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The Dirty Truth: Employee Turnover Cost

White Paper

TalentKeepers® is celebrating 15 years of providing award-winning employee engagement and retention solutions to help companies around the globe increase their performance. We provide employee engagement solutions, leader development programs, on-boarding processes and standardized or customized surveys, and other key talent management services to address critical business issues and enhance stakeholder value. TalentKeepers helps clients respond to industry and market factors that create uncertainty and organization exposure. Let us help you build a culture that keeps your best talent, boosts productivity and delivers outstanding performance.

Please direct questions, comments, and press inquiries to solutions@talentkeepers.com, please access our website at www.TalentKeepers.com or call 407.660.6041.

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TALENTKEEPERS®



A COMPANY IS KNOWN BY THE PEOPLE IT KEEPS

The Cost of Employee Turnover

We're all familiar with the expression, "you don't miss someone until they are gone." While this sentiment is typically associated with personal relationships, the same can be said of companies for their top employees. It's not just a matter of missing the camaraderie of a valued team member; it's a bottom line issue as well. Employee turnover takes a toll on morale, productivity levels, and customer satisfaction. For this reason, employee retention is an increasing priority for corporations around the globe, specifically with high performing team members.

The goal of any business, large or small, is to make a healthy profit that can be paid to shareholders or reinvested for growth. An important element of profit generation is the ability to control and minimize cost. Very extensive, yet often unrealized, the cost associated with employee turnover is an aspect of cost management that many business owners or companies fail to proactively control.

Employee turnover costs depend on labor markets in which you are competing. When the market is loose, for instance, it is relatively easy to find and train new employees quickly and at moderate costs. In contrast, in a more competitive market where labor and skills might be somewhat scarce, recruitment is generally more costly, and open positions may be vacant longer, resulting in higher loss of productivity and profitability. This is especially true when you are losing top talent to competitors or when customers have developed relationships with individual employees. Although market and labor conditions are indeed a factor, broad estimates put the cost of turnover in the U.S. at more than \$150 billion annually.

In many cases, the financial impact of turnover is severe, both in terms of increased recruiting fees and downtime associated with the on-boarding of new hires. When top talent leaves, they are not just leaving holes in a workforce that negatively impact employee morale and productivity, they are taking with them knowledge and skills that provide a competitive advantage in your marketplace. Their departure causes a harsh ripple effect on both direct and indirect costs in an organization.

What is Employee Turnover?

Before we explore the costs associated with employee turnover, let's step back for a moment to define it. At TalentKeepers, we work with our clients to define employee turnover in several ways: managed, unmanaged, controllable, and uncontrollable. Here is a quick look at the differences.

Managed employee turnover is, as the term implies, when employees leave the organization and it is initiated by the organization. Managed employee turnover can range from mass layoffs to a specific employee being asked to leave. This type of turnover also includes someone that has resigned because they were on a performance management plan with a strong probability it would lead to termination. This is often referred to as involuntary turnover.

Even as a leader in employee retention, TalentKeepers wholeheartedly agrees that some turnover in an organization is necessary. Some people are simply not a good fit for the organization in terms of performance; some can't seem to get to work on time or violate company policy, and the like. They need to go.

On the contrary, **unmanaged employee turnover** occurs when someone leaves who the organization would like to keep. Voluntary employee turnover is another common description for this type of attrition -- that is, the employee leaves the organization under their own volition.



This distinction leads to the further delineation of controllable versus uncontrollable employee turnover. For example, when someone leaves the organization, and it is someone that the organization would like to keep (i.e. highly trained, productive), he/she may be leaving for reasons outside the control of the organization.

Examples of **uncontrollable employee turnover** include spouse relocation, returning to school, joining the armed forces, and in some extreme cases - even death. Although the organization would prefer the person to stay, uncontrollable turnover occurs when there is little that can be done to prevent them from leaving.

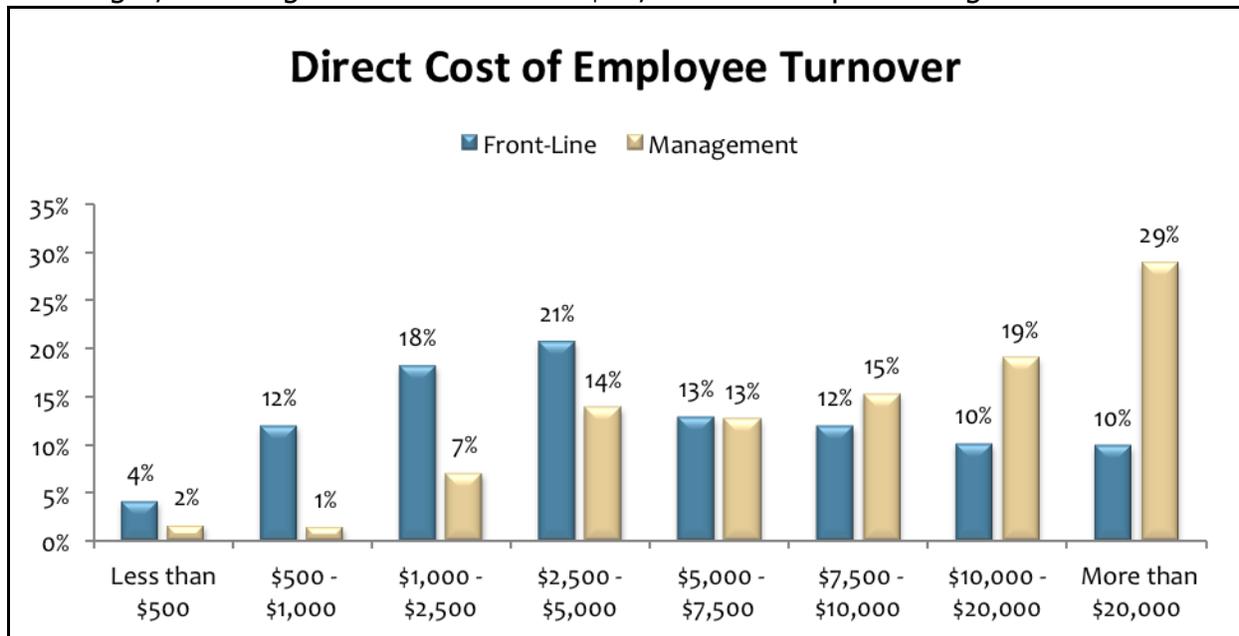
Conversely, **controllable employee turnover** occurs when a desirable employee leaves the organization for reasons that *were* under the control of the organization. Unmanaged, controllable employee turnover is the type of turnover that TalentKeepers helps organizations not only identify, but also provide recommendations to reduce. Although some of the causes of unmanaged, controllable employee turnover can easily be identified and resolved by improving communication, enriching job duties to be more interesting, developing leaders, increasing flexibility in work processes, etc.

What are the Direct Costs of Employee Turnover?

Unmanaged, controllable employee turnover has a significant monetary cost to organizations, as well as a significant impact on other key functions within the organization. To provide some scope of the costs typically experienced by organizations, TalentKeepers embarked on a study about employee engagement and retention challenges (with over 500 organizations participating from a range of industries), analyzing causes, costs, and consequences impacted by employee turnover. In this survey, we asked organizations to report their estimated direct financial cost of losing even a single front-line employee or leader. Direct costs include some of the more obvious expenses such as filling the vacancy (e.g., recruiting, interviewing, selection, testing), training costs for replacements, equipment and tools, uniforms, and similar expenses.

Direct costs are often just the tip of the iceberg compared to indirect costs.

For front-line employees, organizations indicated that the direct cost for replacement ranges from \$500 to more than \$20,000, with the most frequent cost ranging from \$2,500 to \$5,000 per frontline employee. When asked about the direct cost of replacing a manager, most organizations indicated \$20,000 or more per manager.



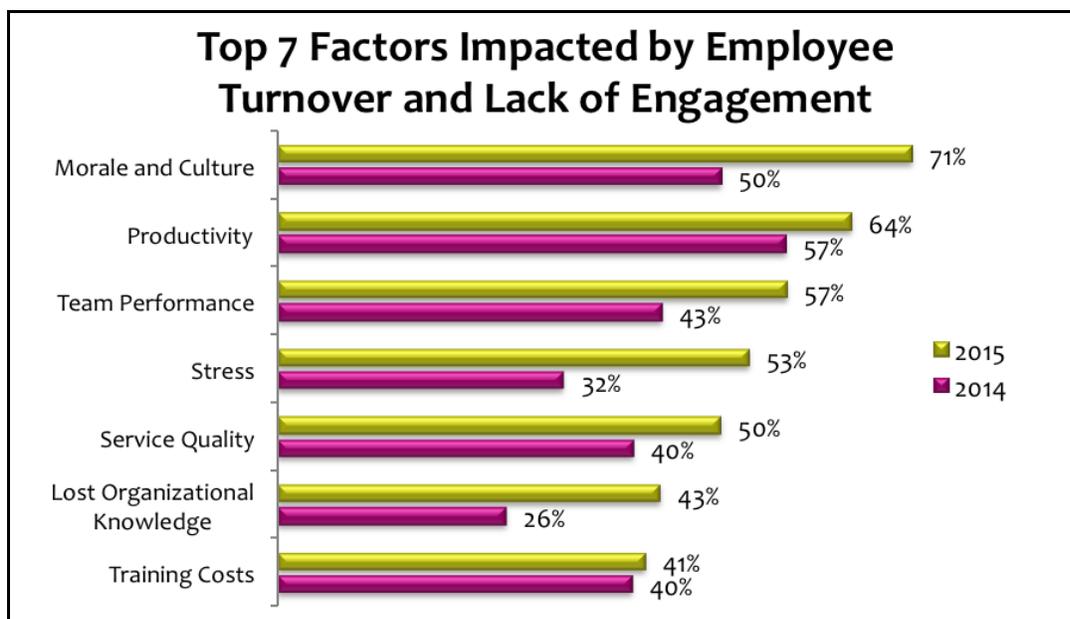
To help reduce employee turnover, TalentKeepers advises organizations to view their employees as resources, not expenditures.

What are the Indirect Costs of Employee Turnover?

Of the two categories of cost that are associated with employee turnover, direct costs are typically the costs that leaders focus on because they are visible. Yet of equal importance and very often neglected, are the hidden or indirect costs. These costs are represented by lost productivity, the financial value of time that is used to find and hire the replacement employee and the negative impact on colleagues and customers when a valuable employee leaves an organization.

According to Robert Morgan, president of Spherion's Human Capital Consulting Group, a world leader in the measurement of human capital, several noted experts believe that 70 percent of the country's wealth today is in human capital as opposed to physical capital. "In a knowledge economy, the primary profit lever is people and therefore companies must take seriously their responsibility to manage this asset," says Morgan. To help reduce employee turnover, TalentKeepers advises organizations to view their employees as resources, not expenditures.

As further evidence on how employee turnover affects organizations, we asked organizations to indicate their top seven issues impacted by turnover. "Morale and Culture" rose significantly between 2014 and 2015 and remains ranked as the highest issue.

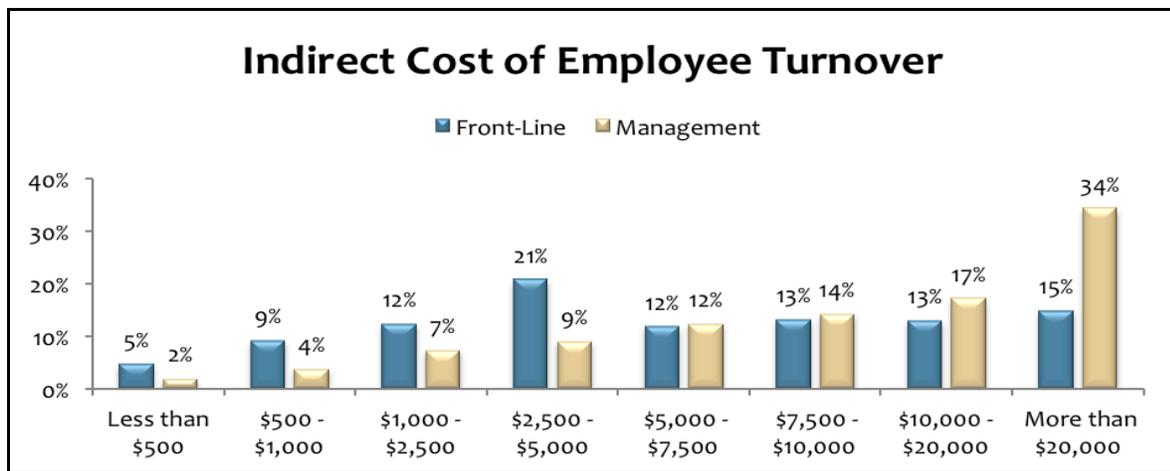


As employee turnover increases and the war for the best talent intensifies, hidden costs will escalate.

To estimate productivity levels, there are several formulas out there; some are based on thresholds such as an employee being 25% productive for the first month, 50% productive after two months, and so on. Naturally, for more senior-level positions or those requiring longer periods of time to develop full productivity, the costs will be higher.

One of the simpler formulas proposes that the cost of lost productivity is at a minimum of 50% of a person's compensation and benefits cost for each week the position is vacant, even if there are people performing the work. Factors to consider is the "cost" of the knowledge of skills – and customer relationships – of the person walking out the door, missed deadlines due to disrupted work flow, the morale of the team members who must pick up the work or who might grieve the emotional loss of a respected colleague.

In the TalentKeepers Employee Engagement and Retention study, organizations were also asked to estimate the indirect cost of losing a single front line employee or manager. Although indirect costs are often difficult to quantify, they are often the most damaging to organizational viability. Consider the indirect impact on profitability when employee morale drops, customer service wanes, and sales are lost because relationships between employees are broken. Organizational knowledge leaves, and there are not enough employees to meet market demands. For front-line employees, most organizations indicated indirect costs added an additional \$2,500 to \$5,000 to the loss of one front-line employee. For most organizations, the indirect cost associated with losing a single manager tracked more than \$20,000, compared to 2008 data of \$10,000 to \$20,000 per manager. As employee turnover increases and the war for the best talent intensifies, hidden costs will escalate.



If leaders aren't made aware of employee turnover costs, they can't take appropriate action.

Why Don't More Companies See the Critical Need to Measure Employee Turnover Costs?

There are a variety of reasons companies do not see the critical need to measure employee turnover costs, all of which cost companies in expertise and dollars. Some large company leaders, for example, believe that employee turnover is "an HR problem." True, Human Resource employees need to serve as partners in reducing employee turnover cost; however, this is a strategic issue requiring top management's attention and actions. In other cases uncovered by TalentKeepers, costs associated with employee turnover are either discounted as "part of doing business" or they are grossly underestimated and therefore register as less of a concern. A final reason why more companies don't view employee turnover as a costly problem is because costs are not reported to top management. If leaders aren't made aware of turnover costs, they can't take appropriate action.

In some cases, there is simply no process to capture and tabulate costs. Our survey found that less than half of the organizations participating track and report employee retention data to executives and stakeholders on a regular basis. This finding is similar to another industry study reported in *WebProNews* that found that only 44% of its respondents had a process in place to estimate employee turnover costs; 43% of companies relied on intuition; and 13% had no process at all.



Employee turnover does not just affect a single area – its effects can spread unnoticed throughout many areas of an organization, ultimately impacting the bottom line.

Digging Deeper

When we consider the top business areas influenced by employee turnover, we quickly realize that none of these factors are isolated. Instead, these factors have wide reaching impacts on many other aspects of the organization. Take lower employee morale as an example. Lower employee morale can directly affect productivity, quality, and the customer experience. We also know that low employee morale perpetuates even more turnover as employees begin to look for greener grass. As can be seen, employee turnover does not just affect a single area - its effects can spread unnoticed throughout many areas of the organization, ultimately impacting the bottom line.

Some factors to be calculated in the cost of employee turnover are a combination of direct and indirect costs. Take recruiting costs as an example. An internal recruiter has to take the time to understand the position requirements, develop and implement a sourcing strategy, review candidates' backgrounds, prepare for interviews, review resumes, schedule and conduct interviews, prepare candidate assessments, conduct reference checks, etc. HR experts suggest this time (*indirect costs*) can range from anywhere from 30 to 100 hours. And don't forget the time for managers and employees involved in the selection process and any internal candidates that will be away from their jobs during the interviewing process. Then we must factor in *direct costs* such as drug tests, background checks, and pre-employment tests for each candidate. According to Bliss and Associates, the cost of advertising for a position ranges from a \$200.00 classified to a \$5,000.00 or more display advertisement, agency costs at 20 - 30% of annual compensation.

Training is another example of "blended" costs. Beyond the cost of new hire training, a company has invested in the person who is leaving, the cost of orientation, and job-specific training in terms of the new person's time salary and the cost of the person who conducts the training must be factored in. We also need to include the direct costs of training materials such as workbooks, folders, identification cards, technology and/or space required to deliver the training, etc. Lastly, let's not forget to include the new hire costs outside of training such as laptops, telephone hook-ups, credit card accounts, mobile phones, business cards, and so on!

As you can see, the costs and impact associated with an employee who leaves a company can be quite significant.

So What *is* Employee Turnover Really Costing Companies?

While employee turnover is one of the largest costs in all different types of organizations, it's also one of the most unknown costs. Companies routinely record and report costs such as wages and benefits, Workman's Compensation Insurance, utilities, materials, and space, yet research indicates that few companies have a consistent commitment or process for measuring and reporting the cost of employee turnover.



Most organizations simply track their basic employee turnover rates on a month by month or year by year basis by applying this common formula:

$$\frac{\text{Total number of leavers over period} \times 100}{\text{Average total number employed over period}}$$

More complex approaches to employee turnover costing give a more accurate and invariably higher estimate of total costs. Several well-regarded studies have begun estimating the true cost of losing an employee. For example, SHRM, the Society for Human Resource Management, estimated that it costs \$3,500.00 to replace one \$8.00 per hour employee when all costs were considered. SHRM's estimate was the lowest of 17 nationally respected companies who calculate this cost!

A generally accepted principle is that the cost of turnover is estimated at one to two times the annual compensation and benefits per individual position. In this case, to calculate employee turnover cost, use 100% to 200% of an employee's annual salary.

What retention-focused leader wouldn't want to add \$50 million to their top line?

Let's apply this on the conservative end of this range. Assume the average salary of employees in a given company is \$50,000 per year. Taking the cost of employee turnover at 100% of salary, the cost of turnover is then \$50,000 per employee who leaves the company. For the mid-sized company of 5,000 employees who has a 10% annual rate of employee turnover, the annual cost of employee turnover is \$25 million! What about the company with 10,000 employees? The cost of turnover equals \$50 million! What retention-focused leader wouldn't want to add \$50 million to their top line?

Although useful, recognize that general "rule of thumb" estimates can be misleading since direct and indirect costs vary greatly in a diverse and complex workforce. Actual turnover costs are usually much higher than we think they are!

TalentKeepers' Solutions

TalentKeepers recommends monitoring employee retention statistics, turnover costs and causes, as well as best practices of other local employers on a monthly basis. To identify that a problem exists, a company will need to rely on company comparisons. Benchmarks will allow you to not only determine how many similar companies are doing better, but will define criteria for improvement.

TalentKeepers' Strategies for Being on Top of Employee Turnover Costs

- Know how employee turnover rates are determined.
- Check your employee turnover rates.
- Know how costs associated with employee turnover are determined.
- Monitor retention practices of other local employers.
- Research best practices.
- Evaluate your findings that will drive business goals.
- Communicate team retention issues and employee turnover costs to superiors.

We know that determining the cost of employee turnover can feel a bit challenging; therefore we would like to invite you to access our website at www.TalentKeepers.com and utilize our online cost calculator to determine the direct and indirect cost per job title. This quick and effective tool will breakdown key items and show you how to calculate the actual costs for positions within your organization. Gaining access to this data is a powerful way to evaluate how your competition measures up to your organization.

Furthermore, if you would like to benchmark your data with other industry-like positions, please contact us at solutions@talentkeepers.com or call 407.660.6041 x124 for assistance. One of TalentKeepers' experts can help you decipher your key data inputs and help you feel more confident with communicating your employee turnover cost to Senior Leadership.

TalentKeepers has helped thousands of leaders improve skills with their teams through our blended-learning leadership training programs. **Retention Monitor** and **Retention Expert** are two of a series of leadership training programs that will help your leaders better understand the cost, causes, and consequences of employee turnover and share best practices to keep leaders forward-thinking with regards to employee retention.

Conclusion

Future success depends on effective human capital management, and this begins with identifying, analyzing, and evaluating data about a company's human resource assets and then measuring them against best practices for similar companies.

Companies that fail to see the importance of measuring the cost of employee turnover — especially the price of losing high-performing talent— is allowing dollars to slip away instead of adding them to their bottom line. The time to measure is now. Waiting until there's a crisis limits options to prevent or correct employee turnover causes.



Talent Management Solutions

TalentKeepers[®] is celebrating 15 years of providing award-winning employee engagement and retention solutions to help companies around the globe increase their performance. We're a recognized leader in innovative onboarding tools, employee engagement surveys that drive growth and accountability, HRCI and SHRM certified training for HR professionals, unique eLearning leadership programs, teambuilding tools and much more. Twice we have won HR Executive Magazine's Product of the Year award. Re-energize your efforts and expect more from your engagement and retention partner. Contact us today at solutions@talentkeepers.com.

Leadership Training Programs

All of TalentKeepers training and development programs are built around critical competencies and designed to give leaders the skills they need to be increasingly effective in their careers. Leaders learn talents including Trust Builder, Flexibility Expert, Talent Developer & Coach and High Performance Builder in a total, blended learning approach including e-learning modules, reinforcement workshops and off-line practice activities.

Employee Engagement Solutions

Retaining and actively engaging high-performing employees builds strength in an organization's culture and improves overall performance. TalentKeepers offers several tools proven to increase commitment and positively impact engagement and productivity.

Surveys/Assessments

TalentKeepers' surveys and assessments can help you measure and report the impact of critical factors that contribute to engagement and the degree of influence those factors have on employees' decisions to join, stay or leave your organization.

For details on our Talent Management Solutions or to get more information on TalentKeepers' full range of products and services:



Call us! 407-660-6041



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