What Inspires You, Inspires Us.

June 2018

Gain-Sharing Program Study

State of North Dakota

Contents:

Executive Summary

Eide Bailly has completed a study of the North Dakota Mill and Elevator Association (ND Mill) gain-sharing program for the State of North Dakota. The study was completed to satisfy the legislative intent of SB 2014. Section 30 of that bill requires the Industrial Commission, in consultation with the North Dakota Mill and Elevator Association, perform a study of the gain-sharing program. The study must include consideration of the costs and benefits of the gain-sharing program, best practices in other milling operations, and the estimated fiscal impact of repealing or modifying the gain-sharing program.

As part of this study, we considered financial benchmarking data of comparable entities with the same North American Industry Classification System (NAICS) code, data from a milling company survey that was conducted, compensation data, local market considerations and an internal employee survey in evaluating the current gain-sharing program. As part of our analysis, Eide Bailly considered the costs and benefits of the gain-sharing program related to ND Mill efficiencies, yields, turnover and safety along with consideration of survey data from other milling operations, local labor force considerations, and financial metrics of the ND Mill as well as non-financial impact of the gain-sharing program.

For the purposes of this analysis, the current gain-sharing program details are attached in the appendix.

Findings:

Financial Benchmarking

- Net income before transfers is within the parameters of comparable entities with similar NAICS code.
- ND Mill has a favorable labor and benefits percentage compared to entities with similar NAICS code.

Milling Company Survey, Compensation Data and Other Local Market Considerations

- The Company has favorable turnover compared to milling companies surveyed.
- Bonus compensation for all mill respondents is based off profitability.
- Limited survey data indicates certain positions of the ND Mill compensation ranges from 50th to 75th percentile.
- National Compensation Data based on revenue size, industry size and general location collected by the Economic Research Institute (ERI) indicated ND Mill compensation was below average at the time the data was collected in December 2017
- Local comparison of labor competition indicated lower or similar base pay scales.
- Unemployment in North Dakota is 2.6% and 1.8% in Grand Forks.

Employee Survey

- Employee survey responses consistently indicated that gain-sharing program was effective to increase profits, improve safety and overall work performance. On a scale of 1-5, 1 being important – overall response rating was 1.104.

Analysis

- In considering the ND Mill's financial performance from 2001-2005 in comparison to 2013-2017 attributing certain percentages of the profitability increase to the gain-sharing program, we found that increased profitability would outweigh potential costs considered if the gain-sharing program was removed.

	Attributable to Gain-Sharing Program		
	25%	50%	75%
Increase in Earnings Attributable to the Following:			
Favorable Yield	$ 850,000	$ 1,700,000	$ 2,550,000
Favorable Employee Production Efficiency	750,000	1,500,000	2,250,000
One-Time Initial Employee Turnover Cost*	713,000	713,000	713,000
Favorable Employee Retention*	56,000	56,000	56,000
Improved Safety	102,500	205,000	307,500
Increase in Earnings Attributable to the Gain-Sharing Program	**2,471,500**	**4,174,000**	**5,876,500**
Less: Estimated Future Gain-Sharing Expense	1,738,060	1,738,060	1,738,060
Net Increase in Gain Before Transfers Attributable to the Gain-Sharing Program	**$ 733,440**	**$ 2,435,940**	**$ 4,138,440**

* We estimated that the analysis is attributable to the gain-sharing program.

Each flour mill included in our survey included a bonus or incentive program as a part of their employee compensation package. The calculated cost/benefit analysis assumes removal of the entire incentive program which may not be realistic and not representative of the marketplace.

Consideration

Based on the findings above, specifically the earnings analysis along with consideration of compensation data comparisons and other financial and non-financial aspects of maintaining the gain-sharing program, the gain-sharing program is financially feasible.

Financial Benchmarking Report

North Dakota Mill and Elevator Association Benchmarking Report

We compared the results of operations from the North Dakota Mill and Elevator Association (ND Mill) with similar companies operating in the same industry. We searched for comparable industry companies using Risk Management Association ("RMA") Annual Statement Studies and ProfitCents. Industry financial measures provide limited comparative perspective and strict comparisons should be made with caution.

We searched for comparable companies using North American Industry Classification System (NAICS) code 31121 – Flour Milling and Malt Manufacturing. Due to the limited availability of benchmarking data at a similar sales range, we compared the ND Mill with companies without filtering by sales range. As presented in the schedule below, the industry average data from RMA and ProfitCents includes 58 and 10 companies, respectively. Management noted that the Malt Manufacturing industry tends to achieve a stronger profit margin that the Flour Milling industry. Common sized margins for the Mill compared with the industry average companies are presented in the schedule below.

	FYE 6/30/2013	FYE 6/30/2014	FYE 6/30/2015	FYE 6/30/2016	FYE 6/30/2017	RMA Industry Average	ProfitCents Industry Average
Sales	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of Sales	90.3%	88.7%	86.7%	88.2%	86.8%	76.6%	76.0%
Gross Profit	**9.7%**	**11.3%**	**13.3%**	**11.8%**	**13.2%**	**23.4%**	**24.0%**
Operating Expenses	5.1%	5.9%	6.5%	7.4%	8.6%	16.6%	19.6%
Operating Income	**4.6%**	**5.4%**	**6.8%**	**4.4%**	**4.6%**	**6.8%**	**4.4%**
Nonoperating Revenue (Expenses)	-0.2%	-0.2%	-0.1%	-0.1%	-0.3%	-0.9%	-0.8%
Gain Before Transfers	**4.4%**	**5.2%**	**6.7%**	**4.3%**	**4.3%**	**5.9%**	**3.6%**

Note: The industry data is unfiltered by sales range.

We included the ND Mill's material cost and labor in the production and quality control departments in cost of sales to compare gross profit margin to the industry average companies. However, due to classification differences between the ND Mill's financial statements and the industry average companies, we consider the operating income and gain before transfers margins to be more meaningful metrics of comparison. The ND Mill's operating income margin was greater than or equal to the industry average company from ProfitCents throughout the analysis period. In addition, the ND Mill's gain before transfers margin was generally slightly less than the industry average company from RMA, but generally greater than the industry average company from ProfitCents. This indicates that the ND Mill's profit margin, which includes the expenses related to the gain-sharing program, is consistent with its national peers.

Next, we compared the level of salaries and wages as a percentage of total sales for the ND Mill with the industry average company from ProfitCents. There were four companies in the dataset reported in ProfitCents for direct labor as a percentage of revenue. ProfitCents reported the industry average company's direct labor as a percentage of revenue of 12.98 percent. There were nine companies in the dataset reported in ProfitCents for general and administrative labor as a percentage of revenue. ProfitCents reported general and administrative expenses as a percentage of revenue of 4.22 percent. Overall, the ND Mill's salaries and wages as a percentage of sales were significantly less than the industry average company. This indicates that the ND Mill utilized less labor expense to generate sales than the industry average company reported in ProfitCents.

	6/30/2013	6/30/2014	6/30/2015	6/30/2016	6/30/2017	Industry Average Recent 12-Months
Salaries and Wages as a % of Sales	3.8%	4.1%	4.6%	5.2%	5.8%	17.2%

Overall, the ND Mill's earnings capacity is in-line with the industry average company. In addition, salaries and wages as a percentage of sales for the ND Mill were significantly lower than the industry average company. This indicates that the ND Mill utilizes its labor expense in an efficient manner to generate sales when compared to its peers. Based on this information, the Subject's gain-sharing plan results in an earnings performance for the ND Mill that is comparable with its peers.

Sources:

"NAICS – 311210 Flour Milling and Malt Manufacturing Industry Financial Data and Ratios Report." *ProfitCents.*

"NAICS – 31121Y – Flour Milling and Malt Manufacturing 2017-2018 Annual Statements Studies." *Risk Management Association.*

RMA Description

The Risk Management Association (RMA) is a not-for-profit, member-driven professional association serving the financial services industry. Its sole purpose is to advance the use of sound risk management principles in the financial services industry. RMA's Annual Statement Studies® have been around for 98 years and are the industry standard for comparison financial data. Today, it features data for over 788 industries derived directly from more than 260,000 statements of financial institutions' borrowers and prospects.

RMA has approximately 2,500 institutional members. These include banks of all sizes as well as nonbank financial institutions. Relationship managers, credit officers, risk managers, and other financial services professionals in these organizations with responsibilities related to the risk management function represent these institutions within RMA. Known as RMA Associates, these 18,000 individuals are located throughout North America and financial centers in Europe, Australia and Asia.

ProfitCents Description

Sageworks is a financial information company that provides lending, credit risk, and portfolio risk solutions to financial institutions and provides financial analysis and valuation applications to accounting firms and private companies. Through these markets, we have created the largest real-time database of private-company financial information in the United States, analyzed over 11.5 million loans and aggregated the corresponding loan data.

Sageworks was founded in 1998. Sageworks began helping community banks and credit unions more efficiently lend to commercial borrowers and grow their business communities in 2006. Now, several thousand accounting firms and over 1,200 financial institutions leverage Sageworks in their operations.

Compensation Data, Milling Company and Employee Survey Results

North Dakota Mill – Compensation & Gain-sharing Report

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Scope of Engagement

Develop a survey to identify compensation ranges for mill workers and office staff. Invite competing mills to participate in the survey. Gather information on base compensation, benefits and bonus/incentive programs offered by mills participating in the survey. Utilize data gathered related to bonus/incentive programs for the gain-sharing program study.

Compensation Survey Results

COMPENSATION SURVEY PARTICIPANT DATA:
Twelve mills across the United States were asked to participate in a confidential compensation survey regarding base compensation, pay increase percentages, bonus compensation factors and benefits information for mill-related positions. Of those, 4 participated in the study; a 25% response rate. All respondents are within the flour mill industry, so data provided is 100% relevant to this gain-sharing report. Participants reported the total number of employees, employees who are members of a union and employees working in North Dakota. While 32% of respondent data indicates employees working in North Dakota, all participating organizations are within similar pay markets.

UNION WORKFORCE IN THE SURVEYED MILLS
North Dakota Mill is the only mill participant utilizing union staff. 16% of the pay data represented unionized labor for positions within the mill.

TURNOVER WITHIN THE SURVEYED MILLS
The average turnover for the mills participating in the survey for the last fiscal year was 11.7%. North Dakota Mill reported turnover of 8.5%, which is well-below the average for the flour mills who participated.

COMPENSATION SURVEY FINDINGS
Surveys provide information on the "going pay rates" at a specific point in time in a labor market. As such, labor markets may include incumbents with varying years of experience that meet minimum requirements for a position.

> **Annual Pay Adjustments** – The average pay increase across all 4 responding mills was 2.9% for all positions. Pay increases were found to be effective during specific months for 3 of the mill respondents, and on an employee's anniversary for 1 mill respondent.

Bonus Compensation - All 4 mills offer bonus compensation each year. All employees are eligible for a bonus. Bonuses are paid during specific months for all 4 mill respondents. Bonuses within the mill respondents are determined by any of the following criteria:

- Profitability - 100% of mill respondents base bonus on this criteria
- Individual employee performance - 50% of mill respondents also base bonus on this criteria
- Years of service - 25% of mill respondents also base bonus on this criteria
- Hours worked - 25% of mill respondents also base bonus on this criteria

Benefits – All 4 mills offer benefits. Overall mill responses include:

Health Insurance	100% of mill respondents offer health insurance; 75% pay 80% - 100% of employee premiums
Dental Insurance	75% of mill respondents offer dental insurance; 25% pay 100% of the employee premium
Vision Insurance	75% of mill respondents offer vision insurance; 25% pay 96% of the employee premium
Short-Term Disability	100% of mill respondents offer STD; 50% pay 100% of the employee premium
Long-Term Disability	75% of mill respondents offer LTD; 25% pay 100% of the employee premium
401K	75% of mill respondents offer 401k; 50% contribute towards an employee's 401k plan
Health Savings Account	75% of mill respondents offer an HSA; 50% contribute to the HSA
Flexible Spending Account	50% of mill respondents offer an FSA to employees
Paid Time Off	100% of mill respondents offer paid time off
Paid Holidays	100% of mill respondents offer paid holidays
Paid Sick Leave	50% of mill respondents offer paid sick leave
Paid Bereavement	75% of mill respondents offer paid bereavement
Wellness Program	75% of mill respondents offer a wellness program

Additional benefits offered include: pension, life insurance, Employee Assistance Program, jury duty/witness leave, service awards

Position Compensation Ranges – Pay ranges with a 25th, 50th and 75th percentile as well as an average compensation were provided for positions with 3 or more respondents. Average compensation was provided for positions with 2 respondents. All positions with at least one respondent were provided with information on the number of mills who responded as well as the number of employees included in the results for the position.

Pay at the 25th percentile indicates that 75% of survey participants pay more, and 25% pay less.
Pay at the 50th percentile indicates that 50% of survey participants pay more and 50% pay less.
Pay at the 75th percentile indicates that 25% of survey participants pay more and 75% pay less.
Most organizations pay at the 50th percentile unless being a market leader with regards to compensation is part of their compensation philosophy to hire and retain strong talent, or to hire specialized skill sets.

Survey results for positions with 3 or more respondents show that ND Mill pays below the 50th percentile for 3 positions; around the 50th percentile for 4 positions; between the 50th and 75th percentile for 5 positions; and at or above the 75th percentile for 14 positions.

ADDITIONAL COMPENSATION INFORMATION PROVIDED BY PROCESSING COMPANIES IN GRAND FORKS

In addition to the data provided through the Mill Industry Survey, North Dakota Mill gathered pay data from two processing operations in Grand Forks. Similar positions were compared from a compensation perspective. The compensation average of North Dakota Mill and the 2 processing companies – as well as the average comp for ND Mill is shared below for several positions:

- Maintenance Workers: Average = $26.28; ND Mill = $25.85
- Miller: Average = $26.71; ND Mill = $24.03
- Electrician: Average = $28.12; ND Mill = $28.93*
- Bagger: Average = $21.15; ND Mill = $21.22
- Lab Tech: Average = $21.15; ND Mill = $18.42
- Production: Average = $22.50; ND Mill = $21.93
- Grain Cleaner: Average = $24.05; ND Mill = $22.60
- Yard Worker: Average = $22.61; ND Mill = $21.42
- Feed Loader: Average = $22.81; ND Mill = $21.53
- Utility Worker: Average = $19.61; ND Mill = $16.82
- Forklift Operator: Average = $19.62; ND Mill = $20.81
- Warehouse: Average = $22.48; ND Mill = $21.22

**ND Mill has 2 incumbents – both Journeyman Electricians and long-term employees*

This data indicates that North Dakota Mill is paying a bit below the average of direct competitors in Grand Forks. While the base compensation may be in the 75th percentile for flour mills per the 2018 Mill Industry Survey, they are not above average for their specific market when compared with companies that recruit and hire the same/similar talent.

Effect of Removing Bonus/Incentive Programs

When employees have received bonuses for years in a row, they no longer think of the bonus as "extra" compensation, but rather come to rely on it as part of their total compensation package. When a bonus (or any benefit) is removed, there are costs:

- **Employees feel de-valued –** The initial offer which includes compensation, benefits and perks such as a bonus set the expectation for the employee and their worth to the organization. When benefits, perks and/or bonuses are removed, employees are left wondering if their worth is now less than it was when they started. Resentment can come in to play when they are expected to do the same work for what they deem is "less" overall compensation.

- **Morale is stripped and employees' job satisfaction lowers -** Bonuses are perks. When you take away the perks, it's just another job.

- **Productivity suffers –** Making the company profitable so that you can share in the financial reward of that accomplishment makes people work harder. If there isn't a reason to work harder, employees won't. And, when employees aren't working harder, productivity declines.

- **Employee loyalty is reduced –** If a company cuts one perk or benefit, employees are left wondering what will be cut next. They become more willing to listen to other job offers.

EMPLOYEE SURVEY

A survey of 153 mill employees with 134 employees responding provided the following findings:

- Tenure of mill employees with North Dakota Mill are as follows for the mill employees surveyed:
  - 23 between 0 and 1 year of service
  - 31 between 2 and 5 years of service
  - 20 between 6 and 9 years of service
  - 60 with 10 or more years of service

- Employees were presented with 4 questions and asked to rank the appropriate response from the following choices:
  - 1 = Strongly Agree
  - 2 = Agree
  - 3 = Neutral
  - 4 = Disagree
  - 5 = Strongly Disagree

  Here are the responses:
  - Employees "Strongly Agree" (1.2 rating) that they understand what they need to do to ensure the company achieves the required results for the gain-sharing bonus to be offered.
  - Employees "Strongly Agree" (1.133 rating) that the gain-sharing program promotes extra effort by employees to achieve goals.
  - Employees "Strongly Agree" (1.267 rating) that gain-sharing promotes a safe work environment at the North Dakota Mill.
  - Employees "Strongly Agree" (1.156 rating) that gain-sharing increases profits and overall performance of the North Dakota Mill.
  - Employees were also asked to identify the importance of the bonus to them in determining their overall yearly compensation by selecting one of the following choices:
    - 1 = Very Important
    - 2 = Important
    - 3 = Neutral

The overall response rating was 1.104. Employees place a lot of importance on the gain-sharing bonus they receive. We also noted historical data from management indicating average tenure of 13.01 years of service.

Comments shared by employees regarding their opinion of the overall effectiveness of the gain-sharing program were consistent, and included the following:

- North Dakota Mill's gain-sharing program is one of the reasons I joined the company.
- Gain-sharing is one thing keeping people here.
- Without profit sharing it would be difficult to find people that are willing to put in the hours necessary to work here.
- Gives everyone a reason to work hard and stay safe. Boosts people to do their best at their job. We work 7 days a week so it goes a long way. I feel if gain-sharing is decreased or gotten rid of, it will negatively affect the morale and productive efforts of all employees.
- Keeps people focused on daily performance – individually as well as on the company goals. People strive to get the best out of their shifts day in and day out to help the company achieve better success so that they can receive a bigger gain-sharing. Everyone does their best to have a safe and successful year.
- It helps morale and encourages so many people to continue working at a facility that runs 7 days per week.
- I believe we are the only state employees that work 7 days a week. It helps morale knowing we are getting compensated for those weekend days lost.
- We strive to get that profit sharing. We work 7 days a week, get calls at all hours of the night and in the end that all pays for itself. Gain-sharing is a great thing.
- Gainsharing promotes "think what is best for the mill."
- Without it, what is the purpose of going the extra mile to ensure things are done as effectively as possible? This program makes us all winners – company and employees alike.
- Employees of the mill work very hard to produce the product customers need. For employees that work 5-7 days a week, the gain-sharing is their incentive. All the hard work = more profits.
- I believe it's what keeps a lot of people here. If we were not to get it I would have to assume a lot more people would not last and retire much earlier, putting more stress on the retirement fund.
- I have worked here with and without gain-sharing. The years without, a couple of people lost their homes, morale was horrible.
- If it goes away, you will see a change in performance.
- Judging by how we can't get new employees now with it, how can we expect it if it's gone? All of us count on it as part of our wages. We give up a lot of our lives to be here 7 days a week to ensure the company's growth.
- Take away gain-sharing and the answers to the 5 questions above change from "Strongly Agree" to "Strongly Disagree" – just the ugly truth.
- I will strongly reconsider working here if we lose gain-sharing.

Cost of Removing Bonus/Incentive Programs

COMPENSATION ADJUSTMENT

As mentioned previously, when employees have received bonuses for years in a row, they no longer think of the bonus as "extra" – it becomes an expected component of their overall compensation. If a bonus is removed, the company must identify a way to make the employee's overall compensation "whole" again. A successful method involves looking at the bonus for an employee for the previous three years and averaging that figure – then adding that amount to base compensation.

For Example:

John earns **$55,000.00** per year and has been paid bonuses in the past 3 years of $6,000.00, $6,500.00 and $7,000.00. The average of John's bonuses for the past 3 years is $6,500.00 – so John's new compensation is **$61,500.00** ($55,000.00 + $6,500.00).

Sam earns **$21.75 per hour** and has been paid bonuses in the past 3 years of $3,400.00, $3,500.00 and $3,600.00. The average of Sam's bonuses for the past 3 years is $3,500.00 – so Sam's new compensation is **$23.43 per hour** ($21.75 *2080 hours per year = $45,240.00; $45,240.00 + $3,500.00 = $48,740.00; $48,740 / 2080 hours per year = $23.43 per hour)

Figuring out the new base compensation is simple, and the company is able to show the employee that their annual compensation has not changed. However, after a year, the employees will no longer view their compensation as being whole – they will forget their base compensation was increased, and will see the bonuses as something they still deserve. The small increase in compensation per pay period will not be as rewarding as receiving a larger annual bonus.

The new base compensation will also be the figure used for pay increases. If we use a 3% pay increase for the examples used above, the company ends up paying more for the same labor:

John – 3% raise at $55,000.00 = $56,650.00 (or a $1,650.00 increase)
John – 3% raise at $61,500.00 = $63,345.00 (or a $1,845.00 increase)

Sam – 3% raise at $21.75 = $22.40 (or a $0.65 per hour increase)
Sam – 3% raise at $23.43 = $24.13 (or a $0.70 per hour increase)

TURNOVER COSTS

Turnover is another cost of removing bonus/incentive programs from an organization's compensation plan. There will be employees who leave if bonuses are removed. The cost of replacing an employee varies depending upon the specialized skills needed. These costs include:

- Recruitment costs (advertising, time to interview, agency fee)
- Lost productivity (products not produced with the employee not there OR overtime costs paid to others to take on the workload)
- Lost time during on-boarding and training (current employees are taken away from their normal job duties to train the new hire)
- Lost engagement (employees who remain are left wondering if they should stay)
- Cultural impact (when someone new comes in, everyone has to make an adjustment to the way things have been done)

Other Factors to Consider

When discussing labor costs, it is important to keep in mind unemployment and the market for labor.

In the state of North Dakota, unemployment is at a low of 2.6%. Unemployment within Grand Forks, ND specifically is 1.8%. That means that for every 100 people, only 1.8 people are unemployed. That figure is staggering when considering if there is a pool of qualified individuals ready and available to fill open positions that may arise. When a company considers changing its compensation, benefits, perks and bonus programs, they must keep the labor pool in mind.

There are 8,346 jobs in North Dakota posted on Indeed.com; 1,143 of those positions are in Grand Forks, ND. Of those 1,430 positions, 154 are production-related positions, 96 are manufacturing-related positions, and 58 are plant-related positions. Other industries hiring in Grand Forks include: education, agriculture, distribution, oil & gas, construction, agriculture, healthcare, restaurant, etc.

Competitors for the same talent ND Mill seeks within Grand Forks include:

- American Crystal Sugar (8)
- Philadelphia Macaroni Company (5)
- J.R. Simplot Company (11)
- EMW Industrial (1)
- Hood Packaging Corporation (2)
- Steffes Corporation (6)
- MGI Grain (1)
- LM Glasfiber
- Cirrus Aircraft (6)
- Amazon
- Altru Hospital (49)
- University of North Dakota (33)

With that much competition in the marketplace, employers cannot risk making decisions regarding compensation, benefits, perks and bonuses that will cause employees to go elsewhere.

Benefits of Maintaining a Bonus/Incentive Reward Program

There are many positive reasons for offering and maintaining a bonus/incentive reward program.

- **Align bonuses with the company's strategic initiatives -** You can align individual work performance to department metrics/expectations and company strategic initiatives. Tying a bonus to achieving those objectives gets everyone on-board with helping the company be successful.
- **Bonuses increase motivation –** When a bonus is on the line, people are motivated to work harder/smarter.
- **There are recruitment benefits to offering bonuses –** Employees who receive a bonus are more likely to feel appropriately compensation and are loyal to your organization. Loyal employees will speak positively about their employer to those they know which could lead to employee referrals of candidates for open positions. In a market with 1.8% unemployment, an employer needs every advantage it can get when it comes to recruiting new talent.
- **Bonuses can be used to build team collaboration –** When everyone on the team knows what the department metrics/expectations and company strategic initiatives are, they are more inclined to work together to achieve them. It also encourages accountability. Achieving shared goals as part of a team helps build camaraderie and effective communication which increases overall productivity.

Compensation Data

In December 2017, the ND Mill requested a compensation salary range for certain positions. Economic Research Institute (ERI) was used to gather compensation data.

ERI information is based on the following key factors

- Job duties versus job titles
- Years of Experience or Revenue Size
- Industry Codes (NAICS)
- Metro market areas

We have outlined our findings for each position in separate tables. Each table contains the following data:

- Position title provided
- The ERI position title if different
- Years of Experience or Revenue Size
- Market salary data from ERI at the 10th, 25th, Median, 75th, 90th percentile of all market data

Compensation data based on the above criteria for certain positions indicated that ND Mill paid below the 10th percentile for 23 positions; around the 10th percentile for 10 positions; around the 25th percentile for 9 positions and the 50th percentile for 4 positions.

Analysis

Gain-Sharing Program Expense

	6/30/2013	6/30/2014	6/30/2015	6/30/2016	6/30/2017	Average
Gross Revenue	$ 318,974,830	$ 310,189,181	$ 305,574,444	$ 273,637,401	$ 287,986,843	$ 299,272,540
Gain Before Transfers	$ 11,907,227	$ 13,351,342	$ 16,675,348	$ 9,336,618	$ 9,719,164	$ 12,197,940
Margin	*3.7%*	*4.3%*	*5.5%*	*3.4%*	*3.4%*	*4.1%*
Gain-Sharing Program Expense	$ 1,545,994	$ 1,665,806	$ 2,167,394	$ 1,528,024	$ 1,783,084	$ 1,738,060
% of Total Salaries and Wages Benefits	*12.8%*	*13.0%*	*15.3%*	*10.7%*	*10.8%*	*12.5%*

As presented in the schedule above, the ND Mill's gain-sharing expense averaged $1.7 million, or 12.5 percent of total salaries and wages/benefits. Gain-sharing program expense averaged 12.5 percent of the ND Mill's total salaries and wages. A bonus or incentive program averaging only 12.5 percent of total compensation does not appear to be an unreasonable amount of bonus/incentivized compensation.

We compared the estimated incremental increase in earnings attributable to incentivizing the ND Mill's employees with the gain-sharing program against the actual gain-sharing expense. It is important to note that this analysis is based on survey response information of other flour mills, management's representations, and actual historical results. The information presented is estimated based on the information available to us and should be considered as such.

We performed a sensitivity analysis on increases in the ND Mill's net gain before transfers margin on gross sales as compared to the gain-sharing expense as a measure of the "hurdle" necessary to achieve a return on investment for the gain-sharing program. We utilized average gross revenue over the last five fiscal years ended of $299 million as the basis for our sensitivity analysis, which is presented in the schedule below.

	Increase in Gain Before Transfers Margin on Gross Revenue		
	0.25%	0.50%	0.75%
Increase in Gain Before Transfers	$ 748,181	$ 1,496,363	$ 2,244,544

Based on average revenue over the last five fiscal years of $299 million as shown above, we noted that the ND Mill needs to achieve an increase of only 0.59 percent in its gain before transfers margin on gross revenue to achieve a return on investment for the gain-sharing program. This is based on a hurdle of increased profits of approximately $1.7 million, which is equal to the average gain-sharing expense over the last five years. We considered the ND Mill's favorable yield, employee production efficiency, workforce turnover, and safety increases in our consideration of increased earnings for the company that are attributable to the gain-sharing program.

Favorable Yield

Based on survey responses of two other flour mills, the ND Mill achieved a favorable yield on raw product over the last five fiscal years of 2.0 percent. Management noted that each 100 basis point increase in yield results in a $2 million increase to the ND Mill's gain before transfers. As presented on the following page, because the ND Mill achieved a 2.0 percent favorable yield compared to its peer group of two percent, this represents a $4 million increase in the gain before transfers margin.

Favorable Yield for the ND Mill Compared to the Industry Average	**2.0%**
Increased Earnings Per 100 Basis Point Increase in Yield*	$ 2,000,000
Increased Earnings Based on Yield	**$ 4,000,000**

* Estimated by Management

We were also provided with the ND Mill's actual yield for the early years of the gain-sharing program and current yield numbers. The ND Mill did not retain yield records before the gain-sharing program was implemented. Therefore, we considered the ND Mill's actual yield from 2002 through 2005 (earliest years of the gain-sharing program) as indicative of the company's yield pre-gain sharing. We utilized the ND Mill's average yield for 2013 through 2017 as indicative of its yield post-gain sharing program. Based on average yield for the aforementioned periods, the ND Mill achieved an increase in its yield of 1.4 percent when comparing pre and post gain-sharing. We applied this percentage to the $2 million estimated increase in earnings per 100 basis point increase in yield as presented in the schedule below.

Favorable Yield for the ND Mill Based on Pre & Post Gain Sharing	**1.4%**
Increased Earnings per 100 Basis Point Increase in Yield*	$ 2,000,000
Increased Earnings Based on Yield	**$ 2,800,000**

* Estimated by Management

We utilized the average of these two estimates as indicative of the ND Mill's increase in earnings based on its favorable yield on production.

Increase in Earnings Based on Yield - Industry Average Estimated	$ 4,000,000
Increase in Earnings Based on Yield - Pre & Post Gain-Sharing Program	2,800,000
Estimated Increase in Earnings Based on Favorable Yield (Average)	**$ 3,400,000**

Management attributes increased yield to the quality of the plant workers' quality in production and the experience and leadership of the lead miller. The gain-sharing program incentivizes the Mill's employees to work more efficiently to generate profits for the company. This factor is a key reason why the gain-sharing program is effective for the ND Mill.

However, it is also unreasonable to assume that the entire portion of the favorable yield is attributable to the gain-sharing program. This favorable yield is driven by processes, new technology, additional property and equipment, and employees' work quality. We performed a sensitivity analysis on the ND Mill's increase in earnings based on its favorable yield that is attributable to the gain-sharing program.

	Increased Earnings Due to Favorable Yield Attributable to Gain-Sharing Program		
	25%	50%	75%
Increase in Gain Before Transfers	**$ 850,000**	**$ 1,700,000**	**$ 2,550,000**

Favorable Employee Production Efficiency

We considered the ND Mill's increased efficiency in terms of hundredweight produced per hour (cwt/hr.). The ND Mill does not maintain records on cwt/hr. prior to the implementation of the gain-sharing program. We consider the earliest years of the gain-sharing program to be the most representative information available related to pre-gain-sharing program. Based on information provided by management, the ND Mill's average cwt/hr. from 2001 through 2005 and from 2013 through 2017 is 28.3 and 36.77, respectively. Therefore, the ND Mill has increased its efficiency in terms of cwt/hr. by 8.47 since the early years of the gain-sharing program. The ND Mill incurred 368,283 work hours during 2017, which management indicated is a fair representation of the company's future work hours. Based on information provided to us, net profits per cwt sold from 2013 through 2017 was $0.9663. We multiplied the favorable increase in efficiency of cwt/hr. by net profits per cwt to estimate increased profits due to labor efficiency as presented in the schedule below.

Average CWT/HR 2013 - 2017	36.77
Less: Average CWT/HR 2001 - 2005	28.30
Favorable Increase in CWT/HR	**8.47**
Times: Number of Hours Worked in 2017	368,283
Favorable Increase in CWT Due to Efficiency	**3,119,354**
Times: Average Profit Per CWT 2013 - 2017	$ 0.9663
Increased Earnings Due to Labor Efficiency Increase (Rounded)	**$ 3,000,000**

Because not all of the increase in labor efficiency is attributable to the gain-sharing program we performed a sensitivity analysis of the percentage of increased profits on cwt/hr. attributable to the gain-sharing program.

	Increased Earnings Due to Favorable CWT/HR Efficiency Attributable to Gain-Sharing Program		
	25%	50%	75%
Increase in Gain Before Transfers	**$ 750,000**	**$ 1,500,000**	**$ 2,250,000**

Favorable Workforce Turnover

Next, we reviewed the replacement cost of the ND Mill's assembled workforce. Our calculation of the replacement cost of the ND Mill's assembled workforce is presented on the following page.

Category[1]	Employee Count	Total Comp (Including Benefits) in this Category	Average Rounded Compensation & Benefits (Per Employee)	Years[2]	Cost @ Lost Efficiency %[3]	Hiring Manager Hours Recruiting[6]	Key Executive Interview Costs ($75/Hour)[4]	Human Resources Hours Recruiting[6]	Human Resources Interview Costs ($30/Hour)[5]	Subtotal	Cost Per Position/Level
Key Executive	7	$ 1,123,777	$ 160,540	1.00000	$ 53,513	12	$ 900	12	$ 360	$ 54,773	$ 383,412
Office	38	2,627,923	69,156	0.50000	11,526	8	600	8	240	12,366	469,907
Plant	108	12,820,358	118,707	0.28846	11,414	5	375	5	150	11,939	1,289,427
									Replacement Cost of Assembled Workforce (Rounded)		$ 2,140,000
									Replacement Cost Per Employee (Rounded)		$ 14,000

Key:

[1]The Subject's employees were broken into three categories consisting of key executives (CEO, VP of Finance, VP of Sales, Logistics Management Top Executive, Manufacturing Director, Procurement Director, and Quality Assurance Director), office, and plant.

[2]Training time for each position is based on management's estimates. Management estimated training time for key executives, office, and plant employees at 52 weeks, 25 weeks, and 15 weeks, respectively.

[3]"Lost efficiency" assumes 1/3 of the time spent training is nonproductive.

[4]Management noted that each of the key executives spend time hiring in their respective areas. Therefore, we utilized an average annual wage for the key executives of $160,540, which represents an hourly wage of $77/hour based on a 2,080 hour work year, which we rounded to $75 per hour.

[5]Management noted that the Human Resource Manager sits in on all interviews with prospective employees. The company's Human Resources Manager is paid $63,500 annually, or $31 per hour based on a 2,080 hour work year, which we rounded to $30 per hour.

[6]Management estimated that both the key executives and Human Resources Manager spend 12 hours, 8 hours, and 5 hours on hiring each key executive, office staff, and plant staff, respectively.

We calculated a replacement cost of the ND Mill's assembled workforce of $2,140,000, or approximately $14,000 per employee. Based on our survey of the ND Mill's employees, it is reasonable to assume that approximately one-third of the company's employees would leave the company for other employment opportunities if the gain-sharing program disappeared. Therefore, we considered the cost of replacing one-third of the ND Mill's employees as an initial one-time turnover as presented below.

Replacement Cost of Assembled Workforce	$ 2,140,000
Times: One-Time Employee Attrition from Removing the Gain-Sharing Program	33.33%
One-Time Initial Employee Turnover (Rounded)	**$ 713,000**

As previously mentioned, based on survey results of the ND Mill's employees and conversations with management, removal or reduction in the gain-sharing program would result in a significant initial runoff of the ND Mill's labor force. This would result in the Mill paying overtime to its employees that retain employment with the company to sustain production. Although we did not quantify this cost, it does represent an additional disadvantage in removing or reducing the gain-sharing program.

Our survey of flour milling companies indicated that their employee turnover for the most recent fiscal year is 11.7 percent. The ND Mill's employee turnover during 2017 was 8.8 percent. This results in a favorable employee turnover for the ND Mill of 2.9 percent. The ND Mill had 153 full-time employees (FTEs) during 2017. Multiplying the ND Mill's favorable turnover by 153 FTEs results in a rounded favorable retainage for the Mill of four employees per year. We multiplied the replacement cost per employee by the ND Mill's favorable retainage, resulting in increased annual earnings from favorable employee retainage of $56,000 as presented in the schedule on the following page.

Average Annual Employee Turnover for the Peer Group	11.7%
Less: ND Mill Employee Turnover FYE 2017	8.8%
Favorable Employee Turnover for the ND Mill	**2.9%**

Actual Number of Full-Time Employees	153
Times: Favorable Turnover for the ND Mill	2.9%
Favorable Employee Retainage Annually (Rounded)	**4**

Cost of Recruiting/Training Per Employee*	$ 14,000
Favorable Employee Retainage Annually	4
Increased Earnings Based on Favorable Employee Retention (Rounded)	**$ 56,000**

*Based on a replacement cost of the workforce of $2,140,000, consisting of 153 employees.

Based on our survey results, the gain-sharing program is a key benefit for employees in both recruitment and retention of the ND Mill's employees. Based on the responses from the survey, it is reasonable to assume that the gain-sharing program is the sole reason for the ND Mill's favorable employee retention. Therefore, we considered the entire increase in earnings based on favorable employee retention to be attributable to the gain-sharing program.

Improved Safety

The ND Mill greatly improved its safety once the gain-sharing program was initiated. Management estimates that the cost for the ND Mill of each accident where the employee incurs lost days of work is $87,956. A large portion of this expense is medical bills. Management indicated that the ND Mill averaged 6.3 accidents each year where the employee incurs lost days of work pre gain-sharing. Management further indicates that the ND Mill averages 1.6 accidents per year where the employee incurs lost days of work post gain-sharing. We multiplied the favorable decrease in the amount of accidents at the ND Mill resulting in lost time by the average cost of each accident to estimate the increase in earnings based on improved safety.

Average Number of Accidents Results in an Employee Missing Work - Pre Gain-Sharing	6.3
Average Number of Accidents Results in an Employee Missing Work - Post Gain-Sharing	1.6
Favorable Decrease in the Number of Accidents Resulting in Days Off	**4.7**
Cost Per Incident Resulting in Days Off*	$ 87,956
Favorable Decrease in the Cost of Accidents for the ND Mill (Rounded)	**$ 410,000**

* Provided by North Dakota Workforce Safety & Insurance

Because not all of the decrease in the cost of accidents is attributable to the gain-sharing program, we performed a sensitivity analysis on these cost savings as presented in the schedule below.

	Increased Earnings Due to Safety Increase Attributable to Gain-Sharing Program		
	25%	50%	75%
Increase in Gain Before Transfers	**$ 102,500**	**$ 205,000**	**$ 307,500**

Consideration

The schedule below presents an overall sensitivity analysis of the net increase in earnings attributable to the gain-sharing program. The schedule below presents the cost/benefit analysis in the first year after hypothetically removing the gain-sharing program. Each flour mill included in our survey included a bonus or incentive program as a part of their employee compensation package. The calculated cost/benefit analysis assumes removal of the entire incentive program which may not be realistic and not representative of the market place.

	Attributable to Gain-Sharing Program		
	25%	50%	75%
Increase in Earnings Attributable to the Following:			
Favorable Yield	$ 850,000	$ 1,700,000	$ 2,550,000
Favorable Employee Production Efficiency	750,000	1,500,000	2,250,000
One-Time Initial Employee Turnover Cost*	713,000	713,000	713,000
Favorable Employee Retention*	56,000	56,000	56,000
Improved Safety	102,500	205,000	307,500
Increase in Earnings Attributable to the Gain-Sharing Program	**2,471,500**	**4,174,000**	**5,876,500**
Less: Estimated Future Gain-Sharing Expense	1,738,060	1,738,060	1,738,060
Net Increase in Gain Before Transfers Attributable to the Gain-Sharing Program	**$ 733,440**	**$ 2,435,940**	**$ 4,138,440**

* We estimated that the analysis is attributable to the gain-sharing program.

Appendix

NORTH DAKOTA MILL
GAIN SHARING PROGRAM
FY2018

- **Eligibility – all full-time employees on June 30, 2018 that worked a minimum of 1,000 hours during the program year are eligible.**
- **No pay out of any bonuses if profit before gain sharing expense accrual does not exceed 2.0 million dollars.**
- **No payout on the profit part of the plan if profit before gain sharing expense accrual does not exceed 4.0 million dollars.**
- **Payout will be calculated as a percent of earnings from July 1, 2017 to June 30, 2018.**
- **Goal numbers were set to reflect current realities for the new plan year.**
- **Goal numbers were set by the General Manager and are attainable with effort.**

The plan consists of two independent parts. 4% potential payout is from exceeding gain sharing goals and an un-capped potential payout is from profits.

For the year ending June 30, 2018 the goals are as follows:

Gain Sharing 1st Part – 4% Bonus Potential*

Goals	
Cwt./man-hour (includes all hours)	36.5
Cost per cwt. (before gain sharing exp.)	$2.17
Yield	77.2%
Safety Record	165 Points

*4% bonus potential if all numbers are met or exceeded. Each goal is worth 1% of the 4%.

Gain Sharing 2nd Part – Uncapped Bonus Potential

Profits (before gain sharing expense accrual):

2.0 million = 0.0% bonus pay out

4.0 million = 4.0% bonus pay out

Each additional 1.0 million in profits = 1.0% additional bonus payout.

NOTE: The 1st Part of the gain sharing goals begin to payout at a profit (before gain sharing expense accrual) level greater than $1.0 million. The 2nd Part of the gain sharing goals begin to payout at a profit (before gain sharing expense accrual) level greater than $2.0 million.

EXAMPLE #1:

The mill makes $2.0 million profit (before gain sharing expense accrual) and we exceed the goal for cwt./man-hour and cost/cwt. but not the safety record or yield. The total bonus received would be 2% for goals + 0% for profit = 2.0%.

EXAMPLE #2:

The mill makes $4.0 million profit (before gain sharing expense accrual) and we exceed the goal for cwt./man-hour, cost/cwt., and the safety record but not the yield. The total bonus received would be 3% for goals + 4.0% for profit = 7.0%.