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Retention of Key Talent and the Role of Rewards

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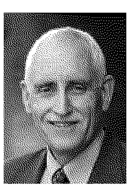
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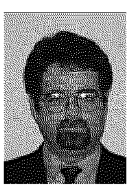
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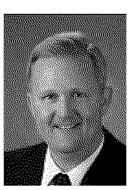
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Economic recovery in the United States has been slow, but competition for key talent has already become intense (Bureau of Labor Statistics 2012). Numerous scholars predict that talent shortages are going to increase well into the next decade, which will limit the ability of companies to expand and in fact, jeopardize their chances of survival as global competition becomes more intense (Coombs 2012; Gordon 2009; Krell 2011). These long-term shortages are the result of Baby Boomers retiring, slower population growth, increasing specialization and technical demands of jobs, the Millennials and Generation Y not getting the education or experience to advance into more responsible and demanding jobs, and increased global competition for talent (Bureau of Labor Statistics 2012).

Retention of key talent — those employees who are the strongest performers, have high potential, or are in critical jobs — is even more important during economic recoveries when organizations aggressively compete for market share and talent. Key talent disproportionally contributes to current and future organization performance since designated key talent most often become organization leaders. Estimates suggest that the cost of employee turnover often ranges from 50 percent to 200 percent of the employee's annual salary based on the type and level of job he/she holds. These costs are substantial even for medium sized organizations that have moderate rates of turnover (Allen 2008, Cascio 2010; O'Connell and Kung 2007). Losing key employees costs considerably more since their impact and contribution is greater than that of typical employees and they are more difficult to replace.

Even though unemployment is still relatively high in many parts of the world, the United States and other industrial countries are already experiencing talent shortages in a number of labor markets. The U.S. Bureau of Labor Statistics (BLS) reports an increasing trend in voluntary terminations; the rate of unemployment for people with college degrees is about half of the national unemployment rate and is decreasing (Bureau of Labor Statistics 2011). Employers report finding it difficult to fill positions such as engineers, high-skilled technical roles, managers and executives, skilled tradesmen and sales representatives (Minton-Eversole 2012). Finally, even when there are high unemployment rates, key talent is always in demand and an improving economy will exacerbate the challenge of holding the most capable employees who have unique or critical skills.

Not only is competition for key talent going to increase, Hay Group employee opinion norms indicate that 20 percent of employees plan to look for a new job in the next two years and another 20 percent plan to leave their employers within the next five years. These trends suggest discontent in the workforce, which is not surprising since employees are working harder as a result of recent downsizing, there have been limited base salary increases and incentive payouts awarded in recent years, and there has been increased pressure to perform. But the trends may also highlight that the social contract surrounding the employment relationship is changing. Because individuals and organizations have become more tenuously attached to each other, turnover has become a more prominent and accepted aspect of organizational life.

Not only has the relationship between employees and employers become more tenuous but advances in technology and social networking platforms are making it more difficult to retain talent. In today's world a company cannot hide its top talent because social media outlets such as LinkedIn openly promote capabilities and accomplishments of employees. Furthermore, top talent can compare the "deal" or pay package they currently receive with that of other organizations through websites such as salary.com, vault.com, glassdoor.com and onetonline.org.

It is clear that one of the foremost challenges for management today is how to retain its key talent. Turnover is costly and directly impacts business performance, particularly during an economic recovery. As a result, rewards professionals will be under increased pressure to make counter-offers, increase new hire offers, offer more frequent exceptions to reward policies and programs and attempt to "handcuff" key employees to the organization by offering stock options and other programs that make it difficult to leave.

Given the unique position that rewards professionals hold, they can offer insights into how organizations can retain key talent. Consequently, the authors surveyed rewards professionals to learn which strategies they are using to retain key talent and how effectively these strategies are working.

The study has been framed to answer some fundamental questions from the perspective of rewards professionals.

- Is retaining key talent a significant challenge?
- Are special efforts made to retain key employees?
- Why does key talent leave organizations?
- What is done to retain key talent and what is the effectiveness of these approaches?
- What role do counter offers have in retaining key talent?
- Does organization context determine how key talent retention efforts are managed?
- What are the best practices for retaining key talent?

DATA COLLECTION AND SAMPLE CHARACTERISTICS

Rewards professionals, primarily mid-to-senior rewards professionals (WorldatWork members or Hay Group registered website users), were invited to participate in a survey that focused on key talent retention practices. The survey, hosted by WorldatWork, was open for approximately two months from Dec. 15, 2011 through Feb. 15, 2012. A reminder to complete the survey was sent half way through the period and again just before the survey closed. The survey required approximately 15 minutes to complete and had 682 respondents.

Since rewards professionals are accountable for the design and execution of rewards programs and are often involved in assessing the cause of employee turnover, they have one of the best vantage points within the organization on how rewards programs impact retention of key talent.

Figures 1 through 3 indicate that the organizations sampled in this research comprise a wide variety of organizations. Figure 1 shows approximately 19 percent of organizations had fewer than 999 employees, 45 percent had 1,000 to 9,999 employees, 10 percent had 10,000 to 19,000 employees, 11 percent had 20,000 to 39,999 employees, and 16 percent had 40,000 or more employees. Note that because of rounding, tables and figures do not always equal 100 percent.

Figure 2 shows the diverse range of industries represented by the rewards professionals who responded to the survey. The largest representations were from manufacturing (18 percent); financial, insurance and real estate (17 percent); health care and social services (9 percent); utilities, oil and gas (14 percent); consulting, professional and technical services (8 percent); and information (6 percent). The "other" designation was assigned to the 30 percent of respondents who were from industries that made up less than 5 percent of the total.

Figure 3 indicates how different types of organizations are represented, such as public sector (local, state, federal government), 10 percent; private sector, publicly

FIGURE 1 Number of Employees

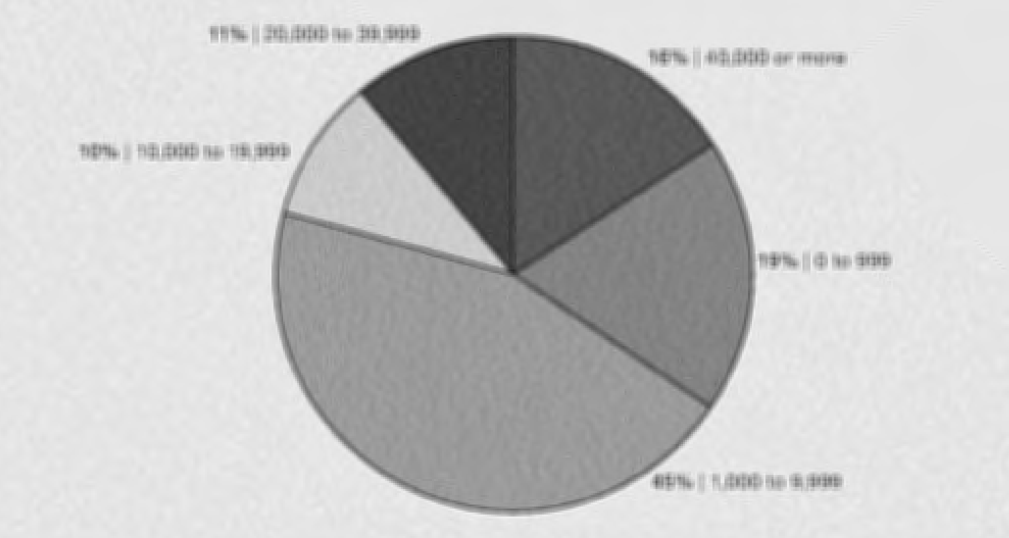
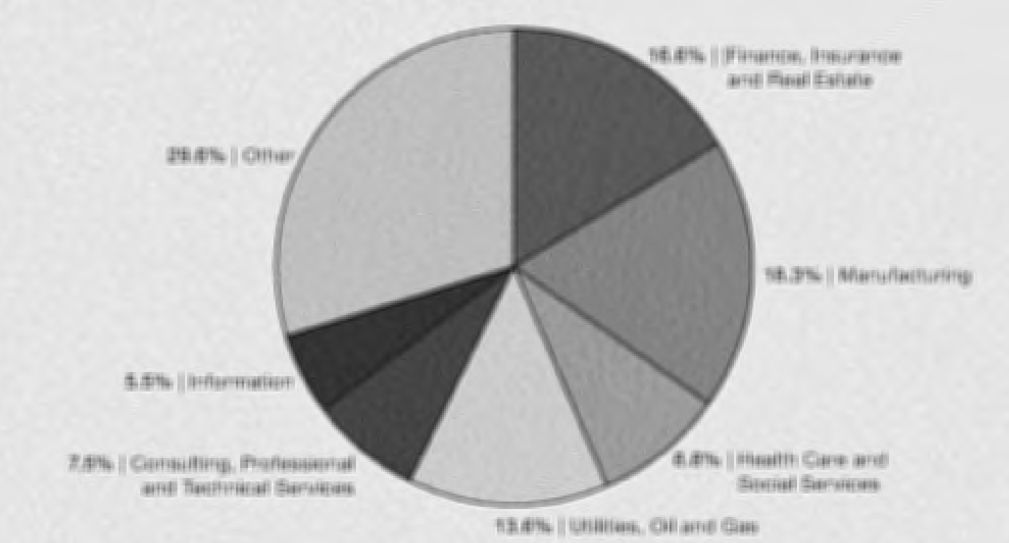


FIGURE 2 Organizations Represented: Industry Affiliation



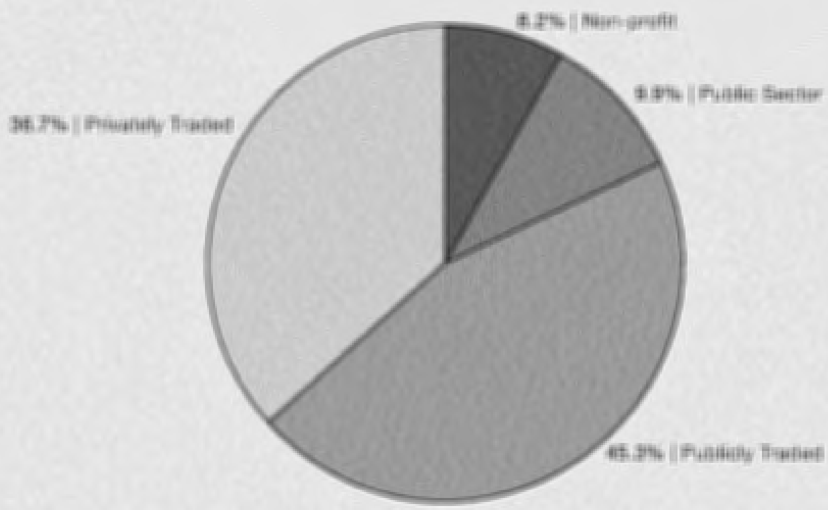
traded, 45 percent; private sector, privately held, 37 percent; and not-for-profit (education/academic organizations, charitable organizations, 8 percent.

FINDINGS AND IMPLICATIONS

Is retaining key talent a significant challenge?

The survey findings shown in Figure 4 point to the challenges organizations are facing in retaining key talent. First, 81 percent of the respondents recognize that turnover of key talent is very costly. Sixty-eight percent of rewards professionals

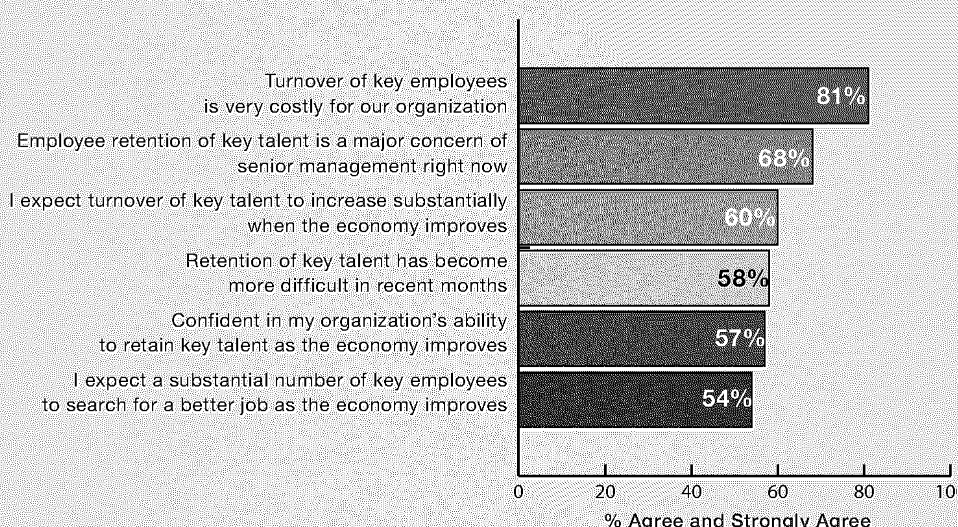
FIGURE 3 Economic Sector



said that employee retention is a major concern of senior management right now. Furthermore, most expect turnover of key talent to substantially increase when the economy improves and say that retention of key talent has become more difficult in recent months, 60 percent and 58 percent, respectively. More than half of survey respondents are not confident in their organization's ability to retain key talent as the economy improves (57 percent). In fact, 54 percent expect a substantial number of key employees to search for a better job as the economy improves.

Discussions with senior rewards and HR professionals indicate that retention of key talent is one of their top challenges, and that they worry about having the people necessary to win market share when the economy improves.

FIGURE 4 Is Retaining Key Employees a Significant Challenge?



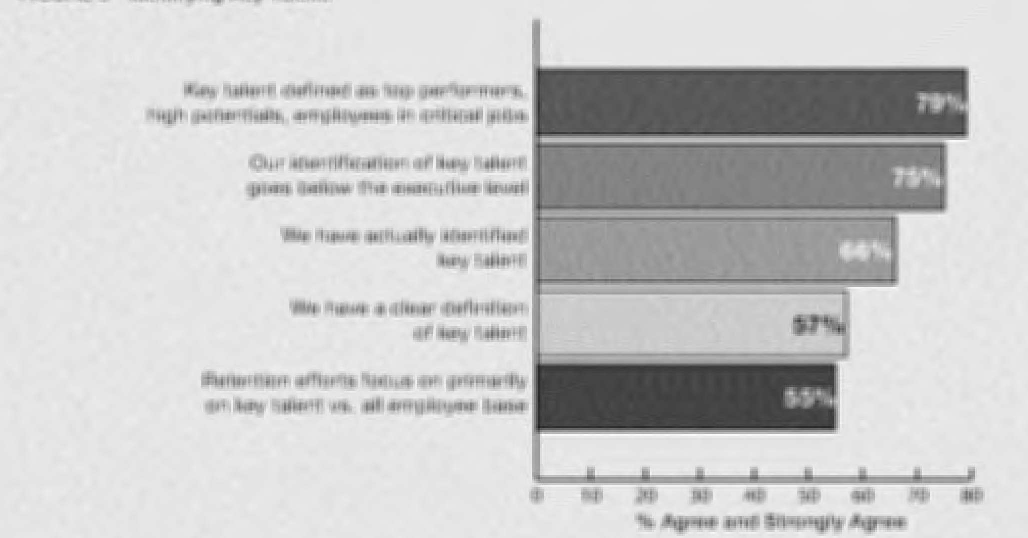
These professionals fear that key employees are becoming increasingly frustrated in their organizations due to layoffs, the resultant expansion of job accountabilities, and constraints on reward programs — primarily limited base salary increases, lower incentives and fewer advancement opportunities. These comments reinforce the message from survey respondents that retention is a dominant organizational concern during the recovery. More than 30 percent of respondents report that turnover rates of key employees is higher than 10 percent and 78 percent had turnover rates of more than 5 percent for key employees. When considering the cost of replacing these individuals, the price is staggering. So that leads us to the next question "Are special efforts made to retain key employees?"

Are special efforts made to retain key employees?

In order to make a special effort to retain key employees, the organization must first identify these individuals. According to the findings shown in Figure 5, more than half (57 percent) of the organizations have a clear definition of key talent and 66 percent of the organizations have identified those individuals. Seventy-nine percent of respondents say that they define key talent to include employees who are top performers, have high potential or are in critical jobs. From other questions in the survey (not included in Figure 5), only 9 percent of respondents say their organizations restrict their focus on key employees to top executives, the vast majority (75 percent) identify key talent below the executive level.

Bivariate correlation analyses found that rewards professionals who were more confident in their ability to retain key talent during an economic recovery were more likely to report that their organizations "have a clear definition of key talent" (r = .38, ∞ = .00), "have identified key talent" (r = .41, ∞ = .00), to "include in their definition of key talent employees who are top performers, have high potential and

FIGURE 5 Identifying Key Talent



are in critical positions" (r = .31, ∞ = .00, r = .33, ∞ = .00, r = .24, ∞ = .00, respectively), and to "focus on key employees below the executive level" (r = .28, ∞ = .00). Rewards professionals reporting that they are more confident in their ability to retain employees believe that "their organization's retention rate is above the average in their industry" (r = .23, ∞ = .00). This data indicates that a best practice is to clarify the meaning of the term "key talent," define it to include a range of employee groups, and develop retention programs targeted specifically for these groups.

Why does key talent leave organizations?

Figure 6 shows the reasons why rewards professionals believe that key employees leave their organizations. The percentages represent the respondents who agree or strongly agree for the stated reason. The primary reason given for quitting is the opportunity to earn more pay elsewhere (77 percent). The next most cited reason is "Lack of promotional opportunities" (67 percent). Feelings that pay levels are unfair relative to employees in other organizations such as external equity (58 percent) was followed closely by "dissatisfaction with job or work responsibilities (56 percent). The fifth most identified reason for quitting is "pay levels perceived as unfair vs. employee performance" (53 percent). One should note that three of the five frequently given reasons for quitting are directly tied to pay. In fact, the No. 2 item, "lack of promotional opportunities" could also be partially related to a desire for more compensation.

Lower ranked items in terms of reasons why key talent leaves shown in Figure 7 organizations include: opportunity for a better health-care package (14 percent)l better retirement/saving benefit package (16 percent). Likewise, even during a significant downturn in the economy, rewards professionals indicate that job security for

FIGURE 6 Most Likely Reasons Why Key Talent Quits.

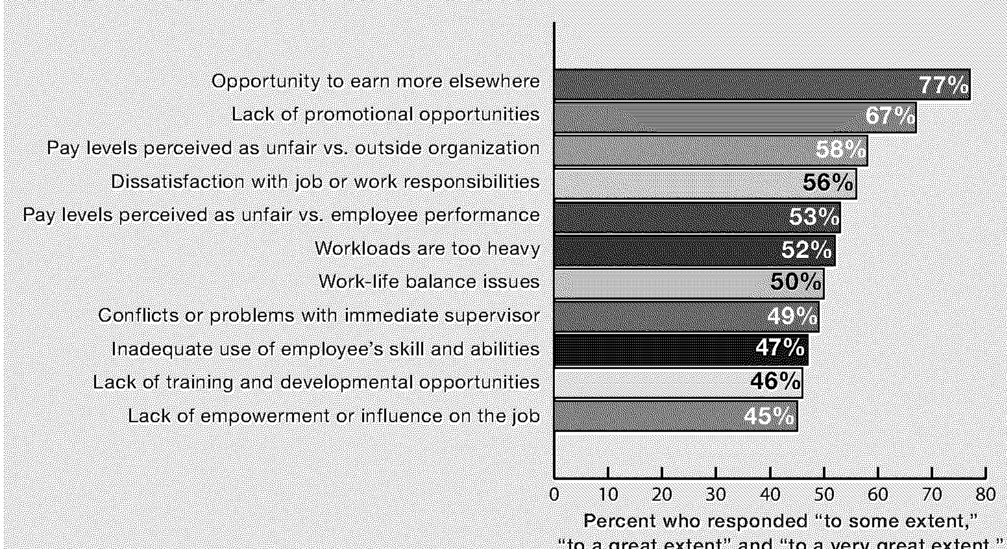
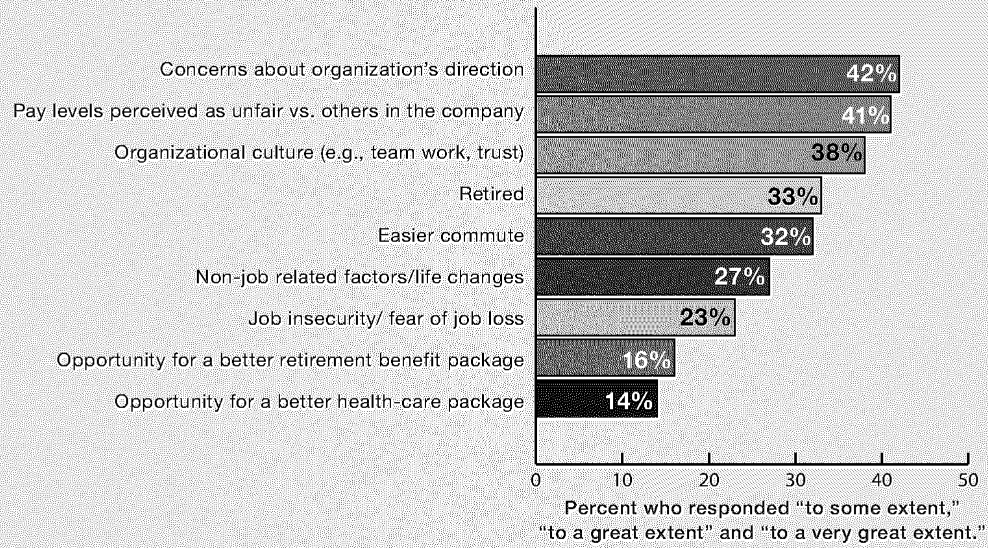


FIGURE 7 Least Likely Reasons Why Key Talent Quits.



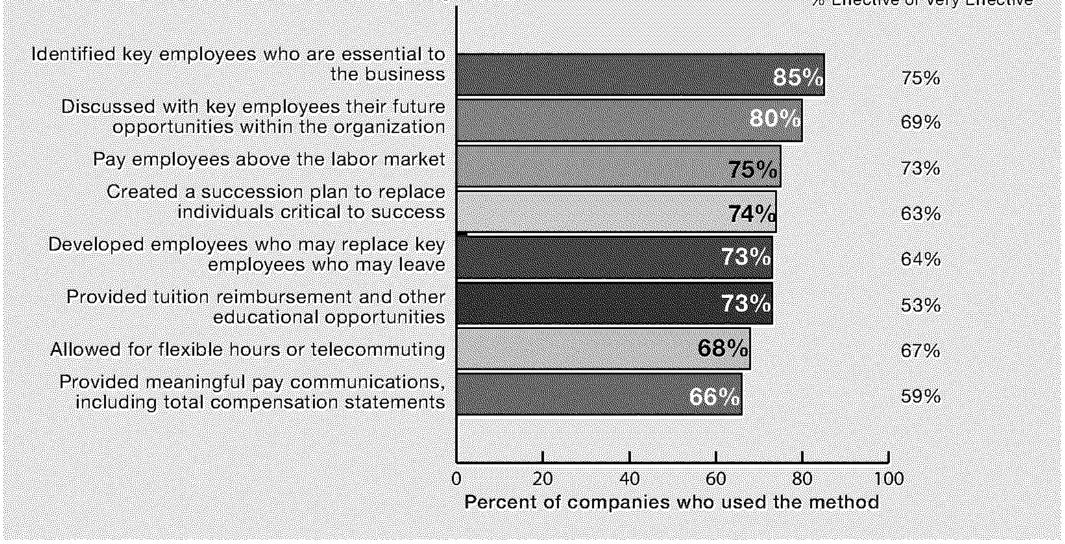
key talent remains high. Twenty-three percent of respondents think that fear of job loss and job insecurity is either not an issue or only to a minor extent in turnover decisions. Both "easier commute" and "non-job related factors" also score low as reasons why a key employee might quit (32 percent and 27 percent, respectively).

Knowing which factors may lead key employees to quit and which don't provide important insights for crafting methods for retaining them.

What is done to retain key talent and what is the effectiveness of these approaches?

Figures 8 and 9 focus on the types of programs organizations used to retain key talent and the perceived effectiveness of these efforts. Consistent with responses to other questions, key talent identification is a core attribute in terms of programs that are deemed as effective in retention of key employees (85 percent). Seventy-five percent of rewards professionals who responded to the survey indicate that this strategy is either "effective" or "most effective." The other methods reported most often used to retain key employees include, "discussed with key employees their future opportunities within the organization" (80 percent), "paid key employees above the labor market" (75 percent), "created a succession plan to replace individuals critical to success" (74 percent), "develop employees who may replace key employees who may leave" (73 percent), and "provided tuition reimbursement and other educational opportunities" (73 percent). Although "allowed for flexible hours or telecommuting" is down toward the bottom in terms of percent used (68 percent), it is toward the top of list in terms of evaluated effectiveness (67 percent). All of these programs were perceived to be "effective or "very effective" in a majority of cases (more than half the time).

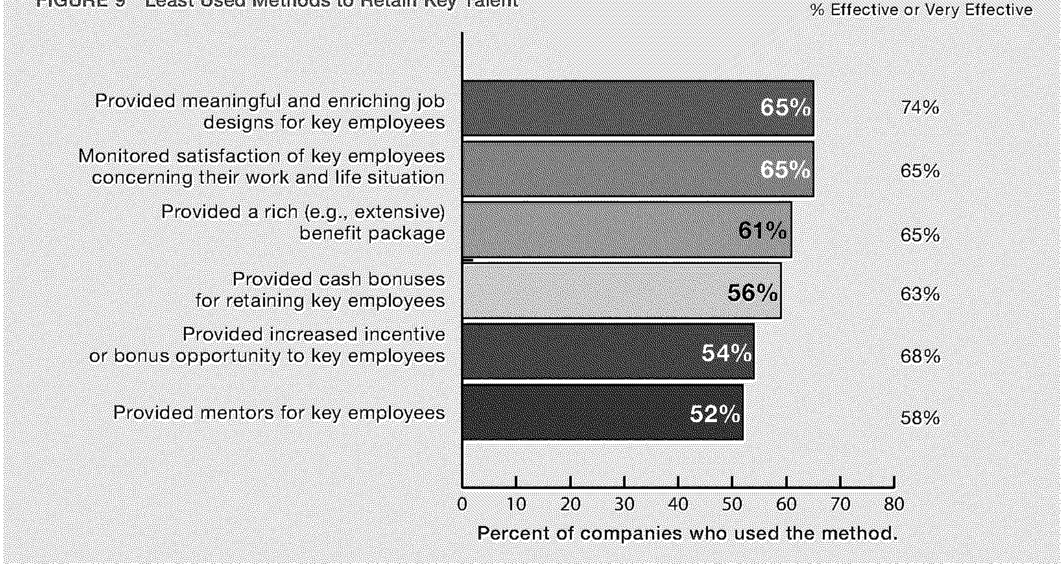
FIGURE 8 Most Used Methods to Retain Key Talent



As shown in Figure 9 lesser utilized methods for key talent retention noted by respondents include: "provided mentors for key employees" (52 percent), "provided increased incentive or bonus opportunity to key employees" (54 percent), and "provided key employees with stock options or equity awards" (56 percent).

The methods deemed to be the least effective in retaining key talent are "provided tuition reimbursement and other educational opportunities" (53 percent), "providing mentors for key employees" (58 percent), and "provided meaningful pay communications, including total compensation statements" (59 percent). One can note that the most frequently used methods are not necessarily the methods considered the most effective.

FIGURE 9 Least Used Methods to Retain Key Talent



To determine if there were methods for retaining key talent that were overlooked, rewards professionals were asked to respond to an open-ended question: "In terms of retention of key talent, what is your organization doing that works particularly well?" The authors found that cash compensation was most often identified as being the best method for retaining key employees.

Rewards professionals definitely have opinions as to the effectiveness of different methods for retention of key talent, but do they formally evaluate the effectiveness of these methods? The answer is mixed: 21 percent say they do not evaluate their key talent retention programs, and 31 percent say they rely on only informal feedback from employees and managers. However, 26 percent examine formal attitude surveys, 31 percent examine turnover data, and 7 percent conduct a return-on-investment (ROI) analysis on the subject.

What role do counter-offers play in retaining key employees? Consistent with the authors' earlier counter-offer study (Scott, McMullen, and Nolan 2005), few organizations have a formal policy on counter-offers. Eighty-three percent said, "We do not have a counter-offer policy; each situation is decided on a case-by-case basis." Fourteen percent said they have "an informal policy (or practice) that provides general guidance." Only 4 percent said they have a formal written policy. For those organizations that have either a formal or informal policy, the survey found that counter-offers are typically provided "only for key employees" (10 percent) or "at the request of the employee's supervisor or manager" (34 percent). Rewards professionals said that extending a counter-offer either "seldom creates a problem" or "has created some problems (33 percent and 25 percent, respectively). The majority of respondents indicated that the HR/compensation function and management are either jointly involved in extending counter offers (57 percent) or the "HR/compensation function may provide some input, but management primarily determines who receives a counter-offer and the nature of that counter-offer" (26 percent).

Does organization context determine how key talent retention efforts are managed?

One question that is commonly asked is how context influences the degree to which key talent retention is considered a problem or what methods are more effective in retaining key employees. In this study, the authors found that organization size, industry and sector have little impact on the reasons why high talent employees quit or the methods used to retain them. The only systematic impact is found across economic sectors. The private sector respondents (i.e., both privately held and publically traded organizations) are more likely to identify and provide a definition of key talent than respondents in the public sector or non-profit sector. The public sector respondents also are less confident that they can retain key employees during an economic recovery than respondents from other sectors.

CONCLUSIONS AND RECOMMENDATIONS

Several conclusions can be drawn from this study. First, rewards professionals are concerned about their organizations' ability to retain key employees. More than 50 percent believe that key talent retention will be challenging in the future. Second, there is considerable variation in how organizations define key talent and how far down into the organization they actively manage this group. However, the authors found that organizations that identify, define and manage key talent deeper into the organization are more confident that they will be able to retain these individuals. Additionally, key talent leaves organizations for a variety of reasons, with perceived inadequate rewards being one of them. Finally, based on the authors' experience, most organizations use many different methods for retaining key talent but the effectiveness of these methods substantially varies.

According to rewards professionals, the following recommendations should enhance an organization's ability to retain key talent. First, and foremost, management must develop clarity around what defines "key employees" or "top talent." If this definition includes "high potential," management must answer the question: potential for what? Specific criteria to distinguish "top talent" from other employees must be carefully developed and then applied consistently throughout the organization to ensure that correct individuals have been identified.

Once top talent has been identified, important questions must be answered as to how this group of employees will be managed and developed. Should the organization communicate their key talent status to them? How should it address concerns of employees who are not on the "top talent" list? How and under what circumstances are employees removed from the "top talent" list? What extra resources are going to be invested in top talent? Who is responsible for managing or at least overseeing the pool of "top talent," e.g., corporate, business unit or functional leadership? What role do HR professionals play in managing "key talent?"

To retain key talent the rewards system must be perceived as relevant, differentiated and fair. Furthermore, management should consider paying differential pay treatments across most rewards elements to lessen the chances that competitors can lure them away. Careful monitoring of the external labor market for key talent is advisable but also one must make sure that employees identified as top talent understand why they are paid what they are. A rewards system designed to differentiate key talent from other employees is important to enhance perceptions that the pay system is fair.

Key employees are also concerned about their opportunities for development and advancement. Management should have development and succession planning processes in place for each key employee. Furthermore, key employees should be kept apprised of their development and advancement opportunities. Although it may be tempting to leave a key employee in a position, such action could create retention problems when his/her advancement is perceived as slow.

Study results indicate that management should monitor voluntary turnover among key employees; make sure that the company understands why key employees leave so that more effective strategies for retaining key employees can be developed. Furthermore, management should develop counter-offer policies, which identifies employees to whom counter-offers will be made, what role management and human resources will play in making those offers, how counter-offers will be formulated, and how counter offers will be structured and communicated. Since a company has a very short time period from the time it is informed that a key employee is leaving to the key employee's departure, having a streamlined well-thought-out process for making counter offers is essential.

To improve the company's ability to attract and retain key talent, the authors have found that systematically evaluating these efforts is important. Effective measures include the ability to replace employees holding critical jobs, the velocity of key talent through the pipeline, success in developing key talent, and ultimately the ability to attract and retain key talent.

According to rewards professionals, retaining key talent is challenging and numerous factors indicate that key talent is going to become even scarcer in the future. To survive in a competitive global economy, management must develop strategies for attracting key talent, developing talent and retaining talent. This requires a carefully developed HR strategy and coordinate efforts of senior management, HR and rewards professionals to effectively manage this challenge. ∎

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