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PRACTICAL MATTERS

10 Myths of Executive Compensation

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Letting go of misconceptions about this function will enable boards to build stronger programs.

Hiring and retaining the right hospital leaders and ensuring that they achieve the organization's goals are among the board's most important functions, and executive compensation plays a major role in the success of those efforts. However, preconceived notions about executive compensation may hurt hiring and retention efforts. By taking a closer look at 10 long-standing myths, trustees can ensure that their program is competitive and supports the organization's mission and vision.

1. The board and CEO cannot be supportive partners in designing compensation plans. While the board's independence is of utmost importance, "independent" does not have to mean "adversarial." The best executive compensation plans result from a design partnership, with management serving as the primary architect and trustees providing critical review and oversight. The ideal program should support the mission of the organization to improve the health of the communities it serves, address stakeholders' concerns and respond to competitive market demands.

2. More pay results in better performance. It can be tempting to throw money at a performance challenge with the hope of improving outcomes. However, unless there is clear alignment with performance metrics, additional pay by itself will not necessarily produce desired results. A supportive environment with the right organizational structures, clearly articulated success measures and a well-crafted strategy all are essential for enhanced performance. Further, compensation isn't always delivered just for performance — sometimes paying for retention of key talent can be just as important. But it is as essential to know why you are paying as what you are paying.

3. We cannot afford to hire or recruit that executive. Many health care organizations believe they will not be able to afford top talent, and nonprofit organizations often feel constrained by the inability to match a current salary or offer long-term equity awards to candidates. Don't disregard a candidate solely based on his or her current earning potential. Financial rewards are important, but so is the opportunity to contribute to a meaningful mission alongside a group of committed and capable peers. Some executives will trade financial rewards for the chance to join an industry that they find challenging and engaging or one that offers more long-term career potential. Early and candid conversations with a candidate will help to identify his or her personal value drivers.

4. We should constantly adjust our compensation plans. It can be tempting to chase market trends and offer the latest in compensation design. However, the best plans often withstand the test of time. The changing health care landscape makes it especially important to stick with a program that achieves your talent-management goals and supports your organization's mission. A consistent program can provide the stability that your executive team requires.

Best practices are: first, periodically review the core purpose and philosophy of the plan to determine whether it supports your goals; and, second, check for alignment between the plan and the organization's strategy. If there is a disconnect, then it might be time to consider modifying your plan design.

5. Our compensation plan should look like that of our peers. In many ways, it is important not to be an outlier in compensation because of the potential for scrutiny from regulators. But compensation plans should reflect the organization's distinctive culture, strategy and goals. Those three factors always should add up to

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a unique plan for every organization. Remember that what works for one company may not work for another. It is important to incorporate your organization's unique attributes into your compensation plans.

6. Disclosing executive compensation always will backfire. Hospitals and systems are very sensitive to public criticism about the rising costs of care and the role that executive salaries play in the cost structure. But disclosure is an opportunity to tell a compelling story about your organization's contribution and the role that experienced, capable leaders play in the delivery of those services. In the for-profit sector, the compensation discussion and analysis (a required part of an annual proxy statement) is a great opportunity for companies to explain how the levels of executive compensation directly link to the organization's achievements. Its counterpart in the nonprofit world, the more rigorous Form 990, offers the same opportunity.

7. There is nobody like us, so comparisons don't work. No two organizations are identical. However, just because there isn't an exact likeness doesn't mean there isn't a comparable entity. Whether a company can be considered comparable for compensation purposes depends on such factors as size, industry, life cycle, capital structure, sources of executive talent and organizations that recruit your team members. Many systems today are drawing talent from finance, aviation and telecommunications. These industries also are regulated heavily, have experienced major business model disruptions, face serious cost pressures, employ technology to deliver individualized customer service and are responsive to market changes.

8. It is too difficult to set reliable, measurable long-term goals. While every organization is at a different place in its life cycle and faces different industry pressures, there are many useful approaches for setting long-term incentive goals. Many times, it is not the measurement process that proves so challenging but, rather, deciding what matters most. For example, one organization decided that proper hand-washing would have the greatest impact on their clinical outcomes throughout the organization, and 100 percent compliance with hand-washing protocols became a long-term incentive plan goal. The drop in infection rates was dramatic. An organization that finds the right balance of quantitative and qualitative metrics will indicate clearly what activities and actions are crucial to its future success.

9. Employment agreements are restrictive and will tie our hands. Not everyone in an organization requires a written agreement. However, for some of the most senior executives, an agreement can build trust. This may be especially important for executives hired from industries outside of health care who are accustomed to employment contracts. With the risks inherent in health care today, such an agreement can help to persuade an executive to make the leap. Expectations can be communicated openly, and both the board and the executive can have a clear sense of what will happen under a broad range of circumstances.

10. Compensation is the only reward that matters. Executives increasingly report that their performance is driven by the opportunity to make a meaningful difference in the lives of the people their organizations serve, and to contribute to the good of their communities. Data on engagement suggest that if pay is great but every other factor suffers, an organization is at substantial risk of losing its leader. Culture, lifestyle, mission, interactions with team members and recognition all bear heavily on an individual's feelings about his or her employment. We began this article by noting that it's tempting to throw money at a situation to make it better. In the end, it's the nonmonetary intangibles that deliver the greatest value and the best rewards.

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