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EXECUTIVE REWARDS IN THE MODERN WORLD

The executive talent global landscape is as challenging as ever:

- Globalization and industry consolidation have led to a shortage of executives with the knowledge and expertise to run leading multinational firms.
- On top of that, the aging workforce is creating serious gaps in succession plans.
- The global convergence of the talent market has resulted in increased mobility of executives across borders, creating knotty executive reward design and administration problems.
- Developments in technology and social values are changing how work gets done, requiring new leadership competencies, such as the ability to work with remote global teams or embrace democratized decision-making over hierarchical power.

Instead of companies being enterprising in addressing these challenges, pressures from regulators, shareholders, proxy advisors, and the media are making many organizations leery about deviating from the mean when it comes to executive rewards programs. To satisfy current external pressures, they are seeking the safety of the masses.

This short-term approach, however, does little to address the current landscape. It threatens to impede companies' prevailing business priorities and talent requirements and will do little to support long-term shareholder value creation and sustainability. Remuneration committees and management are best advised to employ a more business-centric executive rewards approach.

FIVE STEPS TOWARD A MORE EFFECTIVE APPROACH

Complexity calls for thoughtful deliberation and strategic business analysis, not conformity to blanket norms. Here are five action items to consider.

1. INTEGRATE EXECUTIVE TALENT PLANNING AND REWARDS DECISION-MAKING

Executive talent planning and rewards management should be intricately connected. Mercer research shows that an increasing number of companies are already combining responsibilities. For example, 17 of the 30 Dow Jones Industrial US-based companies include at least one non-rewards-related activity among the duties of the remuneration committee, and 12 engage in multiple non-rewards tasks. The most common of these activities are succession planning (12 companies) and leadership development (10 companies). Four companies include management selection, and an equal number mention broader workforce management. Regardless of structure, boards should consider how talent information (such as leadership potential) and rewards information (such as retention value of equity holdings) are best managed in an integrated manner when reviewing their annual agenda, calendar, and processes.

2. UNDERSTAND TOTAL CAREER COMPENSATION

Few remuneration committees consider realizable pay over an executive's full tenure or have a sense of historical pay, and many gloss over the value of benefits in evaluating competitiveness against peers. Many executives are delaying retirement due to scaled-back retirement programs and insufficient personal investment portfolios. The impact can be substantial, as these leaders may be less likely to drive major, time-consuming changes, and ambitious younger executives may become frustrated and leave due to the clogged promotion pipeline. Analyzing the value of all of the executive reward elements — from the past, in the present, and for the future — is essential to understanding the full impact of executive rewards programs. Heart-to-heart discussions with executives about career and retirement goals can create tangible savings and transition plans that support succession planning or profitable redeployment.

3. HARNESS THE POWER OF DATA

Leading companies are investing heavily in their people and pioneering new ways of monitoring and managing the return on these investments. Yet, according to Mercer research, compensation professionals continue to guide their decisions by relying primarily on benchmarking as opposed to including projections, simulations, and predictive modeling used by other HR functional areas. More in-depth analyses enable companies to make decisions that recognize their unique business and enable them to more easily justify decisions to stakeholders. As a first step, remuneration committees should regularly review a dashboard of human-capital metrics that provide objective, data-driven insights into organizational threats and opportunities.

4. REORIENT TO THE GLOBAL TALENT MARKET

Boards and executive teams are increasingly diverse in terms of nationalities — a trend that requires thinking differently about managing executive rewards. Decision-makers must understand global differences in tax, social welfare, and regulatory requirements in order to identify and mitigate internal equity concerns while continuing to attract and retain the required talent. More systematic and rigorous international mobility practices should be on the agenda as a strategy to address business imperatives (for example, refocusing efforts in a growth region), promote leadership development, and develop managerial talent that can work successfully across geographic and cultural boundaries.

5. EMBRACE MULTIPLE STAKEHOLDER COLLABORATION

Investors have taken a positive step in having more detailed conversations with companies earlier in the executive rewards process; however, they also should consult with a broad range of stakeholders — including management, outside advisors, HR, finance, and legal — to obtain a variety of perspectives and avoid shortsighted biases. Committees should consider whether current processes provide a wide enough range of views. Annual agendas should be paced so that information and opinions can be shared, discussed, and reflected upon before important decisions are made, and stakeholders should have multiple opportunities to provide input and identify potential problems leading up to each meeting.

ENERGY COMPANY ENERGIZES EXECUTIVE REWARDS PROGRAM THROUGH ANALYTICS

One global, US-based energy company has shed its herd mentality by successfully adhering to proxy advisory standards while building a powerful executive talent and rewards program. It has accomplished this by harnessing the power of workforce analytics to satisfy increased regional market demand for talent while trying to manage a workforce with an impending retirement bubble.

This organization found itself unexpectedly competing for talent regionally when a shale-oil boom drew top talent away from the traditional local market. In addition, its workforce was starting to retire, leaving structural weaknesses in its leadership roles, which were suddenly difficult to fill.

To assess the scope of the retirement issue, Mercer conducted several Internal Labor Market (ILM) analyses. Described simply, an ILM map summarizes important rates and flows of employees by career level in, through, and out of the organization. One ILM map analysis of talent inflows and outflows by level and retirement eligibility outlined the stark reality of losing senior talent to retirement and the significant risk for increasing gaps at those levels.

The analyses also showed how significantly the company's total rewards program was impairing the ability to hire talent in the changing market and how it was encouraging departures at senior levels. In addition, the company saw that it was not adequately quantifying the value of its total rewards, including direct cash compensation, retirement benefits, and health benefits.

As a result of these analyses, the company:

1. Redesigned its succession planning and leadership development programs to strengthen knowledge transfer and to minimize the risk that future retirements would create.
2. Evaluated the defined benefit retirement strategy and its alignment with the company's changing talent needs. One option involved replacing the retirement program with more incentives and a 401(k) approach designed to be more attractive to the younger demographic that is in such great demand. The company can now use predictive modeling to understand impacts as the population changes over time.
3. Incorporated ILM maps as part of its data dashboard to regularly monitor the effects of strategic workforce planning and rewards design.

LEARN MORE

Attend our free webcast, Executive Remuneration 2015: Global Trends, on October 28, 2014, to gain further insights from the article's authors and ask them questions. The webcast will be held twice that day to accommodate all time zones.

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