Fun With Numbers…
Objectives

• Identify best practices in HR ROI measurement
• Determine the cost and benefits of HR initiatives in business terms
• Use a model to demonstrate HR solutions to business problems
The Saying Goes….

What Matters Gets Measured

What Gets Measured Gets Attention
The Role Of HR

• Understand key business goals
• Identify how HR impacts those goals
• Align HR business plan with strategic plan
• Measure results and communicate the value/ROI
What’s the Bottom Line?

Solve business problems with HR solutions!
Building the Business Case

Business Problem

Potential HR Solution/s

HR Metrics

Business Case
HR Value Proposition

How can HR help? Add value? Contribute to overall success?
What Does It Come Down To?
How Would It Add Value to Do It . . .
Better—Faster—Cheaper

Outcome → Impact/Value
Crawl Before You Jump

• Build upon every experience
• Little by little – analytics mindset
• Begin each project knowing what business issue or challenge needs to be addressed
Case Study Exercise
Case Study – Widgets Inc.

- Growing concern over 40% product return rate ($500/day in shipping costs alone)
- Suggestion of 100% inspection before shipment (would require more QA techs)
- Production is short-staffed with high turnover
- CEO wants a solution now!
Case Study – Widgets Inc.

• What will you do first?
• What are you curious about?
• What questions do you need to ask and why?
Identify HR Solutions to Business Problems

1) What is the business problem?
2) What does it cost?
3) What is a human resource based solution?
Identify HR Solutions to Business Problems

4) What is the cost of the solution?
5) What savings does the solution generate?
6) What is the cost/benefit ratio or return on investment?
ROI

- Compares value to costs
- Demonstrates efficiency of resources used

\[
\text{ROI} = \frac{\text{Value received from investment} - \text{Cost of investment}}{\text{Cost of investment}} \times 100
\]
Identify HR Solutions to Business Problems

7) Obtain approval and implement
8) Report measurable results!
Practical Tips on Using Model

1. Business Challenge
2. Cost of Business Challenge
3. HR/OD Oriented Solution
4. Cost of Solution
5. $ Improvement/Benefit from Solution
6. Cost/Benefit Ratio
Know the business strategy

Explore HR solutions

Identify metrics

Best Practices
Stop Doing What Doesn’t Work
Best Practices

• Organization goals should guide HR initiatives

• Determine which initiatives would provide the most value
  – Keep asking: how can this activity translate into something measurable?
Best Practices

• Get input and data from others
• Focus on increasing productivity, instead of cutting costs
• Identify the metrics that matter
Where To Start

• What are you currently measuring in your organization? What is done with the information gathered?

• How do you know what the C-suite values? Do you know what your CEO is looking for in the HR function?

• Where do HR initiatives come from? Who drives it – culture, CEO? Is it proactive or reactive?
Where To Start

• What successes have you had with ROI? How is success attributed to HR rather than other areas?
• What is communicated to the C-suite that demonstrates impact, value, ROI and alignment to goals of your organization? How well is that working?
Where To Start

• Do you have key dashboard outcomes? What are they? Are they different for recruiting, training, learning and development, succession planning? Are you measuring efficiency or effectiveness or both?

• What do you feel you could do better in terms of measurement and why?
Key HR Measurements

- Efficiency
- Effectiveness
- Predictive (advanced!)
Thought Leaders

• Jac Fitz-enz - *How to Measure Human Resource Management, The ROI of Human Capital, The New HR Analytics*

• Jack Phillips - *Proving the Value of HR: How and Why to Measure ROI, Show Me the Money: How to Determine ROI in People, Projects, and Programs*
Thought Leaders

• Michael Mercer - *Turning Your Human Resources Department into a Profit Center*
• John Sullivan – *Articles in HR Metrics & Analytics on drjohnsullivan.com*
• David Ulrich – *The HR Value Proposition*
Wrap Up

• Focus on what is important to your organization (i.e. alignment)
• Determine what to measure and how to measure
• Communicate HR’s success
  
  = HR IMPACT and VALUE
thank you!

- Call (866) HR – Hotline - available 24/7
  (866) 474-6854
- Email your request to InfoNow@mranet.org
Six-Part Planning Model

1. Business Challenge
2. Cost of Business Challenge
3. HR/OD Oriented Solution
4. Cost of Solution
5. $ Improvement/Benefit from Solution
6. Cost/Benefit Ratio

Source: Adapted from Michael Mercer's book *Turning Your Human Resources Department into a Profit Center*
Six-Part Planning Model

**Business Challenge.** First, a business challenge needs to be clearly stated. It could be an issue with productivity, turnover, managerial effectiveness, sales or a myriad of other business challenges that every business must successfully handle in order to enhance profitability.

**Cost of Business Challenge.** Here is where basic cost accounting comes into play. It is not enough merely to specify a business challenge that needs to be handled. That would be a passive and not profit-oriented approach. Instead, the human resources profit center must determine how much the challenge costs. Only by having such cost figures can a human resources or OD manager measure the cost-beneficial effectiveness of solutions to the business challenge being tackled.

**Solution to Business Challenge.** Now the human resources or OD manager gets to show his or her ingenuity. The question arises: What specific human resources-OD oriented solution would overcome the business problem? For instance, if productivity is the business challenge, then some solutions might be better selection methods, quality circles or productivity improvement programs, incentive pay systems, an engagement survey, employee assistance programs, suggestion boxes, teambuilding or many other solutions.

**Cost of Solution.** Cost accounting again comes into use here to determine the dollars that need to be spent to implement the solution. This step also provides an important check in that almost all of the time the solution should cost less than the challenge.

**Improvement/Benefit Stemming from Solution.** This part of the planning model enumerates the dollar improvement value resulting from the solution. To create a worthwhile, cost-beneficial solution, the dollar improvement stemming from the solution should be more than the cost of the problem and the cost of the solution. If it is not, then the solution was not worthwhile from a cost-benefit standpoint.

**Cost-benefit ratio.** This final step provides the crucial bottom line measure of how successful the solution proved. The cost-benefit ratio is similar to a return on investment figure. It tells how much money was earned compared to how much money was spent on the solution. Actually, this should be referred to as the benefit-cost ratio since the ratio is calculated by weighing the benefit stemming from the solution. For example, if a $100,000 improvement results from a $10,000 solution, then the cost-benefit ratio was 10:1. That is, for every one dollar spent on the solution, the organization reaped $10 in benefits. Such a cost-benefit ratio surely would be a great return on investment in any business venture.

*Source: Turning Your Human Resources Department into a Profit Center by Michael Mercer*
HR Metric Descriptions and Definitions

Revenue Per Employee

What is It?
Revenue per Employee, also known in its more advanced form as the Human Capital Revenue Factor, quantifies the value of labor as a revenue generator to an organization. The simple form of this calculation provides a measurement to determine human productivity as a per employee sum of the revenue generated in a fiscal year.

How is it Calculated?
The Revenue per Employee Calculator uses Revenue for an organization and an average number of employees as represented by the calculation of Full Time Equivalents (FTE’s) that takes into consideration various work schedules.

\[
\text{Revenue Per Employee} = \frac{\text{Revenue}}{\text{Total Number of FTE's}}
\]

Profit Per Employee

What is It?
Profit (or Loss) per Employee quantifies what value, as reflected by profit or loss, employees contribute to the organization. This calculation removes all expenses to provide a measurement that demonstrates what profit (or loss) human productivity generated over a period of time or in a fiscal year.

How is it Calculated?
Profit (or Loss) is calculated by taking Total Revenue and subtracting out all operational expenses (Direct and Non-direct non-personnel costs) and human cost expenses (Direct Personnel Costs) This is divided by the number of Full Time Equivalents (FTE’s)

\[
\text{Profit per Employee} = \frac{\text{Revenue} - \text{Total Operating Expenses (before taxes and interest)}}{\text{Total Number of Full Time Equivalents (FTE's)}}
\]

HR Expense Factor

What is It?
The Human Resource Expense factor is a measurement that demonstrates a cost of the human resource function as a percentage of an organization's total expense. This measurement permits an analysis of the value delivered by the human resource department during a period of time against other functional cost centers.

How is it Calculated?
The Human Resource Expense factor percentage is calculated by dividing the total expense (actual or budgeted) by the organization's total operating expense (actual or budgeted). Total operating expense does not include interest, depreciation and tax expense.

\[
\text{HR Expense Factor} = \frac{\text{HR Expense}}{\text{Total Operating Expense}}
\]
Total Compensation As A Percentage Of Revenue

What is It?
The Total Compensation as a Percentage of Revenue factor is an indicator measurement that is used to monitor labor costs. Tracking total compensation as a percent of total costs provides managers with valuable information for use in managing the costs associated with human capital, including evaluating the use of fixed versus variable compensation. Following this measurement will also permit an organization to determine if personnel cost (as indicated by base pay, incentives and benefits) is in line with organization goals, industry benchmarks and business plans.

How is it Calculated?
Total Compensation As a Percentage of Revenue = \( \frac{\text{Compensation Cost} + \text{Benefit Cost (Workforce on Payroll)}}{\text{Revenue}} \)

Absence Rate

What is It?
Calculating the absence rate helps an organization determine the number of days lost as a result of all absences from work during a given period. This ratio will enable the organization to compare with others within their industry through national surveys to determine whether the organization is in line with those averages or if further investigation is needed. Calculating the absence rate is the first step in determining how absences affect an organization in terms of productivity and actual cost. The absence rate can be calculated by organization, department or job group.

How is it Calculated?
For purposes of this calculator, the Absence Rate ratio is calculated by dividing the worker days lost through absence in a calendar, fiscal year or other 12 month reporting period by the average employee population in that calendar, fiscal year or other 12 month reporting period multiplied by the number of work days available per employee in that calendar, fiscal year or other 12 month reporting period.

\[
\text{Absence Rate} = \frac{\text{Workdays Lost Due to Absence}}{\text{Average Employee Population} \times \text{Number of Work Days Available per Employee}}
\]

Turnover Rate

What is It?
Turnover is an area heavily studied by all organizations to determine movement out of an organization (separations). Turnover is further categorized as either voluntary or involuntary. Voluntary turnover (resignations) is most often studied, as voluntary turnover is typically greater than involuntary turnover (discharges) and management's desire to reduce or maintain turnover at an acceptable level. Turnover can be further analyzed by looking at specific causes for separations. The U.S. Bureau of Labor Statistics provides survey data on a quarterly basis with regard to turnover.

How is it Calculated?
For purposes of this calculator, turnover is calculated by dividing the number of terminated employees in a calendar, fiscal year or other 12 month reporting period by the average number of employees that calendar, fiscal year or other 12 month reporting period.

\[
\text{Turnover Rate} = \frac{\text{Total Number of Employees who Terminated During the Period}}{\text{Number of Active Employees During the Period}}
\]
Cost Per Hire

What is It?
Cost per hire calculates what the true cost of hiring a new employee through external avenues and or through internal placement. While internal placements may not have all of the costs usually associated with recruitment (e.g. advertising costs, agency fees, etc.), nevertheless there are some costs associated with internal placement. The calculation includes advertising costs plus agency fees plus employee referral bonuses plus travel costs plus relocation costs plus reference checking costs multiplied by 1.10 (which is a cost variable multiplier) divided by number of hires.

How is it Calculated?
For purposes of this calculator, the cost per hire is calculated by first totaling the costs associated with advertising, agency placement fees, employee referrals, travel and lodging costs, relocation and reference checking costs of candidates and multiplying that total by 1.10 (which is a cost variable multiplier). This total in turn is divided by the total number of hires. These figures are to be based upon a calendar year, fiscal year or other 12 month reporting period basis.

(Note: for abbreviation purposes, the word "costs' in the formula is abbreviated using the letter "C")

Cost Per Hire =
(Advertising C + Agency C + Employee Referrals + Travel C + Relocation C + Reference Checking C) X 1.10
Number of Hires

Turnover/Replacement Cost

What is It?
Turnover/Replacement Cost measures the cost of turnover and looks at the cost of replacing the exiting employees. The expenses associated with the turnover/replacement calculation generally fall into categories such as separation costs, replacement costs, training and orientation costs and lost productivity.

How is it Calculated?
Turnover/Replacement Cost is calculated by adding separation costs plus replacement costs plus training and orientation costs plus performance differential in a calendar, fiscal year or other 12 month reporting period divided by the number of hires for that calendar, fiscal year or other 12 month reporting period:

(Note: for abbreviation purposes, the word 'costs" in the formula is abbreviated using the letter "C")

Turnover/Replacement Cost =  Separation C + Replacement C + Training C + Performance Differential
Number of Hires

Benefit Cost As A Percentage Of Revenue

What is It?
The Benefit Cost as a Percentage of Revenue factor is an indicator measurement that is used to monitor non-taxable/non-cash labor costs. Tracking benefit cost as a percent of revenue provides managers with valuable information for use in managing the costs associated with human capital. Total financial impact of new programs such as wellness efforts or insurance plan design can be evaluated in relationship to revenue. Trends up or down in this factor will reveal costs that need attention or value that has been added. Following this measurement will also permit an organization to determine if the benefit labor cost (as indicated by non-taxable/non-cash benefits) is in line with organization goals, industry benchmarks, and business plans.

How is it Calculated?
Benefit costs are totaled and then divided by either period actual or budgeted revenue for a calendar, fiscal year or other 12 month reporting period.

Benefit Cost As a Percentage of Revenue = \[
\frac{\text{Benefit Cost}}{\text{Revenue}}
\]
Benefit Cost As A Percentage Of Total Compensation

What is It?
The Benefit Cost as a Percentage of Total Compensation is an indicator measurement that is used to monitor non-taxable/non-cash labor costs. Tracking benefit cost as a percent of total compensation provides management with valuable information for use in managing the costs associated with benefits. This information can be useful when looking at hire versus lease or outsource decisions. Trends up or down in this factor will reveal costs that need attention or value that has been added with increasing relative costs.

How is it Calculated?
Benefit costs are totaled and then divided by total costs for a calendar, fiscal year or other 12 month reporting period.

\[
\text{Benefit Cost As a Percentage of Total Compensation} = \frac{\text{Benefit Cost}}{\text{Total Compensation Cost}}
\]

Variable Compensation As A Percentage Of Total Compensation

What is It?
Variable compensation as a percentage of total compensation is a measurement that demonstrates how much of an organization’s total compensation can vary with the revenues of the organization. Recent compensation trends have focused on increasing the amount of variable compensation. High levels of variable compensation can be correlated to high performing organization and organizations that attract and retain high performing employees. This measurement permits an organization to look at the success of variable compensation programs and fixed and variable compensation as it relates to revenue.

How is it Calculated?
Variable compensation as a percentage of total compensation is calculated by adding up all variable compensation and dividing that sum by total compensation.

\[
\text{Variable Compensation As a Percentage of Total Compensation} = \frac{\text{Variable Compensation}}{\text{Total Compensation}}
\]

Time To Fill Jobs

What is It?
Time to fill is a measurement of how long it takes an organization to fill a position once the opening has been approved. It is an indicator of hiring efficiency but should be balanced with cost and quality hiring measures. Time to fill can provide valuable feedback in determining which sourcing methods and recruitment strategies can most quickly produce the needed candidates. Cost of vacancies in jobs can be significantly reduced by driving down the time it takes to fill a job.

How is it Calculated?
Time-to-fill is measured by calculating the number of days from when the job requisition was received (RR) until the offer was accepted by the candidate (AD) for each job filled during the measurement period. Positions filled both with internal and external candidates should be included.

The number of days open is calculated using calendar days, including weekends and holidays. Aggregate the total number of calendar days that your total number of vacant jobs were open and then divide by the number of positions filled during the measurement period thus providing an average which balances seasonal and other fluctuations.

\[
\text{Time to Fill} = \frac{\text{Total Number of Day of Opened Jobs}}{\text{Total Number of Jobs}}
\]