and insurance premiums.

**Built in factors**

- Without substantial Profit built into your products and Labor the sustainability and Sale ability of YOUR company is Insolvent “meaning worth nothing”.
- Now yes the assets are worth “Sale Value” and the customer list and phone number have minimal value. But the “Blue Sky” that all of us think our company is worth is “0” Meaning.....
- If the company is just making a living, ( paying you and your employees) not updating equipment constantly, and has no profit still left over, your going to have a hard time selling or even selling within your company.
- If you're not purchasing Capitol Equipment or Paying taxes every year (one or the other) You have a PROBLEM!

**What is all means!!!**

- The old rule of thumb was 30% on top of cost or 30% gross profit. If you could get 30% Gross profit on your products you were doing great. Well that was way back in 1970 or before.
- We can agree that some of our products are more than 30% and some less. But the reality is there isn't enough. You should be setting your product prices high enough that when you get to the end of the rainbow that your purchaser, whether it be within your company ( son daughter or other family member or employee) or outside your company, that they can step in, Pay themselves what you make ( you know they are going to want to) sustain all the current expenses including capitol expenses and BE ABLE TO PAY YOU OUT OF THOSE PROFITS! *That is how a company is listed as Saleable or profitable!!!*

**How much in enough?**

- Let's say we purchase 100 pumps a year at \$200.00 per unit. If we put a profit margin in there of 150% then it would sell for \$500.00. 200% would be \$600.00. That's more like what the industry is! For a total gross of \$40,000.00. If we wanted to purchase them for say \$150.00, we would make another \$5,000.00, but if we just add \$100.00 and some sales technique then we make \$10,000.00.
- Now you have built in a better margin and made your company more profitable.
- Material costs are touchy with some industry professionals but by far the larger margin of successful operators operate on a "Cost Plus" basis meaning they set their cost with the supplier/manufacturer and add in their margins to have enough profit to prosper this type of operator is known as a "Market Setter" or the contractor or business who "sets the market up".
- Not to set their prices based on the market ( be the low bidder ) and try to lower their costs with the supplier to compensate their margin. This is a formula or business model set up for failure!

**Example of what to worry about!**

- The reality is you need to add that profit into the bottom line! Most of our suppliers are close in price depending on Brand, Quality and quantity. The more units you purchase the less you pay per unit to a point.
- Set yourself apart from your competition, get your product costs all figured out and set your margins to be profitable.
- YOU are the best Salesman your company has. Sell yourself and your products. If you believe you do better work, sell better products than price them like they are better, and the Public will be smart enough to realize that and believe in you.

**How Do I get there?**

- This is just one way to set up your business for success and profit. There are many qualified people to consult on this in your own area. One thing I will say, “ If we as an industry do not start profiting and paying more attention to our bottom line, we wont be able to attract younger people to continue on in our industry because they want to profit also. So for the sustainability of YOUR COMPANY and the industry as a whole, you owe it to yourself and your family to look at your costs and make the adjustments necessary to stay in the business and beyond!!!!!!

**Sum it all up.**