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COMPENSATION STRATEGIES FOR EMERGING PUBLIC COMPANIES

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How does an emerging public company establish a compensation and rewards strategy that satisfies its organizational needs and its obligations to shareholders while also serving to support one of its most valuable assets—its people? How does a newly public company establish a fair and equitable strategy that optimizes the execution and people-spend associated with a new public company opportunity? The answer is by positioning the company for growth and predictability, which are attributes most valued by capital markets.

For any growing company, especially one on the verge of going public, there is a fine balance between the structure of overhead and expenses (selling, general, and administrative, SG&A), which can limit the scale, speed, or agility of operations, and the demands of a frequent driver of value—the employees. Almost every public company comes out of its initial public offering wanting to be perfect in its delivery of predictable people costs. But in fact it's not easy, nor does anyone ever do it perfectly.

It is in this striving for perfection that we gain insights into cost drivers and learn and improve on pay delivery, as well as challenge operating business models to deliver the next disruptor in an industry. For most new companies, the buildup of staff in the first three to five years, along with balancing growth to align with and anticipate the market demand and operational performance of the company, is a critical deliverable for any executive team. This chapter will outline how newly public companies can best approach aligning and optimizing the people costs within a new public entity with respect to the pressures and demands associated with delivering value to shareholders.

WHAT

The first step for an emerging public company in creating an effective rewards program that serves the needs of all stakeholders—shareholders, customers, and employees—is to create a total rewards strategy. This approach encompasses nonmonetary and monetary rewards and incentives, including base-pay considerations. An effective total rewards approach seeks to align reward programs with the business across all of its regions, business units, and functions as well as all categories of employees, from C-suite executives and line managers to rank-and-file employees and contract and contingent workers.

Intangible rewards can include training and development programs that allow workers to grow and advance in their careers so that their sense of engagement, skills, and base compensation can routinely grow during their careers. A meaningful rewards program will encompass not merely calculating a bonus program but also integrating an employee-rewards perspective throughout the company, from hiring policies and pay levels to policies on transfers and promotions. Other intangible bonuses include social rewards, such as company picnics and holiday celebrations, employee discounts, or company-sponsored social clubs and activities—many of the things that reflect the “culture” of the company.

While ensuring that rewards are broadly designed to work across all functions and business units for all employees, employers must also ensure that the measurement system put in place for earning specific rewards be designed to balance several different types of performance measures; these include financial results, customer satisfaction, operation efficiency, and human capital. Such measurements can range from budget efficiency and revenue production to customer wait-time in a call center, to waste and rework ratio on the plant floor, to employee turnover in an individual business unit.

In this light, an effective rewards strategy can offset its costs by first utilizing already existing business functions, such as training and advancement practices. These strategies can also create savings by increasing efficiency in recruiting and retention of highly talented and motivated employees. Certain types of intangible rewards can also boost the company brand if some rewards, such as creative annual celebrations and employee giveaways, are highlighted in local media. Finally, research by Korn Ferry Hay Group found that implementing rewards strategies that are clearly aligned with organizational goals, strategy, and culture enabled a cross section of FORTUNE World’s Most Admired Companies to pay five percent less in base salaries for management and professional jobs versus a comparison group.

HOW

A critical element for the success of any effective total rewards program is executive support under the new public entity structure for an emerging public company. If executives and managers fail to understand the rewards programs clearly, they will likely not buy into the strategy and thus may not deliver the long-term results shareholders demand. For that reason, it’s vital to ensure that rewards programs are communicated and characterized as a shared investment, not a cost.

When the total reward structure is considered a cost, the goal will be to minimize it. But when seen as an investment, leaders seek to optimize it and leverage rewards, maximizing participation and recognition to achieve company goals that directly benefit shareholders and customers.

Those organizations where senior leaders, managers, and HR operations embrace a total rewards outlook will function quite differently from those that look only at keeping rewards costs as low as possible. When managers view rewards in this light, the incentives may be considered expensive employee entitlements and become separated from the performance goals that good rewards programs support.

One factor that strongly encourages executives to buy into the total rewards approach is that in companies with effectively aligned rewards programs, Korn Ferry Hay Group research found the FORTUNE World’s Most Admired Companies’ top executives receive above-average pay—about 10 percent more at the function-head level and above. When bonuses are taken into account, senior managers in the world’s top companies can earn 20 percent more than their peers. These people are being rewarded for their ability to deliver and ensure their company stays at the top of its sector—given then are the ones who are driving the strategy and leading their people to perform. This allows the business to attract and maintain the best key executives to deliver shareholder and customer results.

Beyond support, managers at all levels need to be actively involved in implementing and

reinforcing rewards strategies, especially being sure to engage line managers in the rollout of reward programs. The role of line managers in promoting and integrating the rewards strategy into daily operations is crucial, and it is a mistake to define rewards strategy as simply an HR function. The design of a rewards strategy isn't the biggest element in making the program succeed; in fact, there is no magic answer or universal set of best rewards practices for achieving results.

What does make the difference in effective programs is a relentless focus on excellence in execution. This means building reward platforms and fine-tuning them in practice over time rather than undertaking wholesale changes or switching to a completely new rewards strategy, which can erode employee enthusiasm for any rewards program.

WHO

To be effective in a post-IPO operation, any total rewards strategy will need to be flexible, and it is likely to need to change over time from the rewards strategy of a nonpublic company, especially a startup. In addition, an effective total rewards strategy has to be able to respond to the company's operating cycles, the larger business cycle, and the ways in which the company and its market grow and evolve over time.

In the initial surge of activity, a startup may be focused on grabbing a large portion of market share, increasing name and brand recognition, and scaling up rapidly. However, the post-IPO company culture will need to shift to that of a firm that can manage costs in a predictable fashion to give shareholders the certainty they need in a forward-looking business. This includes controlling and maximizing the people spend in a way that supports certainty and shareholder demand for profitability. It's important to remember that in establishing the newly public firm's priorities as first clients, shareholders, and then employees, it is the employees doing the actual day-to-day work who drive value to shareholders.

An effective total rewards program means a company can align those costs, needs, and incentives that produce results by nurturing and developing talent; by frequently promoting from within, companies can actually pay less for talent than other organizations do. Korn Ferry Hay Group found on average, promoting from within costs about five percent less in base pay for management and professional positions.

That's because stronger talent development programs incorporated into a total rewards framework encourage the development of internal candidates, resulting in less need to hire more expensive talent from outside the company. This integration of talent management and rewards makes it easier for the company to attract and recruit the right people, reduces turnover, and, by aligning incentives and rewards with business strategy and goals, creates a more efficient culture that creates increased return on investment.

Newly public companies will find that rewards and incentives will shift at all levels in the company to align with shareholder priorities on forward-looking certainty in the business. For example, top-level executives were once wooed with large grants of stock options in the startup culture, but public companies instead focus on regular grants more strictly tied to performance. As the company grows and looks to manage costs with contingent workers, those employees also should be tied in to the rewards structure, giving the company an opportunity to develop and recruit from that workforce as well.

WHY

The value of creating an effective total rewards strategy is that it can effectively align the tangible and intangible goals of the workforce at all levels of the company with the corporate goals of satisfying customers and shareholders. An effective strategy also helps reduce personnel costs as compared with those of competitors and can help provide the stability and certainty the new public entity will need to provide to its shareholders.

Keep in mind all the global elements of rewards—from tangible elements, such as cash compensation, to intangible rewards, such as a healthy work-life balance. In fact, noncash rewards have been found to be more compelling incentives over salaries and other factors such as benefits, which many workers view as an entitlement. In fact, the constraints on financial elements of reward programs mean a broader definition of “reward” has become more commonplace in the market over the past decade; rewards include perks such as a company gym to the inspirational value of a company’s work for employees who want to feel they are making a difference in the world. Intangible rewards are not merely soft “nice to haves,” such as the ping-pong tables at tech startups. Instead, they have become a core component of employer branding and the backbone of the employer’s “value proposition” to employees.

The value of an effectively managed total rewards program to emerging public companies is that when properly structured, these incentives aren’t simply costs to be minimized by investments that position the company for the growth and predictability shareholders demand. In a growing company, the potential for personnel overhead expenses to limit the ability of the firm to grow and respond to the volatile, ever-changing marketplace can be critical. By turning what has often been viewed as necessary overhead into a core piece of corporate strategy, rewards ranging from base salaries to on-the-job training can become an essential element that controls cost, supports strategy, produces satisfied customers and shareholders, and positions a post-IPO company for growth and success.



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Bob Wesselkamper leads efforts to continue to expand the focus of Korn Ferry's full reward and benefit offerings, including broad-based reward strategy, executive rewards, job evaluation and leveling, reward benchmarking, and pay data. He has more than 25 years of experience as a senior global human resource consultant, working with senior management and boards on all aspects of their rewards, benefits, and HR service delivery needs. His industry focus includes media, automotive, manufacturing, professional, and financial services. Bob has worked across Europe, Asia, Latin America, the Middle East, and Africa. During his career he has focused on the business needs of mature and emerging multinational companies with a deep emphasis on operational improvement, mergers and acquisitions support, new venture startup, and change management leadership. He received his undergraduate degree in economics from DePauw University.