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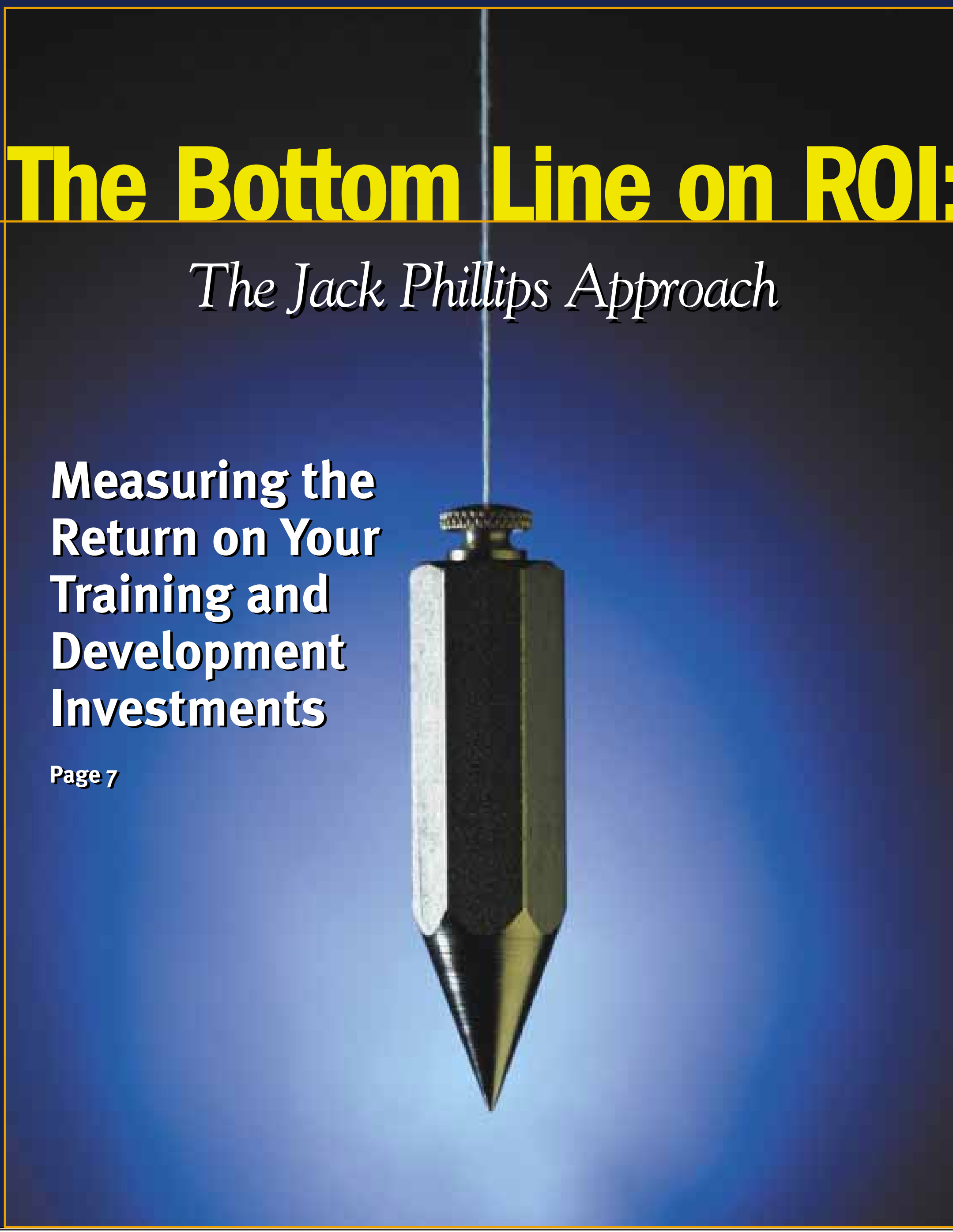

The Bottom Line on ROI:

The Jack Phillips Approach

Measuring the Return on Your Training and Development Investments

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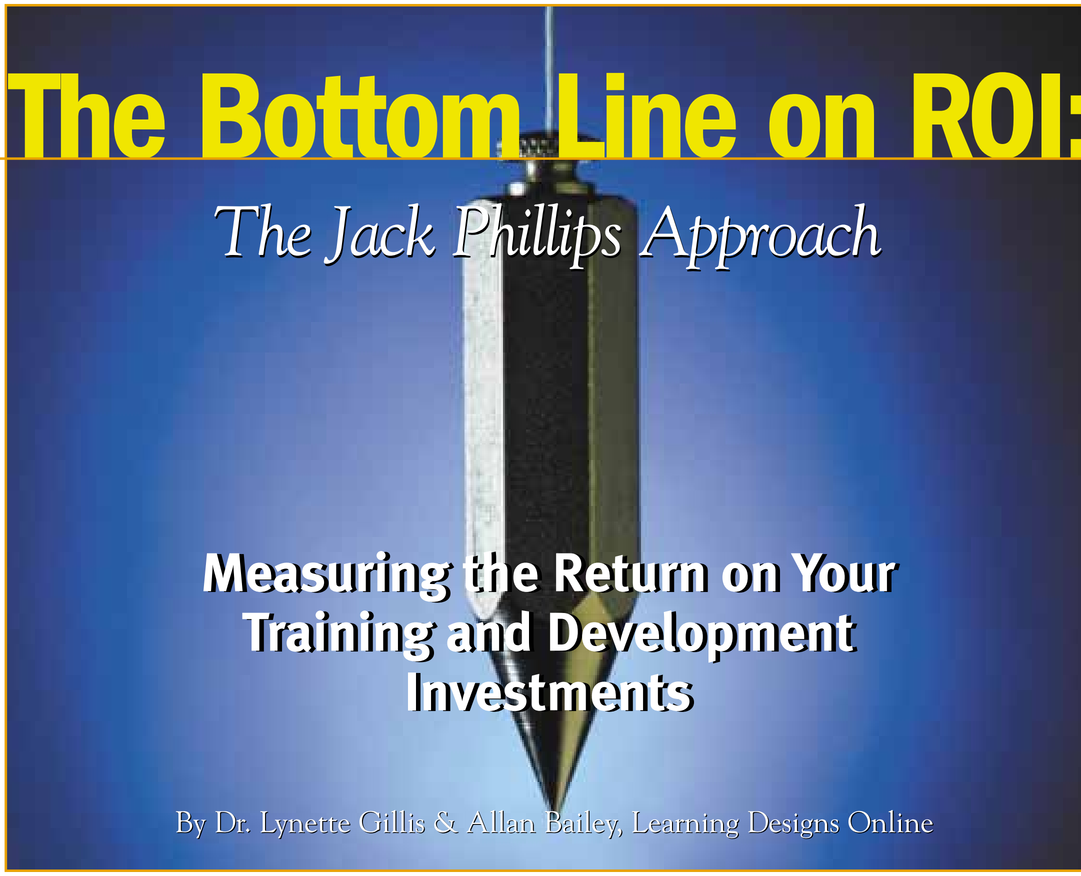

By Dr. Lynette Gillis & Allan Bailey, Learning Designs Online

"You can't manage what you can't measure."
– Peter Drucker

Fundamental changes sweeping the business world are shifting more and more focus onto the measurement and evaluation of training. Increasingly, training departments are being asked to demonstrate that training objectives are aligned with business objectives – that training improves the company's bottom line.

Training and development have long been regarded as necessary – almost inviolable – corporate activity. North American companies invest an estimated $70 billion dollars annually in training and development. ASTD studies show the average training budget is equal to about two per cent of a firm's payroll. In the past, corporations have traditionally viewed this investment as an inevitable expense – part of the cost of doing business.

In the New Economy, however, training is seen as a strategic tool – a competitive edge in times of rapid change. Business leaders get it. 'Learning organizations' now seek to leverage training to meet business objectives and improve revenues. The good news for the training department is that they now have the full attention of the boardroom. Basking in the glare of the executive spotlight, however, means training managers are thrust into the new and unfamiliar territory of accountability. The training department's new marching orders include increasing such business measures as productivity, quality, product knowledge, skills, customer satisfaction – and proving it!

The link between training and bottom line performance means more executives expect training to be run as a business. Donna Goldwasser, Senior Editor for *Training* magazine, says many executives expect the traditional "soft" training metrics to be accompanied by more direct proof of training's value to the company – business impact and financial metrics. "Many corporate training professionals, along with the decision-makers who approve their programs, would prefer to get that proof in the form of dollars and cents."

Increasingly, the training department is being asked to justify its budget in terms of return on investment (ROI). Demonstrating training effectiveness (ROI), has become one of the most challenging issues facing human resources development (HRD) professionals, says Dr. Jack Phillips, a leading authority on training and performance measurement. "The interest in ROI during the 1990s has been phenomenal," says Phillips, founder of the Jack Phillips Center for Research (A Division of Franklin Covey). A survey of 35 members of the International Federation of Training and Development Organizations consistently rated ROI as the hottest topic among those organizations.

The topic of ROI, Phillips observes, appears on every HRD conference agenda and is the subject of hundreds of articles and books aimed at executives and training professionals. Indeed, one of his own books, *Measuring Return on Investment*, published by the American Society for Training and Development, was the best selling ASTD book in 1995 and 1996, and is well on its way to becoming the ASTD's all time best-seller.

The focus on accountability has also been fueled by recent studies. An ASTD

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report, for instance, offered the first definitive evidence that increasing training investment improves profits and total shareholder return (TSR). The study ranked 2,500 corporations on how much they spent on training. The results showed that companies in the top half of the ranking had a TSR that was 86 per cent higher than those in the bottom half.

The training intensive Information Technology (IT) industry illustrates the growing pressures for accountability. Spurred by rapid innovation and product upgrading, the IT training industry has blossomed into a $20 billion a year business. Executives and shareholders, however, increasingly demand to know what they're getting for their money. CIO Magazine asserts that there is no other workplace issue on which so much is spent with as little accountability as training. Quoting California-based elearning consultant, Brandon Hall, the magazine states: "So far, training has managed to fly under the radar, but increased shareholder scrutiny combined with the growing need for training in companies means this is about to change."

Jack Phillips points out that these concerns have caught the attention of business leaders and are a key driver for this new focus on training metrics and accountability. "Top executives who watched their training budgets continue to grow without the appropriate accountability measures have become frustrated and have demanded a return on the training investment," he says. The popularity of other business trends such as Total Quality Management (TQM), re-engineering, and continuous process improvement have encouraged management to look to ROI metrics to evaluate the effectiveness of such initiatives.

Knowing something needs to be done and knowing what to do about it are two different things. Corporate leaders today face substantial barriers to developing training metrics and calculating ROI. A 1999 ASTD study observes: "Managers and their firms simply don't know how to assess whether workplace training and related programs are achieving their goals. Often they don't even have a clear idea of what those goals are..." The study, *Linking Training and Performance: Benchmarking Results* concludes, "The bottom line: budget battles will continue to be lost unless the professionals charged with administering workplace education and training programs are able to demonstrate their value according to widely accepted performance standards."

Jack Phillips, who has authored ten books on the subject, acknowledges that many barriers militate against embarking on calculating ROI. In addition to the lack of in-house evaluation skills, Phillips identifies typical issues that inhibit evaluation initiatives: fear of failure (i.e., negative ROI), and the cost and time of implementing ROI studies. In his book, *Return on Investment*, Phillips shows how these barriers can be overcome. He explains that adopting the ROI process in the right situations can yield powerful insights and provide important strategic benefits to the organization:

> **"Top executives who watched their training budgets continue to grow without the appropriate account-ability measures have become frustrated and have demanded a return on the training investment," [Phillips] says.**

- **Measuring Contribution:** HRD staff can determine if the benefits (expressed in monetary values) outweigh the costs of the training investment and if it contributes to the organization's bottom line
- **Setting Priorities:** Calculating ROI in different areas or initiatives will help management determine which provide the greatest impact
- **Focusing on Results:** The act of implementing an ROI process introduces a heightened focus on business results that has a spillover effect, benefiting all programs, even those not targeted for an ROI calculation. The effectiveness of all training programs can be improved by requiring instructional designers, facilitators, participants, and support groups to concentrate on measurable objectives.
- **Altering Management's Perceptions of Training:** When applied consistently and comprehensively, the ROI process can convince senior management that training is an investment not an expense. By demonstrating that training is making a viable contribution to management objectives, ROI can increase management's respect for the training function—an important step in building a partnership with management.

Since the 1960s, the training world has regarded the Kirkpatrick model as the 'gold standard' for measuring and evaluating training and performance. Developed in 1959 by management professor Dr. Donald Kirkpatrick of the University of Wisconsin, this evaluation approach relies on four levels of evaluation to determine the effectiveness of a training or performance intervention.
Level 1 Reaction: Did participants like it?
Level 2 Learning: Did they learn?
Level 3 Application: Did they apply the new skills or knowledge on the job?
Level 4 Results: Did the training have a measurable business impact?

Conducting evaluations becomes increasingly more involved and complex as you move to the higher levels of evaluation. Not surprisingly, studies show a majority of organizations (95%) evaluate at level one but far fewer (5 - 20%) evaluate training and performance at the fourth level.

In the last decade, Jack Phillips enhanced the venerable Kirkpatrick model to include financial metrics. Using the Phillips methodology, managers can evaluate a given HRD initiative, training or performance intervention and calculate the return on investment (ROI). ROI is a financial measure that is familiar to managers, who use it to compare the benefits of an investment – the amount saved or gained – with its cost. This measure also allows executives to compare the benefits of a training program with other investment opportunities within the organization. Another key evaluation metric is the Benefit/Cost Ratio (BCR). (See sidebar for an explanation of how ROI and BCR are calculated.)

The ROI method involves assessing the project success according to six levels of measures including data from the four Kirkpatrick levels. Phillips's approach involves careful evaluation planning followed by the collection of data on learner reaction, learning, behaviour (application to the job), business results, and return on investment. Some benefits, judged to be difficult to quantify, are reported as intangible benefits. Reaction and learning data are collected during the training while the application and business impact results are measured on a pre-determined schedule sometime after training.

In developing his ROI model, Phillips insisted that it be simple, economical and credible. He explains that HRD professionals have been wary of ROI measurement approaches because of the perceived difficulty of quantifying training and development impact. It has been assumed that ROI could not be measured without long formulas, complicated equations and complex models. Phillips believes much of the success of his ROI model results from a relatively simple and easy-to-understand ROI process. Because the Phillips approach is relatively straightforward, it answers managers' concerns about implementing an evaluation process that could involve tremendous effort and cost to carry out.

Another hallmark of the Phillips ROI approach is its focus on credibility. For instance, when collecting data, evaluators are required to use only the most credible sources and to select the most conservative alternatives for calculations, when several possibilities exist. Phillips warns that HRD practitioners, senior management and researchers will only support a process that measures up to their scrutiny and close examination. It is essential, therefore, that these results must meet the same level of accuracy and reliability as would ROI calculations derived for any other business operation. Indeed, he attributes the global success of this ROI model to its acceptance by CFOs and other senior business leaders, who welcome an impact measurement process that yields quantifiable, accurate values and consistent outcomes.

A critical step in the ROI process is isolating the effects of the training from other influences. This procedure relies on one or more techniques to separate out those non-training related factors from the ROI calculations. For example, if revenues spike after a sales training program, the gains might have been caused – at least in part – by other factors (i.e., cyclical sales patterns, a new product release, a successful marketing program). The Phillips model requires that all contributing factors be identified and analyzed to determine the exact contribution of the training to the revenue increase. It is essential to the credibility of the ROI process that only those benefits that can be directly related to training are included in the calculations.

The step-by-step procedure for calculating ROI includes data collection, isolating the effects of training, converting 'hard' data and subjective data to monetary value, tabulating all the training program costs and then calculating the ROI. Phillips recommends a conservative approach in the data collection including subjecting estimates and subjective data to a confidence testing.

Before the ROI is calculated, the business impact data (Level 4 data) are converted to monetary values – the various program costs as well as the value of its benefits. These values are then used in the calculation of the BCR and ROI of the training or performance initiative. Importantly, the Phillips model includes a strategy for collecting and reporting on intangible measures – those benefits of the program that cannot easily or reliably be

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converted to monetary values. This comprehensive measurement methodology is now being used by thousands of corporations and private- and public-sector organizations around the world.

In efforts to respond to the surge in interest in evaluation and measurement, OSTD is launching the Canadian ROI Network this spring. It will provide a forum for members with a special interest in ROI issues and an opportunity for them to enhance their knowledge and skills. Similar to the network launched by ASTD in May 2002, the new OSTD service will offer members that subscribe to the ROI Network, workshops, newsletters, tools and forums. Both OSTD and ASTD's ROI Networks are based on the measurement and evaluation model developed by Jack Phillips.

In the end, this attention on measurement and evaluation means that the old paradigm, training for training's sake, is a thing of the past. What's important today, says *Training* magazine's Donna Goldwasser, is that a business value has finally been attached to the corporate learning experience. "By attempting to measure value – by any means – we can't help but promote its existence."

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Learning Designs Online is the exclusive Canadian partner with Jack Phillips and Patti Phillips. The partnership was created to provide Canadian corporate and government organizations with enhanced access to ROI workshops and measurement and evaluation services.

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BCR expresses the total benefits as a ratio of the total costs. ROI expresses the *net* program benefits as a percentage of program costs. (Net benefits equal the total program benefits less the program costs.)

$$\text{BCR} = \frac{\text{Total Program Benefits}}{\text{Total Program Costs}}$$

$$\text{ROI} = \frac{\text{Net Program Benefits}}{\text{Program Costs}} \text{ X } 100\%$$

Note:
Net Program Benefits = Total Program Benefits – Total Program Costs

Example

The results from an actual ROI analysis conducted for a Canadian company illustrate the calculation of BCR and ROI. Because skilled machinists were in short supply, a valve manufacturing company had to develop a machine operator-training program in order to meet its growth plans. The costs for the training program totalled $131,500 while the total benefit in the first year, resulting largely from improved productivity, was calculated to be $304,950.

$$\text{BCR} = \frac{\text{Total Program Benefits}}{\text{Total Program Costs}} = \frac{\$304{,}950}{\$131{,}500} = 2.32 \text{ or, } (2.32 : 1)$$

$$\text{ROI (\%)} = \frac{\text{Net Program Benefits}}{\text{Program Costs}} \text{ X } 100\% \quad \frac{\$304{,}950 - \$131{,}500}{\$131{,}500} \text{ X } 100\% \quad \frac{\$173{,}450}{\$131{,}500} \text{ X } 100\%$$

$$\text{ROI (\%)} = 132\%$$

The Benefit/Cost Ratio shows that for every dollar invested in the training program, $2.32 in benefits were returned. The program resulted in an ROI of 132%. This means that for each $1 invested, there is a return of $1.32 in *net* benefits, after costs are covered.