Special Reprint Edition
As seen in USA TODAY,
June 2, 2008

Slow times mean pay cuts for many

Workers suffer as bonuses, commissions, tips all fall

By Jayne O'Donnell

When times were good, Mark Gershman's salary was all but an afterthought. It made up only about 20% of his pay. The remaining 80% flowed from sales, which were brisk, of the floors and countertops he sells in the once white-hot housing market of Scottsdale, Ariz.

Now? His commissions have shrunk, and he's living mainly on the monthly stipend that is his salary.

"Since I can't control my commissions, I must watch every cent going out with greater care," Gershman says. "Meals out are less often, and shopping at the mall is for recreation only."

To understand the human consequences of the economic slowdown, you have to look beyond the widespread layoffs. Consider the millions of people who have managed to keep their jobs yet have seen their pay slashed, often drastically. From home-improvement contractors to waiters to salespeople, those who are paid at least in part with commissions, bonuses or tips have been battered by the slowdown.

"This may be the first downturn where, because variable pay is so pervasive, it's affecting everyone down to hourly workers," says John Bremen, a director in Watson Wyatt's compensation consulting practice.

With their pay diminished, such workers typically reduce their spending. And when they do, the effect tends to ripple through layers of the economy. A saleswoman now taking home smaller commissions, for example, is likely to tip less at her next restaurant meal.

Chris Koch, a waitress in Elgin, Ill., says her customers are tipping so much less on basic meals that her earnings are down by $100 to $150 a week. Most of her customers who used to tip 15% to 20% are now tipping 8% to 10%. She's now working two to four extra shifts a week just to make up for the lost income. "Impulse purchases," Koch says, "have been cut to almost nothing."

If you count the people covered by some form of so-called "variable pay" at just the 1,500 largest companies, the consulting firm Watson Wyatt estimates there are about 25 million workers. Add the salespeople at small to midsize businesses — the 1.25 million real estate agents and 229,100 new car salespeople, for example — and you're talking about a sizable chunk of the labor force: at least one in five workers.

That doesn't even include the 20 million people who the Small Business Administration says own companies but have no employees and whose sales in many cases have declined. Or the nearly 5 million "micro" businesses, which employ 10 or fewer workers and which Bremen says likely offer variable pay to at least some of them.

You won't find these people reflected in the latest job figures. Nor do the unemployment figures include people, such as most sales clerks, whose hours have been cut because consumer spending is down. Or the small-business owners whose sales have plummeted. Though they've not suffered as much as workers who have lost jobs, these people have seen their living standards fall, with far-reaching consequences for themselves and the overall economy.

Many in the upper salary brackets are feeling it, too. Wall Street bonuses were down about 5% last year, to an average $180,420 per worker, according to New York state's comptroller. Bonuses in the financial services industry are expected to be lower for 2008, and the impact, Bremen says, will likely be toughest on the lower-paid workers who have less discretionary income.

While no one feels very sorry for people with smaller six-figure bonuses, the trickle-down effect of such cuts can be more unsettling. Bonuses, says Carl Steidtmann, chief economist at Deloitte Research, are frequently used as down payments on cars or houses. When they shrink or vanish, the resulting spending cutbacks hurt whole categories of workers — auto sales staffers, real estate agents, clothing salespeople — who themselves rely on commissions far more than on salary.

James Matthews works in financial services, but his life couldn't be more different from that of his counterparts on Wall Street. Matthews' total compensation this year is about half what it was last year. In a better year, about 60% of his pay came in the form of commissions on loans or other investments he sells for a bank. Now, about 90% of his take-home pay arrives in the form of a relatively small salary; only about 10% is commissions.

Matthews, 26, and his wife, who is expecting, had moved to Charlotte from Columbia, Md., in February to escape the higher cost of living. That meant that Matthews had to give up his "book" of clients, which reduced his earnings. The sputtering economy, he says, has made it a one-two punch.

"We've cut everything that's not necessary," Matthews says. "We've still got cable, but that will be the next thing to go."

Try living on no paycheck for 26 months

Charlie Kehler enjoyed several good years in commercial real estate development before he opened a real estate investment firm two years ago with two others, including Terry Hindermann. Their company, Altus Realty Partners in McLean, Va., buys properties with partners and renovates and leases them or redevelops and sells them.

Because their business is so new, they reinvest nearly all the money they earn back into it. But it's taking far longer to make deals, which makes waiting the years for investments to pay off that much harder.

Hindermann, who’s been in business seven years longer than Kehler, says he’s been putting away money for years for times like this. But the slowdown’s taking more of a toll on Kehler’s budget.

“I haven’t had a paycheck in 26 months,” Kehler says. “I used to sleep straight through the night. Now, I’m pretty much guaranteed to wake up at 3:30.”

Kehler, who has a small child, says his wife has asked why he doesn’t “go work for someone again.” He’s resisting.

“At this stage, we’re committed to projects 12 to 18 months out,” he says. “It would be very hard, emotionally and morally, because we made financial commitments to these people. Plus, there’s been a slight letup in the credit markets, so I’m feeling better these days.”

Commission-based pay could get more prevalent

Even as the precarious nature of commission- and bonus-based pay gives pause to some, some experts say these pay structures will probably become more common at large companies.

“In difficult economic times,” Bremen says, “companies are more likely to use these types of programs, especially these days.”

Though shrunken paychecks can hurt morale, Bremen notes, companies often regard layoffs as more problematic over the long run. Many employers prefer not to have to invest the time and money involved in hiring new people or rehiring old ones — some of whom will be disgruntled – once business rebounds.

“People understand in a bad year they get a smaller bonus or no bonus, but it’s much harder to understand losing their job,” Bremen says. “When profits are not as high, (companies) can reduce compensation costs by 10% to 15% instead of having to lay off 10% to 15% of employees.”

Watson Wyatt estimates about 95% of the roughly 1,500 largest for-profit companies offer incentive pay to at least some staffers. Some of them say they can’t imagine life with a steady salary. Bridgit Fitzgerald, who sells cosmetics, apparel and other merchandise at a luxury specialty store in the Washington, D.C., area, has worked on straight commission for more than 20 years. Thanks to a loyal customer base that tends to be recession-proof, she’s earned more each year and has been able to buy a high-end apartment near her workplace, as well as a vacation condo in South Carolina.

Still, there’s a certain level of stress that arises from not knowing how big your next paycheck will be, especially when floor traffic at work has slowed considerably. To assuage the jitters, Fitzgerald says, she always pays her mortgage a few months in advance. She also calls and e-mails clients more often, because some of them aren’t showing up at the store as much.

“I just kind of put blinders on and don’t look at what’s going on around me,” she says. “I don’t think about the nervousness or say, ‘I’ve got to make this much money today.’”

Some who aren’t on salary, Hindermann agrees, think salaries are overrated.

“If you have a salary and you’re working for a corporation, when the economy is going very well, you’re their best friend and they’re happy to pay you,” he says. “When they’re not going so well, you’re expendable. Your salary is much more at risk than people who are self-sustaining. In the end, it’s best to control your own destiny.”

Motioning from his office window, he notes that many of the truly wealthy are — or were — risk-taking entrepreneurs. Some risks, though, become more threatening over time. While there was always waiting involved in Hindermann and Kehler’s business, it’s now become more of the nail-biting variety.

“With the downturn in the economy, it takes much longer to get a lease transaction done; it takes much longer to get a sale done and to get projects financed,” Kehler says. “It’s made the general environment a lot more tentative than it was 12 months ago.”

When it takes longer to execute their business plans, Kehler says, he and his partners need to financially “carry the property while it’s redeveloped or leased up, and that’s what keeps you up at night.”

Problems tend to trickle down

When the economy squeezes people at the upper income levels, the hurt will typically seep down the economic chain. Kehler says he and his wife have cut way back on eating out and have put all home renovations on hold.

That sort of reaction causes salesmen such as Gershman and waiters such as Jason Erickson of Seattle to wince. Yet as their pay shrinks, they, in turn, reduce their own spending.

Erickson’s customers are being so much more cautious about what they order — they favor less expensive bottles of wine, for example — that he says his tip average is down from about $175 a night six months ago to $130 now. Erickson now buys coffee to make at home rather than spending $3.50 a day on a cup. He eats lunch out once a week rather than four or five times.

“I’m only one person, and I can see how because I make a little less money, they make less money,” he says. “Multiply this scenario times even 20 to 30 people, and it’s a real impact.”

Glenda Edmonds of Akron, Ohio, is exerting a similar effect on spending in her area. Paid by the hour, she receives the same check every two weeks from her job as a college financial aid counselor. But her husband, a service manager for a dinner theater, receives a quarterly bonus that’s down about 20% from last year. That bonus had helped pay for vacations and other miscellaneous expenses.

“We pray every day,” she says, “that we don’t get sick or the cars break down.”

To stretch their money, Glenda now buys enough groceries at a warehouse club to last at least two weeks and makes food to last two to three days, like soups and casseroles. Dinners out are out of the question. Vacations this summer will consist of one-gas-tank trips, if there’s enough money.

Gershman, the Arizona salesman, says he’s still saving some money from each paycheck, receiving good employee benefits and investing the maximum he can into his 401(k). Philosophical about the pain the downturn has caused him, he says it’s a “good lesson in materialism.” Like any good salesman, he favors the bright side.

“We’re geographically advantaged,” Gershman says. “We enjoyed the biggest boom in the boom years, (and) we expect to bounce back before many other parts of the nation do. But until then, everyone and everything is on hold.”

"Slow times mean pay cuts for many": Day-to-day financial planning

Objectives

- Read the article "Slow times mean pay cuts for many."
- Analyze the trickle-down effects of a slowing economy.
- Create an estimated budget for living expenses after high school.
- Balance a budget using cost-cutting and creativity.

Preparation

Each student will need:

- A copy of the article "Slow times mean pay cuts for many."
- A copy of the lesson.
- A few copies of the local newspaper including the classified section and grocery store inserts for group reference.

1. Read the article and answer discussion questions. (20 minutes)

- What effects has the slower economy had on consumer spending?

  ____

  ____

- How are people adjusting to reduced incomes? What changes have they made to earn more money or spend less? ____________________

  ____

- How has the slowing economy affected your household? Your personal income?

  ____

  ____

2. Calculate your budget. (25 minutes)

What financial future should you expect after high school? You may be living on your own, making your own money and spending more of your own money. What choices will you make when the bills come due? Let's make a budget. If you plan on working after high school instead of pursuing more schooling, assume you'll be working 40 hours a week. The national median for hourly wages is $12 (meaning half of those employed in non-supervisory jobs make more than that and half make less). At $12 an hour for full-time work, you will be making $480 a week.

1. What are your total gross earnings per month (figure four weeks per month)? ________
2. Multiply your gross earnings by 0.15. Put that total here. ________
   (That's at least how much you'll have taken out of your paycheck each month for taxes, Social Security and Medicare.)
3. Subtract the taxes from your gross earnings. This is your net monthly earnings. ________

This figure shows how much you will have to spend each month. In other words, this is the money you'll have to work within as you create your budget!

Now you need to list what your living expenses will be after high school. You'll be more independent, so your expenses will be higher. Get in groups of three to create a list of your expenses. If you're not sure what some things cost, like rent, look in the classified ads of your local paper to get an idea of where you want to live and how much you will pay to live there. The newspaper will also have ads for different services and products, which may help you calculate expenses.

Directions: In the second column of the chart below, estimate the monthly cost for each of the goods and services listed in the first column. Then, in the second to last row, add all the costs together. Finally, in the last row, write down your net earnings (which you indicated in Step 3 on the previous page).

Rent	
Renter's insurance	
Food/groceries/dining out	
Phone (cell and land line)	
Electricity	
Water/sewer	
Garbage pick-up	
Car payment	
Car insurance	
Gas for car	
Cable/Internet	
Entertainment	
Shopping	
Health insurance	
Other	
Total expenses (Add all above lines here)	
Total net earnings after taxes (Step 3 from previous activity)	

What's the difference? Do you earn more than you spend? If you do, great! Open a savings account and start planning for the future. If not, re-evaluate your budget and answer the following questions:

- What costs can you cut? (For example, would you be willing to live with a roommate or two to help with expenses?)
- In what areas can you be creative to save money?

3. Debrief and apply. (10 minutes)

- How much money did you expect you'd be making each year after high school?
- Does that sound like a lot of money?
- How far does that money go?
- What was your beginning budget?
- How did you change that budget after you compared it to what your earnings would be?
- With this budget in mind, what specific changes will you make to your plans for what you will do after high school?