In recent years, turnover rates have steadily increased as a result of factors such as lower unemployment rates, skill shortages in the labor market and an increasing number of retiring Baby Boomers. While a certain amount of turnover will always exist in an organization, high turnover can take its toll. Not only can it damage morale and harm company culture, but it also leads to significant financial costs.

Just how much does turnover cost your organization? The answer is not always easy to pinpoint. In this guide, we will walk you through the process of determining the real cost of turnover to help your organization make informed decisions. Specifically, we will cover:

- Facts on employee turnover
- The importance of tracking turnover
- A sample costing model for turnover
- Examples for calculating turnover costs
- Communicating turnover data to leadership
- Suggestions on strategic uses for your data

Let’s begin by taking a look at how turnover has changed recently, and what it means for businesses today.
Identifying the Real Cost of Turnover

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Turnover Facts

Unemployment rates are hitting record lows, with more than 10 states currently experiencing the lowest rates they’ve seen since beginning to measure unemployment. According to the U.S. Bureau of Labor Statistics (BLS), the unemployment rate for college-educated workers is just 2.1%.

During the recession, college graduates had difficulty finding jobs, so many people stayed in school and pursued advanced degrees. As a result, they had little to no actual work experience. Now, however, the availability of work has allowed younger generations of workers to gain experience. In pursuit of the best possible work experience to support their overall career goals, these workers are changing jobs more frequently than previous generations.

In fact, Millennials – who are now the largest generation in the workforce – average four jobs within the first decade of finishing their degree. Generation X employees averaged only two jobs in their first ten years in the workforce. Gallup estimates Millennial turnover costs the U.S. economy as much as $30.5 billion annually.

For employers to stay competitive, it has become essential to confront turnover head-on. While total turnover has risen within recent years, voluntary turnover has increased by more than 48% in less than a decade. In 2010, voluntary separations hovered around 9%, but they have climbed steadily in recent years and are now at 13.5% according to Compdata Surveys & Consulting’s BenchmarkPro survey results.

Many business experts suspect employers will continue to compete for labor through the next decade. With growing skill shortages and Baby Boomers reaching retirement age, these turnover rates will likely stick around, and perhaps even rise. Employee Benefit News reported last summer that employee retention is becoming organizations’ biggest concern, and statistics from Future Workplace and Kronos show 80% (of employers) consider improving retention a critical priority.

Indeed, addressing turnover is important, but just how critical is it? Let’s take a look at some of the ways high turnover rates can impact your organization.
Why Track Turnover?

The cultural impact of turnover creates a vicious cycle: as employees begin to see an uptick in voluntary separations, they lose motivation and morale drops. Over time, employees may become disgruntled and performance drops below acceptable levels. You may therefore be forced to increase terminations, which only exacerbates the turnover issue. When performance is low and high performers are forced to pick up the slack, turnover may rise, and the cycle continues. Thus, high turnover rates often cause employers to lose high performers, because these employees get noticed and are more likely to get recruited away.

Of course, the effects of turnover are not just cultural. From a financial standpoint, filling the same position over and over is like throwing money out the window.

In addition to the reasons listed above, there are additional incentives for tracking turnover. For one, turnover impacts all areas of the business, so addressing it can support better overall growth. When your company retains seasoned, well-trained employees, it is more likely to maintain a competitive edge. For another, tracking turnover rates provides specific metrics for a problem, which can be used to address the issue more effectively and prioritize areas for improvement. Having metrics will also allow you to validate proposed solutions to leadership.

Hard & Soft Costs of Turnover

With such a widespread impact on many facets of business, calculating the full cost of turnover can be challenging. Nonetheless, by considering a few key factors, you will be able to create a more complete and accurate picture.

The potential soft costs of turnover include decreased employee engagement, lower quality of customer service or higher occurrence of errors, and the negative effect on company culture described above. In terms of hard dollar costs, consider expenses incurred: from recruiting or agency fees, to training new employees, loss of productivity, or possible overtime pay.
Why Should HR Track Turnover?

Rising turnover is not necessarily a result of internal issues. In many cases, it is a byproduct of the strong economy. Nonetheless, it must still be addressed internally. While HR does not cause turnover directly, it is often put in charge of handling the issue. By starting a conversation about turnover across the organization, HR professionals can ensure the matter is addressed by the people who can play a role in changing it. Ultimately, HR will likely be seen as part of the solution or part of the problem, so by confronting the challenge proactively, they can be viewed as a strategic business partner.

Once turnover rates are identified, it then becomes necessary to adopt a model for calculating costs.
Adopting a Costing Model for Turnover

Because some ramifications of turnover are more difficult to measure than others, it is advisable to focus on the data points that are measurable, indisputable, and relevant to operations in your company. When adopting a cost model, analyzing the aspects that are most compelling can increase the odds of gaining buy-in. It is more important for a turnover cost model to have support from leadership than it is for it to be all-encompassing. Plus, when considering the amount of time and effort it might take to produce the broadest possible cost model, most organizations find it is too resource-intensive. Instead of attempting to analyze every minute detail, or oversimplifying the process, a “middle of the road” approach is often effective for the majority of employers.

Factors to Consider

To begin costing turnover, start by gathering a cross-functional team. The team should include HR professionals with responsibilities in talent acquisition, compensation, and HR business partners. It will also be helpful to include someone from finance, and if possible, the CFO. Additional team members could include affected department heads, executives, and operations employees.

After developing your team, the next step is to determine the data points to analyze. Consider the following categories:

- Separation cost: exit interviews, administrative costs, and separation pay
- Acquisition cost: advertising, travel, interviews, assessments, background checks, sign-on bonuses, employee referral bonuses, and relocation
- Placement costs: agency fees, onboarding, training

This list is not exhaustive, but it may serve as a good starting point. Again, it is best to consider the data points most relevant to your organization.
Once you have chosen which data points to analyze, gather the relevant position and company information, including:

- The position’s annual average total cash compensation and benefits
- All positions’ annual average total cash compensation and benefits
- The projected number of exits this year in the position
- Annual revenue
- Number of full-time employees (FTEs)

Additionally, you can look at historical data to determine lost productivity, including the number of days for which the position is typically vacant, and the anticipated days an employee will need to become productive in the role.

**Limitations to Costing Models**

Every cost model will have its limitations, since accounting for 100% of costs typically is not feasible. Trying to account for every dollar may reach a point of diminishing returns. The objective of identifying the real costs of turnover should be to have executive agreement. If you manage your cost model properly, company leadership should be able to look at it and realize you’ve actually been conservative in your calculations of the financial impact of employee turnover. It can serve as a baseline your company can use for developing retention strategies.
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Calculating Turnover

To begin calculating turnover, select a benchmark job to validate internal and external metrics. The position you choose should be visible across the organization, agreed upon by leadership, and a job that would hinder success if significant turnover occurred. The position could be one that experiences frequent turnover; in healthcare, for instance, this could be a nursing position. Or, it may be one that is especially costly to replace, such as an IT director, or a position that is difficult to do without because it demands special knowledge of your business.

Once you’ve chosen a position, you can then begin analyzing cost factors. Here is an example of the cost factors you might look at for the role of Accountant 1:

- All Accountant 1’s annual average total cash compensation and benefits: $74,000
- All positions’ annual average total cash compensation and benefits: $81,000
- Projected exits for Accountant 1 this year: 5
- Annual revenue/number of FTEs: $400,000
- Separation cost: $1,000
- Acquisition cost for one new employee: $3,000
- Placement costs: $4,000
- Average number of days position is open: 25
- Number of days for employee to become productive in job: 30
- Number FTE workdays per year: 240

Then, you can calculate the gross lost productivity using the following steps:

1. Determine the daily revenue attributed to each employee:
   $400,000 EE revenue/240 workdays = $1,667 per day

2. Compare the average annual total cash compensation and benefits of Accountant 1 ($74,000) to that of all positions ($81,000)
   $74,000/$81,000 = .91
3. Determine daily revenue attributed to an Accountant 1
$1,667 employee daily revenue x 0.91 = $1,517

4. Calculate total gross lost productivity by multiplying the number of days for Accountant 1 to become productive by the daily revenue attributed to an Accountant 1
$1,517 daily revenue x 30 days = $45,510

Thus, for a vacant Accountant 1 position, you can see that the total gross lost productivity amounts to $45,510 in this scenario.

Of course, while the position is vacant, the organization does not pay compensation and benefits. Thus, to calculate the total net lost productivity, you can perform the additional steps:

1. Determine total cash compensation & benefits saved per day during vacancy.
   $74,000/240 days = $308.33/day
2. Multiply daily amount saved by number of days vacant.
   $308.33/day x 25 days = $7,708
3. Subtract total cash compensation and benefits saved from total gross lost productivity.
   $45,510 - $7,708 = $37,802

The total net lost productivity for the vacant Accountant 1 position is therefore $37,802 in this example. However, if you add the costs of separation ($1,000), acquisition ($3,000), and placement ($4,000) to that figure, the total cost of turnover for an Accountant 1 becomes $45,802. If there are five projected Accountant 1 exits during the year, turnover in the position is projected to cost $229,010.

If you could reduce the turnover for this position by 20% in this scenario, you could save the company $45,802. Reducing it by 50% would save $114,505 annually!

Once you have assessed turnover for one position, you can repeat the process to calculate the total cost of turnover for each position, department, and ultimately, for the organization overall.

Clearly, calculating the cost of turnover can yield eye-opening insights. The question then becomes: how can HR communicate these finding to leadership to present a compelling argument for change?
Communicating to Leadership

To clearly communicate your company’s turnover metrics to leadership, be sure to relay the information in a way that executives will appreciate. In other words, speak their language. Be concise, explain the data set used, and present charts, graphs, and other easy-to-read visuals to illustrate your point. Remember that executives often need to analyze overall effects on the organization. Make the report an executive summary of your findings, but be prepared to back it up with supporting details or calculations when asked.

How to Use the Cost of Turnover Metric

After these findings have been made, the organization can begin a dialogue on how the cost of turnover metric should be used. Investing in employees helps companies manage turnover, and if you are able to present projected cost savings, you can justify these programs to garner support from the leadership team.

One area in which employers look to be competitive in this tight labor market is employee compensation. The digital age has empowered employees, so that they now have access to websites where they can gauge competitive wages. Pay is also shared openly with peers and friends, so it is now more critical than ever for employers to ensure they are offering competitive compensation.

Career advancement opportunities also play a role in supporting retention. According to Middlesex University’s Institute for Work Based Learning, 74% of employees don’t feel they are achieving their full potential at work due to lack of development options. Employers must clearly communicate all of the ways employees can thrive inside the organization. When possible, employers should present more career mobility options and ensure managers are providing their direct reports with new opportunities. Assuming your employees understand how they can progress within the company can be dangerous. Many employers have spent time creating career ladders, however, without proper communication of those programs, the efforts are wasted. Taking the time to define existing career opportunities can be a cost effective way to increase employee awareness thereby improving retention.

Investing more into direct learning expenditures for employees can also help companies stay competitive, and flexibility is a primary interest for today’s employees. If possible, consider offering benefit options, flexible work schedules, or telecommuting to support work/life balance.
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Retaining Millennials

Millennials are now the largest generation in the workforce, making it crucial to recruit and retain millennial employees. Here are some interesting findings from Intelligence Group your organization may be able to leverage for increased retention:

- 64% consider making the world a better place a priority
- 72% want to be their own boss
- 74% seek flexibility in their work schedule
- 79% prefer a coach or mentor to a boss
- 88% prefer a collaborative – not competitive – culture
- 88% desire work/life integration

Because making the world a better place is a priority to this generation, employers might consider sponsoring volunteer opportunities, or developing company teams for local charity runs or walks. While HR might be responsible for these events, it’s also possible you could designate a volunteer to run them!

It is not realistic for very many companies to allow employees to be their own boss. However, you can make employees feel as if their voices are heard. Consider scheduling open forums to cover important topics, adopting self- and peer-evaluations to support a collaborative culture, and encourage managers to share as much as possible with their teams. Make sure employees feel included on the plans for today, tomorrow, and how the business is growing overall.
Summary

Identifying the real cost of turnover requires an investment of your company’s resources, including the time and efforts contributed by HR. Yet, addressing turnover is critical not just for strengthening company culture, but also for lowering costs and staying competitive.

To recap some of the main ideas discussed in this guide, here are some key takeaways:

◉ With skill shortages, low unemployment rates, and the retirement of Baby Boomers, high turnover rates are here to stay through the next decade. Because turnover has become the foremost concern for many employers, those who choose to address it proactively will have the best odds of boosting retention and staying competitive.

◉ While HR is often viewed as being responsible for handling turnover, they are not the direct cause for high turnover rates. In the current competitive labor market, high turnover is often a result of economic factors, but there are still internal tactics employers can use to drive retention.

◉ Tracking turnover is critically important because it impacts all aspects of the business. Knowing the cost of turnover provides a metric to the problem, helps prioritize areas for improvement, and enables HR to validate their proposed solution to leadership.

◉ Turnover leads to both hard and soft costs, but to create an effective cost model, it’s best to focus on data points that are measurable, indisputable, and relevant to operations.

◉ To create a turnover costing model, gather a cross functional team, determine appropriate data points, select a job to validate, and run turnover calculations.

◉ Once turnover costs have been developed, findings must be presented in a way that resonates with executives. Only then will HR be able to secure buy-in for strategies and programs that will drive retention.

Although reducing turnover can be difficult, even slight progress reduces costs and improves company culture. As we saw in the example, reducing turnover for just one position can save your organization significant sums of money, improve retention rates, and boost morale. When HR teams identify the real cost of turnover, logically communicate its financial implications, and take action to reduce it, it can have a positive impact to the organization as a whole.
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