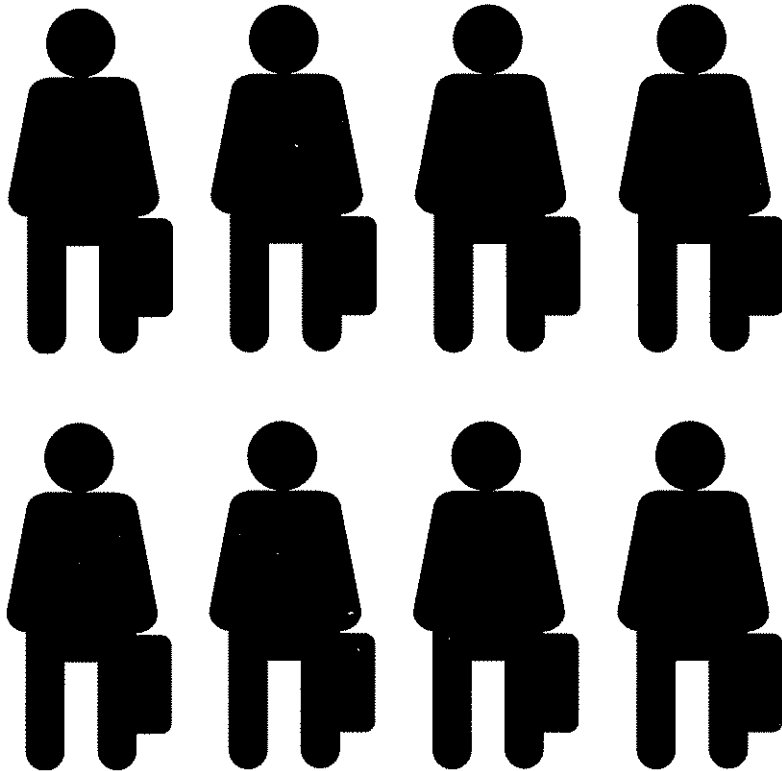


(human resources)



10 questions for calculating how much it costs you not to redress problems related to high employee turnover

By Neale O'Connor

# Putting a Price on \$ Staff Turnover

**T**here are several steps that firms can take to redress high staff turnover. Such steps include reviewing the human resource selection process, career development, socialisation (including general training), and compensation practices. As these practices are critical to the smooth functioning of the organisation, it is important to have an understanding of the costs and

benefits associated with each of them. This article poses 10 questions to ask in order to gather the information needed to make a reliable assessment of the costs of voluntary turnover. Data from a European electronic equipment manufacturer (Bernard) with an assembly plant in China with 65 operational employees is used to illustrate the answers to these questions and the nature of costs involved.

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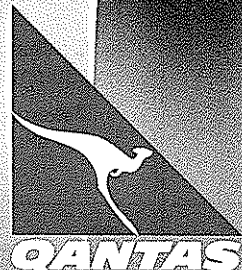
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### Costs of Employee Turnover

There are three parts involved in calculating the costs of a single employee turnover unit. They are:

- the identification and accumulation of tangible and intangible costs into a cost pool;
- the allocation of these costs to a cost object (i.e., a single employee in a particular function, e.g., an operational employee in Bernard); and
- the multiplication of this cost per employee by the number of voluntary turnover employees.

It is possible that the number of voluntary turnover employees be reduced by the number of involuntary turnover employees (those employees forced to leave because of poor performance and non-fit with the position that was allocated. This will then provide an estimate of the cost of total turnover for the firm.

### Tangible Costs

Tangible costs refer to the labour costs (and for larger firms, related building costs) associated with the various human resource management practices. These costs include separation costs (associated with finishing

the employment), replacement costs (associated with advertising, interviewing and hiring), and training costs (associated with bringing new employees up to speed so that they become productive for the firm). Questions 1 and 2 seek information on the monthly salary of the various levels of employees plus the number of employees at each level. The salaries for each level are converted into an annual salary and multiplied by the number of staff in each level. For Bernard, in China there are two human resource management staff (monthly salary of HK\$3,250), eight managers in charge of the operations (HK\$4,875) and 65 operational employees (HK\$1,417) (see Table 1). These salary amounts are multiplied by 12 and then by the number of staff in each level.

In order to allocate these costs to the cost object (a single employee), question 3 seeks information on the percentage of time spent by the human resource managers and other managers on separation, replacement and training practices. The total in the salary cost pool for each employee function (e.g., human resource managers, supervisors, non-HR managers) is multiplied by the percentage and divided by the number of employees to obtain a cost per employee. For

**Table 1 Collection of Tangible Costs and Labour Activity Data**

Monthly Salary		Current Year
1. What is the monthly salary of the various HRM supervisory (managerial) personnel and employees?	HRM staff	HK\$3,250
	Managers/Supervisors	HK\$4,875
	Operational employees	HK\$1,417
2. How many managers and supervisors are there?	HRM staff	2
	Managers/Supervisors	8
	Operational employees	65
Allocation Base (% allocation of tangible costs)		Current Year
3. What percentage of your HRM and supervisor manager time is spent on the following activities?	HRM %	
	Selection (including replacement)	25%
	Career development	14%
	Socialisation (training)	11%
	Compensation	10%
	Separation*	20%
	Non-HRM %	
	Career development	27%
	Socialisation (training)	43%
	Separation*	4%
Selection (including replacement)	25%	
Other Costs		Current Year
4. How much are the advertising and material costs?	Advertising	HK\$
	Training, other material	HK\$
5. What is the depreciable value of building space and equipment used for training and other HRM activities?	Building costs	HK\$
	Equipment costs	HK\$
* Note that separation activities do not affect turnover like the other activities listed		

Bernard, the human resource managers spent 30 percent of their time on separation practices, 10 percent of their time on replacement practices and 11.4 percent of their time on training practices. These percentages are multiplied by the total annual salary costs for the two human resources managers (HK\$78,000) for an allocation of HK\$40,092 across the 65 employees. A similar calculation is made for the non-HR managers involved in the replacement and training practices.

Questions 4 and 5 seek information on other relatively minor costs associated with the HRM activities in the firm. Question 4 asks: how much are the advertising and material costs? While question 5 asks: what is the depreciable value of building space and equipment used for training and other HRM activities? If there is a dedicated room for training then an estimate of the depreciable cost of this room needs to be made. This cost will likely be more relevant if training is believed to be effective in reducing the level of voluntary turnover, which might call for further expansion of the training facilities. But in most firms, labour costs will dominate the tangible costs and be sufficient for determining the tangible costs

associated with voluntary turnover. For Bernard, there is a nil response to these questions.

#### Intangible Costs

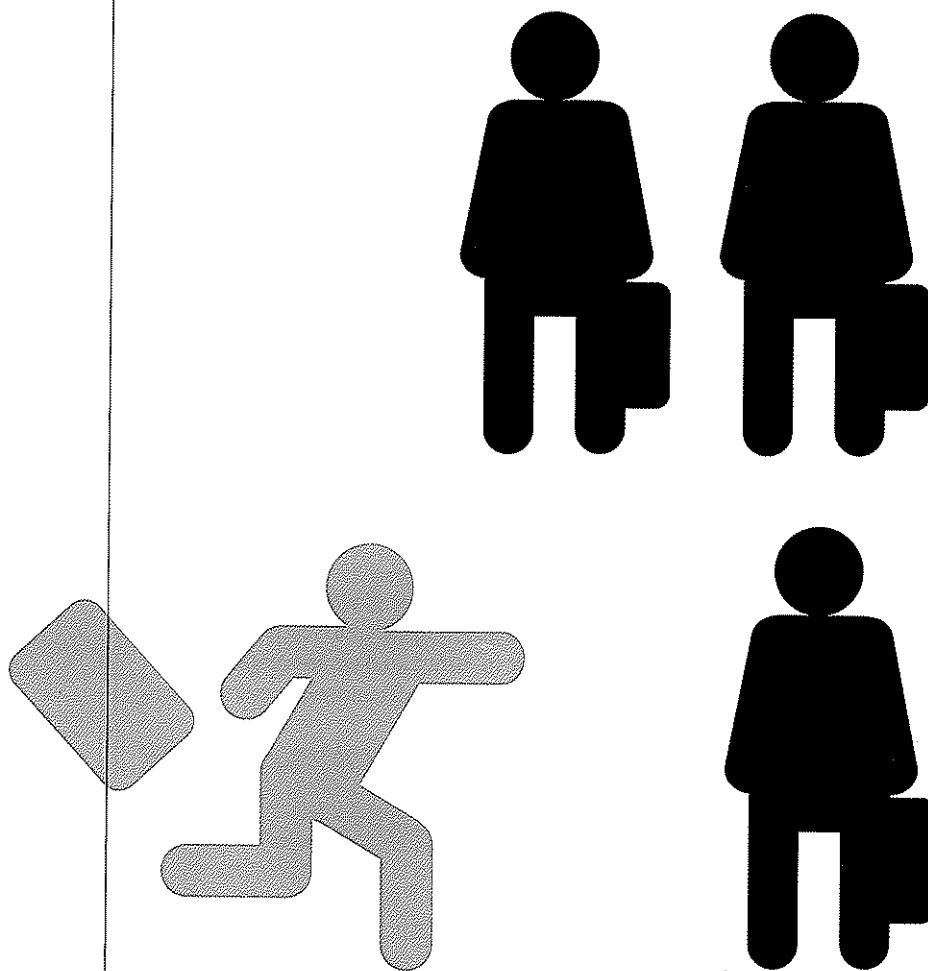
Intangible costs refer to the hidden costs associated with lost production, disruption and retraining associated with gaining a full replacement of the departing staff. In order to estimate the costs of lost production, question 6 seeks information on the time it takes to find a suitable replacement and question 7 seeks information on the gross profit per worker (see Table 2). For Bernard it takes five days to replace an employee and the gross profit per worker is HK\$4,160 per month (see Table 2). To estimate the costs of disruption question 6 seeks information on the costs of disruption in terms of the extra time taken by managers and supervisors in coordinating and rescheduling. For Bernard supervisory disruption was estimated to be an equivalent of five manager working days (see Table 2).

The final part of intangible costs calculation is to estimate how long it takes for a new employee to learn the various systems in your firm in order to become a productive employee (see question 9, Table 2) and what

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**Table 2 Collection of Intangible Cost Data**

Productivity Costs		Current Year
6. If an employee were to leave your firm, how long does it normally take to find a suitable replacement?	<b>Cost of Vacancy</b> # of days to replace	5
7. What do the operational (turnover) employees do to add value to your firms operations?	<b>Loss of Productivity</b> <b>Gross Profit per Worker</b> Sales revenue per watch GP% GP per watch Watches per hour Watches per day GP per day Productivity per month	HK\$5.00 20% HK\$1.00 HK\$20.00 160.00 HK\$160.00 HK\$4,160.00
Supervisory Disruption		Current Year
8. If an employee were to leave your firm, how much disruption is caused in terms of supervising and coordinating activities? (eg overtime, rescheduling, etc.)	Managers Supervisors	5 0
Employee Learning		Current Year
9. How long does it take for a new employee to learn the various systems in your firm in order to become a productive employee	<b>How long does it take to learn the:</b> Formal System Informal System Networks and Contacts	3 6 12
10. What is the average learning rate? - linear = 50%, Learning curve = 51% - 99%	Formal System Informal System Networks and Contacts	50% 6 12



Bernard) is achieved by finding the monthly salary for an operational employee (HK\$1,417) and multiplying this by the number of months required to learn the formal and informal systems, and the necessary external networks and contacts.

#### Computing the Voluntary Turnover Cost

To identify the number of employees that have left in the past 12 months, information is sought for both voluntary and involuntary departures. In Bernard's case 33 operational employees left voluntarily and 15 left involuntarily. This data allows us to calculate the amount of the voluntary turnover cost. The total cost of HRM practices pertaining to turnover per employee is estimated at HK\$22,839 and given 33 employees voluntarily left the firm makes for a total turnover cost of HK\$753,679. This accounts for about 68 percent of the total operational employee salary (HK\$1,105,003).

#### Assumptions

The information provided in Bernard's case largely pertains to the cost of labour and the nature of the job that is the focus of voluntary employee turnover. To be more accurate one might need to include the opportunity cost of assets such as building space used to house the human resources department and other expenses such as the cost of advertising and stationary. As with most issues involving cost allocations there are assumptions regarding the estimates of the intangible costs such as the amount of time it takes to learn the informal networks and relevant contacts.

There are two main benefits for calculating the costs of voluntary turnover. First, working through the 10 questions helps to raise awareness of the real cost of voluntary turnover and the factors that cause such turnover. Over time, more accurate estimates can be made as our understanding of the time it takes to bring employees up to the desired level of productivity improves. Second, the costs of voluntary turnover serve as a starting point for evaluating the potential benefits associated with investing in the various human resources practices such as selection, career development and compensation structure.

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is the average learning rate (i.e., linear learning rate = 50 percent, a learning curve effect = 51 percent – 99 percent; see question 10, Table 2). An estimate is made for the time it takes to learn the formal and informal systems, and the networks and contacts. While an estimate of learning the formal system might range from a few days to several weeks, estimating the time taken to develop sufficient networks and contacts in some positions can take 12 months or more. Hence, estimates of the value of learning the latter might need revising according to the amount of information that is available. For Bernard, the estimate is three months to learn the formal system, six months to learn the informal system and 12 months to establish a reasonable network and list of contacts.

The allocation of the loss of productivity costs to the cost pool (operational employee in the case of Bernard) is achieved by finding the equivalent days salary for the cost of the vacancy (HK\$1,417), loss of productivity (HK\$4,160), and supervisory disruption (manager salary of HK\$4,875), and multiplying this output by the number of days (five) it takes to replace an operational employee. The allocation of the time it takes for a new employee to become job proficient (operational employee in the case of