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KEY PERFORMANCE INDICATORS OF THE HR FUNCTION

Summary. The purpose of this article is to explain the Key Performance Indicators of the HR Function in order to evaluate the HR Effectiveness of an organization. Since employees are the most important assets and key enablers of future success, which often requires considerable investment, it is therefore important to understand to what extent they add value to the financial performance of the organization.

Keywords: key performance indicators, KPI, employment costs rate, retention rate, employee tenure, absenteeism, overtime rate, salary survey, time to hire, training hours, training cost, Kirkpatrick's training effectiveness assessment, Philips ROI model

PODSTAWOWE WSKAŹNIKI EFEKTYWNOŚCI FUNKCJI HR

Streszczenie. Celem artykułu jest wyjaśnienie kluczowych wskaźników efektywności funkcji HR wykorzystywanych do mierzenia skuteczności procesów związanych z zarządzaniem zasobami ludzkimi w organizacji. Z jednej strony, to właśnie kapitał ludzki jest czynnikiem, który decyduje o różnicach między organizacjami i stanowi podstawę przewagi konkurencyjnej, z drugiej jednak, wymaga ponoszenia znacznych inwestycji przez przedsiębiorstwa. Ważne jest zatem, aby zrozumieć, w jakim stopniu wydatki związane z utrzymywaniem pracowników w organizacji przyczyniają się do poprawy wyników finansowych organizacji.

Słowa kluczowe: podstawowe wskaźniki efektywności funkcji HR, wskaźnik kosztów zatrudnienia, wskaźnik retencji, średni staż pracy, wskaźnik absencji, wskaźnik nadgodzin, raporty płacowe, średni czas rekrutacji, wskaźnik ilości godzin szkoleniowych, koszty szkoleń, ocena efektywności szkoleń Kirkpatricka, model Philippsa zwrotu z inwestycji w szkolenia

Among the many building blocks constituting a company's value, it is the people who play a vital role in this value make up as they are the possessors of knowledge. Due to the fact that human capital is a factor that determines the differences between organizations and is the basis for competitive advantage, the Human Resources function is now beginning to take on a more strategic role in the organization.

The main characteristic of HR is evolving in the direction of a leader who proactively affects the business. In order for the human resources department to become more efficient, it is not only to become a partner for senior management, but above all to participate in the decision making process. Since the ultimate goal is to be value creation for stakeholders, with efforts focused on the return on human capital, only by human capital analysis and measurement it is possible to assess direct return on investment and ultimately create company's strategies in a more structured way.

Performance measurement is maintained in organizations because it helps to align daily activities with strategic objectives.¹ KPIs focus on those aspects of organizational performance that are the most critical for the current and future success of the organization.²

The purpose of this paper is to explain the Key Performance Indicators of the HR Function in order to evaluate the HR Effectiveness of the organization. In many businesses, employees are not only the most important assets and key enablers of future success but often represent considerable investments. It is therefore important to understand to what extend employees add value to the financial performance of the organization.³

The HR KPIs are metrics related to self-development and humans as resources. They can illustrate the retention rate, participation in trainings, average number of overtime per employee, average cost of training per employee, and holiday utilization.

The HR metrics below will be described in more details. They were presented in five categories:

- HR General.
- Retention and Absenteeism.
- Benefits.
- Recruitment.
- Trainings and Employees' Development.

¹ Parmenter D.: Key Performance Indicators (KPI): Developing, Implementing and Using Winning KPIs'. Wiley, New Jersey 2010, Kindle Loc. 105.

² Ibidem, Kindle Loc. 278.

³ Marr B.: Key Performance Indicators (KPI): The 75 measures every manager needs to know (Financial Times Series). Pearson, 2012, p. 254.

1. HR General

1.1. Employment costs rate

The total costs of employment include wages, bonuses, fringe benefits, social security payments, taxes, trainings, overtime, and recruitment costs.

$$\text{Employment costs rate} = \frac{\text{Total employment costs in a given period}}{\text{All company's costs in a given period}}$$

Fig. 1. Employment costs rate formula

Rys. 1. Wzór do obliczania wskaźnika kosztów zatrudnienia

It is impossible to provide a generic benchmark when it comes to the employment costs rate. Industries that have large infrastructure costs – have lower salaries as a percentage of operating costs. This is because equipment expenses are high in relation to salary costs. On the contrary, consulting companies that generate revenue by billing out their consultants' time to clients and do not have high infrastructure costs typically have a much higher salary as a percentage of operating expenses.

Employment costs rate can be used to evaluate competitiveness of a company's salaries in relation to operating expenses within their industry. For example, when the metric of salaries as a percentage of operating expenses is greater than that of the competitors, it could mean that the salaries may not be as competitive or that the company does not have enough staff relative to its competitors to achieve business results. Apart from doing the benchmark on the industry level, it is recommended to track the employment costs rate over time within the organization and analyse the grounds of the possible ratio changes.

2. Retention and Absenteeism

2.1. Retention rate

The retention rate answers the question about how successful the company has been in keeping the employees in the organization. Attracting, recruiting, training and developing talented staff takes time and is costly. This is why the organization wants to make sure that once it has identified and trained employees, they will be retained in the company for a reasonable period of time. Replacing employees is expensive. In addition to training costs, there is the cost of recruitment and, even for the best-educated or most professionally qualified staff, a cost associated with adapting them to the new organization. There is also the

problem of tacit knowledge associated with an employee leaving the company. Consequently, the measure of employee turnover rate is used to gain an insight into how many employees the company is losing in a given period of time in comparison to the overall number of employees.

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

Fig. 2. Retention rate formula

Rys. 2. Wzór do obliczania wskaźnika retencji

The total figure illustrates all leavers, even people who left involuntarily due to dismissal, redundancy or retirement. Employee turnover can be measured in any period. It is though common for the data to be collected monthly.⁴

In order to compare employee turnover rate across industries, consulting companies offer annual surveys covering HR metrics. Such benchmark data provides valuable insights into how well other similar organizations are retaining their employees when faced with similar economic challenges. In Poland, it is the HayGroup that provides the annual HR metrics report called Navigator HR.⁵

The straightforward employee turnover rate calculation can be modified in such a way as to distinguish between regretted and non-regretted leavers, as there will always be departing employees that the organization is willing to dismiss.

Exit interviews, in which the departing employee is interviewed as to the reason for their leaving, can be a useful way to begin to understand the drivers of turnover so that appropriate interventions can be made.⁶

2.2. Average employee tenure

It is required for the companies to understand how long on average employees stay with their organization. Long average employee tenure usually indicates that employees are more loyal and dedicated to the company. It will generally help to reduce recruitment and training costs. Long average employee tenure can also indicate that employees might be too comfortable in their occupation and that maybe not enough new and innovative ideas are brought into the company.

⁴ Ibidem, p. 275.

⁵ HayGroup Corporate Site: www.haygroup.com/pl/services/index.aspx?id=29407, 29 March 2014.

⁶ Marr B.: op.cit., p. 277-278.

It can also be compared with average tenure for the industry in order to assess the company's competitive standing.⁷

$$\text{Average employee tenure} = \frac{\text{Sum of all tenures}}{\text{Number of employees}}$$

Fig. 3. Average employee tenure formula

Rys. 3. Wzór do obliczania średniego stażu pracy w jednym przedsiębiorstwie

Average employee tenure should be measured annually.

According to the OECD data, the average job tenure in Poland in 2012 was over eleven years.

Table 1

Average job tenure in the OECD countries (2012)

	Average job tenure 2012		Average job tenure 2012
Austria	10,9	Korea	5,3
Belgium	12,0	Luxembourg	10,8
Czech Republic	10,5	Netherlands	10,5
Denmark	8,9	Norway	9,8
Estonia	8,6	Poland	11,4
Finland	11,0	Portugal	13,5
France	11,9	Slovak Republic	10,3
Germany	11,5	Slovenia	13,0
Greece	13,9	Spain	11,5
Hungary	9,8	Sweden	10,4
Iceland	8,8	Switzerland	9,7
Ireland	10,8	United Kingdom	9,4
Italy	13,1		

Source: OECD.⁸

2.3. Absenteeism

When employees are absent from work it requires from the company additional expenditures and causes disruptions. The costs include the costs of the illness payment, replacing the employees and possible overtime payments, as well as the effect the absenteeism has on the quality of the services delivered by the company.

Absenteeism is defined as an employee's unavailability for work. There are different types of absenteeism: legal (such as public holidays), authorised (such as approved holidays) and unauthorized. While legal and authorised absenteeism are manageable, it is unauthorized absence that causes the majority of problems. This is why most organizations strive to avoid unauthorised absenteeism and keep it to a minimum.⁹

⁷ Ibidem, p. 279, 281.

⁸ OECD.StatExtracts, Employment by job tenure intervals – average tenure https://stats.oecd.org/Index.aspx?DataSetCode=TENURE_AVE, 29 March 2014.

⁹ Marr B.: op.cit., p. 282-283.

Indicator of absenteeism

$$= \frac{\text{Total number of days of absence}}{\text{Number of working days}} \times \text{Average number of employees}$$

Fig. 4. Indicator of absenteeism formula

Rys. 4. Wzór do obliczania wskaźnika absencji

The indicator of absenteeism informs about the loss of the total budget of working time due to the absence of employees. ‘Total number of days of absence’ includes mainly sickness absences. The category does not include holiday, maternity, occasional nor parental leaves.

The level of disruption (and therefore costs to the business) is particularly high when employees take frequent, short and unplanned absences. Measuring those short and unauthorised absences in the organization is a way to identify whether the illness absenteeism needs to be analysed in greater detail.

$$\text{One – day – absence indicator} = \frac{\text{Number of one – day – absences}}{\text{Total number of days of absence}}$$

Fig. 5. One – day – absence indicator formula

Rys. 5. Wzór do obliczania wskaźnika jednodniowych absencji

The one-day-absence indicator informs about the percentage of one-day-absences in the total number of days of absence.

It is most common to measure both the absenteeism ratio as well as the one-day-absence ratio on a 12 months rolling basis, but some companies may want to measure it monthly or quarterly to identify issues in the short term and monitor progress against absenteeism reduction targets.

While both absenteeism ratios are useful key performance indicators, there are often fair reasons for employees to take unplanned leave. Therefore taking the score as the only criterion is not recommended; instead it should only be a trigger for line managers to investigate individual absenteeism further.¹⁰

According to ZUS, the average number of sick days in Poland was 17 days per person in 2012.¹¹ Over 50% of the sick leave certificates were issued due to short-term, i.e. 1-10 days absences.

¹⁰ Marr B.: op.cit., p. 284-285.

¹¹ Calculation was made based on data publicized by ZUS [*Social Security Office in Poland*] and GUS [*Central Statistical Office in Poland*];

- 17 days = (total number of sick days recorded by ZUS in 2012: 246.363.800)/ (total number of people employed in Poland by GUS 14.172.000),

- http://old.stat.gov.pl/gus/5840_670_ENG_HTML.htm,

- <http://www.zus.pl/files/Absencja%20chorobowa%20w%202012%20roku%20.pdf>.

Furthermore, Mercer issued its 2010 Pan-European Survey on Employer Health Benefits conducted in 14 countries across Europe with 556 participants (more than half the respondents have at least 5.000 employees), according to which the respondents from Austria reported the highest absence rates, an average of 9 days per employee per year. Respondents from Germany and France each reported an average absence rate of 8 days. Companies in Poland and the Netherlands reported an average of 7, the Czech Republic and Italy (6 days for each), UK (5 days), and Ireland, Portugal and Spain (4 days for each). Most respondents (73%) stated that absences tended to be short frequent absences but 27% stated that these were absences of 8 days or greater.¹²

2.4. Overtime rate

Working time is any period during which the worker is working, at the employer's disposal, and carrying out his activities or duties in accordance with national laws and/or practice. The Working Time Directive lays down provisions for a maximum 48-hour working week (including overtime).¹³

$$\text{Overtime Rate} = \frac{\text{Number of overtime hours worked}}{\text{Total number of hours worked}}$$

Fig. 6. Overtime rate formula

Rys. 6. Wzór do obliczania wskaźnika nadgodzin

The maximum overtime rate in a calendar year amounts to 20%.¹⁴

The purpose of measuring overtime in the organization is on one hand keeping a record of the overtime payment and on the other hand complying with the Health and Safety requirements.

Some overtime is inevitable due to employee absences or an unexpected increase in workload. However, excessive overtime can affect quality of work, lower morale and lead to staff illness. Therefore a higher overtime rate should be an alert for time management and people management decisions.

¹² Mercer's 2010 Pan-European Survey on Employer Health Benefits Issue, 25 May 2011, www.mercer.com/press-releases/1416840, 29 March 2014.

¹³ Working Time Directive (Directive 2003/88/EC of 4 November 2003), http://europa.eu/legislation_summaries/employment_and_social_policy/employment_rights_and_work_organisation/c10418_en.htm, 29 March 2014.

¹⁴ Directive 2003/88/EC of the European Parliament and of the Council of 4 November 2003 concerning certain aspects of the organisation of working time: Member States take the measures necessary to ensure that every worker is entitled to: maximum weekly working time of 48 hours, including overtime.

3. Benefits

3.1. Salary surveys

Job evaluation is the main factor determining the value of respective roles. In order to carry out the evaluation process successfully, the following criteria are taken into account: main responsibilities in a given role, required skills, knowledge and competencies. Introducing the title structure prepared on the basis of job evaluation methodology enables to make consistent comparisons between job families¹⁵ among companies operating within same industry.

Only then it is reasonable for the company to participate in salary surveys conducted by external consulting firms.

When taking part in the survey, each participant is asked to provide full information about wages, qualifications and occupied positions of its employees. The research is organized in such a way that ultimately each participant receives only averaged and aggregated data with no individual input collected from survey participants. The final report includes minimum, median and maximum salary on different job ranks within different job families, and increases in the average salary.

Apart from remuneration, surveys may also include benefits available to the employees, e.g. medical cover, life insurance, and sports club membership.

Having access to market data provides the company with necessary tools for defining its compensation and benefits strategy reasonably as only then can the company carry out the benchmarking process.

The surveys are conducted every six months.

4. Recruitment

4.1. Time to hire

It is important for the company to fill vacant posts. A failure to do so will have negative consequences, which includes a too low number of staff to complete the work, and lost revenue as not all the orders can be fulfilled.

By measuring the time it takes to hire employees, organizations will get an insight into efficiency in filling employee vacancies from initial posting of the job advertisement to the offer acceptance, and consequently start of work. Time to hire is a number of days between

¹⁵ Armstrong M., Cummins A., Hastings S., Wood W.: Wartościowanie stanowisk pracy. Przestrzeganie zasady równej płacy w praktyce. Wolters Kluwer business, Kraków 2008, p. 147.

the date of posting the vacancy and the start date of a new joiner. This figure can be averaged for specific job roles and across the entire company. If averages are used, it is important to highlight outliers that can have an impact on the average data.¹⁶

Additionally, the time to recruit is a number of days between the date of posting the opening and the date of extending the offer to the candidate. The averaged indicator informs about the number of working days required to recruit one employee in the organization.

4.2. Internal Hire Rate

Internal mobility refers to the movement of people between assignments, across functions, divisions and geographies.

$$\text{Internal Hire Rate} = \frac{\text{Number of internal transfers in a given period}}{\text{Number of all positions filled in a given period}}$$

Fig. 7. Internal Hire Rate formula

Rys. 7. Wzór do obliczania wskaźnika rekrutacji wewnętrznej

A more active and open internal marketplace will benefit both business growth and individual development. Employees selected on the internal market are advantageous over those only joining the company, because their knowledge of the organizational culture is already sufficient to freely interact with other employees. There is a tendency observed that for many organizations the internal resources are the primary source of recruitment.¹⁷

4.3. Referral Rate

Employees are in ideal position to be company's ambassadors, identify and refer people with the skills the company is seeking. Employees are well aware of the qualifications required on different positions, as they constitute the company.

A positive thing about the referral program is that an employee wins through benefit rewards and the company benefits by winning a good candidate. Nevertheless, referrals are a cost-effective recruiting channel (compared to recruitment agencies).

¹⁶ Marr B., op.cit., p. 296, 300.

¹⁷ Chojnacki W., Balasiewicz A.: Człowiek w nowoczesnej organizacji. Wybrane problemy doradztwa zawodowego i personalnego. Adam Marszałek, Toruń 2005, p. 201.

$$\text{Referral Rate} = \frac{\text{Number of positions filled with referrals in a given period}}{\text{Total number of positions filled in a given period}}$$

Fig. 8. Referral Rate formula

Rys. 8. Wzór do obliczania wskaźnika rekrutacji nowych pracowników spośród osób uczestniczących w programie poleceń do pracy

5. Trainings and Employee's Development

5.1. Training hours rate

Measuring training hours per person as an average across the organization, typically per year, is a training and development Key Performance Indicator of the training function. Under this category, it is usually the training time per person on training courses captured.

Previous year's total training time per person is a starting point for making any future comparisons. On top of that, organizations take part in the HR Effectiveness Surveys in order to learn about its approach to trainings in relation to the market competitors' trainings execution.

It is important to agree to targets linked to organizational aims and budget. Every year there is the organizational budget set, with its sub-budgets managed by each department separately. The number of affordable training hours can be derived from the budget available.

$$\text{Training hours per person} = \frac{\text{Total number of training hours in a calendar year}}{\text{Average number of employees at the end of the year}}$$

Fig. 9. Training hours per person formula

Rys. 9. Wzór do obliczania wskaźnika ilości godzin szkoleniowych na osobę

5.2. Training costs per employee

Since training is a major component in enhancing employee competencies, tracking the training cost per employee helps to determine the average investment the company made to provide each employee with trainings. This metric can be calculated by dividing the total training cost for an organization by its headcount.

$$\text{Training costs per employee} = \frac{\text{Total training costs in a given period}}{\text{Average number of employees}}$$

Fig. 10. Training costs per employee formula

Rys. 10. Wzór do obliczania wskaźnika kosztów szkoleniowych na osobę

Measuring the training costs per employee is only the initial step in carrying out the evaluation of learning and development's initiatives. Additionally, it is necessary to analyse the effectiveness of training by identifying operational results that the training had on employee performance (Level 3 of the Kirkpatrick's Training Effectiveness Assessment).¹⁸

Both the training hours per employee rate and training costs per employee are determined by the budget available. Nevertheless, it is still possible to make historical comparisons and analyse training budget utilization at the company as well as at the department level.

5.3. Training ROI

Using ROI for the Training Effectiveness Assessment provides information on how training expenditures impact financial performance.

Return on investment is determined by taking the actual cost of the training from the total value of the benefits. This surplus is then divided by the cost of the training.

The first step in measuring ROI is to identify the costs. These are mainly the costs of the training paid to the training provider. Once costs are determined the various benefits can be counted.

Typical benefits to be considered include time savings (they can be calculated by multiplying the number of hours saved by the workers' average hourly salary), absorbing more volume with the existing number of staff, labour savings (less supervision, less overtime), improved productivity (extra goods produced), improved quality, or reduction in expenses.

Table 2

Five levels of the Philips ROI model

Level 1 Reaction: Participants are surveyed to measure their satisfaction with the training program immediately after the event.
Level 2 Learning: This level is where an assessment is made on what participants believe they have learnt in the program (often through the end-of-class evaluation).
Level 3 Application: Questionnaires and surveys (of participants and their managers) are distributed several weeks later to measure the on-the-job behavioural change.
Level 4 Business Impact: At this level, the actual business results of the program are identified and a monetary value applied to the behavioural changes.
Level 5 Return on Investment: This is where actual ROI is calculated having itemized all the costs and benefits at this point.

Source: Marr B.: Key Performance Indicators (KPI): The 75 measures every manager needs to know (Financial Times Series). Pearson, 2012, p. 301-303.

¹⁸ Kirkpatrick D., Kirkpatrick J.: Evaluating Training Programs: The Four Levels. Berret-Koehler, 2006, p. 52.

Collecting and analysing the data for this KPI can be expensive and time consuming. For this reason a full ROI calculation is usually applied to only a limited number of training programs – typically those that are expensive and that are expected to be impactful.¹⁹

6. Final comments

Key Performance Indicators are part of the reporting and control system in the organization. They are measured on the organizational, team and individual levels to monitor and assess performance of processes and employees.

The purpose of maintaining KPIs is to gain comprehensive information in order to maximize the performance of the organization. Nevertheless, the overview resulting from KPIs measurement should only be the starting point for further interpretations. KPI figures themselves are to provide opportunities for meaningful conversations in order to focus on specific areas of the business to drive process improvement.²⁰

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