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How to retain talent during a transformation

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Introduction

Losing talent is expensive.

In a typical year, 27 out of every 100 employees quit their jobs voluntarily, with over one-third leaving in the first year[1]. This number is even higher during transformations. The direct and indirect costs associated with this voluntary turnover add up to place a significant burden on a company's profitability and growth aspirations (see table belowand consider using as a template for your own cost estimates). Add in the disruption to the business and damage to culture, and a proactive retention strategy should be a high priority for the C-suite.

Table 1. Cost of Voluntary Turnover[2,3]

Direct Costs to Replace an Employee		
A.	Average cost per hire	$3,976
B.	Average first-year orientation and trainings costs per hire	$3,000
C.	**Total Direct Costs**	**$6,976** (A+B)
Interim Reduction in Labor Costs		
D.	Average annual labor costs (including base salary, bonuses, benefits, taxes, and other perks/incentives)	-$130,000
E.	Average time to hire	52 days
F.	**Total Interim Reduction in Labor Costs**	**-$18,200** (D * E / 365)
Lost Productivity Costs		
G.	Average time to hire	52 days
H.	Average time to reach productivity of lost employee	60 days
I.	Average annual revenue per employee	$390,000
J.	**Total Lost Productivity Costs**	**$120,900** (G + H)/365 * I
K.	**Grand Total**	**$109,676** (C + F + J)

The uncertainty that is often triggered by a transformation – whether it's the future direction of the organization, erosion of culture, job security, leadership changes, lack of communication, increased workload, etc. – only serves to enhance the risk of voluntary attrition. This risk becomes more acute when considering the critical workforce and who is needed to drive the transformation.

Developing a clear retention strategy at the outset should be a core component of all transformation project plans. The most successful companies understand the need to balance the financial, non-financial, and communication aspects of retention, while those that overlook even one of these can face significant challenges.

[1] Work Institute 2020 Retention Report

[2] Glassdoor *Employee Engagement Playbook*

[3] Research and Sensing by Deloitte *Calculating the True Cost of Voluntary Turnover: The Surprising ROI of Retention*

What all retention strategies have in common is:

1. The need to carefully identify the right people (or groups of people) to retain
2. A clear non-financial strategy that includes workforce priorities such as career development and work environment
3. A framework for financial awards, and an overall budget to guide decision making
4. A strong, customized communications plan to mitigate uncertainty and promote transparency

Who to include: Identifying key talent for retention

Developing a framework to identify your at-risk, critical talent should consist of reviewing a number of different data points: historical information, predictive analytics, network analysis, job supply & demand. The goal is to provide governance and structure to the process to support consistency across the organization.

A simple review of your historic attrition trends to identify at-risk groups of employees is a good place to start. Secondly, the use of *predictive analytics* can allow companies to zero in on historic attrition trends for key groups and use data to project who might be most at risk.

Network analysis provides valuable insights into how work gets done in an organization – who are the influencers and decision-makers? Where do bottle-necks occur? Where do critical knowledge centers exist?

Finally, an analysis of *critical job demand and supply* can provide perspectives on the market for a given job and be a useful guide to prioritization. This allows companies to understand what jobs and / or skills are in high demand in the market and may be more difficult to replace, helping with workforce prioritization efforts.

Traditional approaches can be used to supplement these data-driven analytics, and typically focus on a subjective assessment of leading “criticality indicators”. For example, does the individual have key management responsibilities, including being a strategic influencer and culture carrier? Does the individual have skills that are critical to the operation of the business that are in high demand in the market? Does the individual have unique institutional knowledge that is not readily available internally or externally?

These indicators and questions can and should be tailored to the unique needs of the business, and while a degree of subjectivity is inevitable, the use of a consistent approach and framework provides some much needed rigor to the process.

Examples of criticality indicators may include:

- Unique skills / marketability
- Leadership position
- Institutional knowledge
- Relationship owner
- Performance
- Location
- Current project roles

Case Study 1

A global organization struggled to retain employees beyond a certain leadership level in the organization. They promoted who they believed were the 'right' people, but once they took on the new role, they routinely did not meet expectations and would leave shortly thereafter.

Using network analysis, they were able to identify the top collaborators, influencers, and knowledge brokers across the organization. The data clearly showed that while they frequently promoted the top collaborators in the business, they consistently failed to backfill the open role with individuals possessing a similar skillset. The result was a breakdown in collaboration, underperformance in the backfilled role, and eventual burnout of the promoted individual, resulting in costly and disruptive attrition.

This data now allows leaders to identify employees with those critical collaboration skills early in their careers, and more pro-actively manage the risk of unwanted attrition.

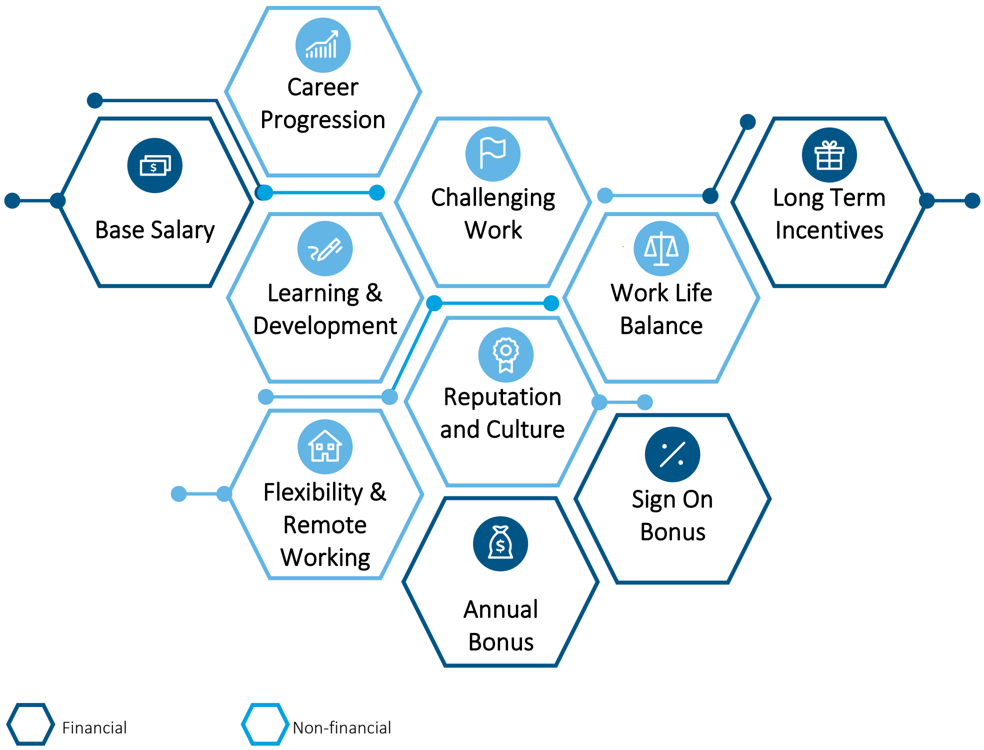
How to retain: Non-financial retention

In times of transformation, the need to move quickly to secure critical talent often means that financial retention becomes a priority. It is the quickest lever to pull and is known to be highly effective in promoting short- and medium-term retention. While financial retention may buy you time, it is not a long-term strategy. Often overlooked are the frequently more affordable and more effective non-financial levers.

Career development, work-life balance, compensation & benefits, and culture make up almost half of the reasons people leave their jobs[4]. All attrition under these categories could be considered preventable – in other words, companies are in control and can take steps to reduce attrition. The most successful transformations recognize this and use data-driven analytics to understand the preferences of the workforce *before* they quit. Developing non-financial programs to address these preferences is a core component of a contemporary retention strategy.

[4] Work Institute 2020 Retention Report

Employee Value Proposition



Non-financial retention approaches can be categorized in two buckets - *programmatic* and *non-programmatic*.

Programmatic non-financial retention efforts are generally longer-term in nature, and typically require more structural and cultural change. Examples include reviewing your organization design and job architecture to ensure both are aligned to the demands of your workforce, particularly when it comes to career progression, learning, and agility – all areas that top talent is known to value extremely highly. The implementation of 'talent marketplaces' to promote internal mobility and provide more opportunities within the organization (rather than looking elsewhere) is another effective programmatic change that promotes retention. It is often a highly valuable and insightful process to conduct a broader review of the workforce experience, including employee engagement and total reward programs. Asking employees how they feel and what they value may sound simple, but insights you gather from this effort can be eye-opening, and can be as simple as familiarity with daily rituals and routines, informal relationships and networks, processes and systems, and attachment to symbols and branding that represent the organization. All these seemingly simple cultural considerations (and many more!) are what shape long-term engagement, which in turn bolsters retention.

Case Study 2

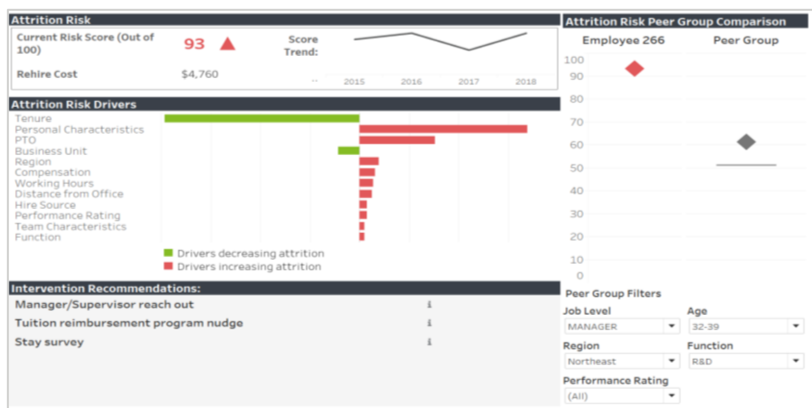
The familiar stresses and uncertainty related to a business restructure resulted in a sizeable list of management being added to a retention list. This list grew so large that it started eroding the value of the transformation.

An effort to engage employees to understand the underlying cause of the uncertainty unveiled some important findings. Most notably, employees felt they were already fairly compensated. The source of the uncertainty was rooted in culture – working long hours with few breaks, and little to no emphasis on talent management and career conversations.

Armed with this information, this company re-focused their retention strategy on non-financial priorities, including new cultural norms around working hours, which bolstered employee spirits and slowed the spike in attrition.

In the shorter-term, **non-programmatic** efforts can also be very effective. Predictive analytics allows companies to identify 'signaling data' in a more pro-active and timely manner than ever before. Understanding the key signals of attrition at your organization, and delivering smaller, more targeted responses is often a more practical solution that can be quickly deployed during a transformation. When you have identified the attrition indicators, developing a menu of responses available to deploy based on individual demographics and likely preferences is a good next step – these may range from providing a clear vision of career trajectory and progression as a result of the transformation, to specific learning programs, new project opportunities, or even non-monetary benefits such as flexible work arrangements, home-office support, or additional childcare options.

Attrition Signaling Dashboard



How much to spend: Building a budget for financial retention

If you are going to leverage financial retention awards, it is leading practice to build a budget upfront to guide your decision making. A retention 'pool' is often built-in to the cost of a transaction and is viewed as a 'cost of doing business'. For other types of transformation, building a budget for financial retention typically involves both a Top - Down, and a Bottom - Up assessment. The former relies on market benchmarks to establish a ball-park range based on the size of the transformation. This has the benefit of being rooted in data for similar projects and is generally readily available and quick to establish. Bottom - Up takes a more targeted view, and requires some assumptions related to both who is eligible for retention, and how much is needed to retain them. Building guidelines based on level - using 'anchors' such as existing bonus and long-term incentive targets, or in certain circumstances, severance amounts – is a good starting point

The amount needed to retain in the short-term typically depends on three factors, (i) existing hook (this 'hook' may be financial i.e., unvested equity, or non-financial i.e., cultural attachment), (ii) length of retention period, and (iii) level. A modest existing 'hook', a longer retention period, and a more senior level typically translates to a higher required retention amount.

If the retention period (time from establishing the retention agreement through the final date the employee is needed), is 18 months or longer, it is common split the vesting in to two installments e.g., 40% end of year one, 60% end of year two. This 'back loaded' vesting strategy provides a strong hook at the end of the period but keeps some short- / medium-term motivation due to the interim payout.

Case Study 3

A C-suite executive at a Target had an employment agreement with a 'Good Reason' Change in Control termination provision. The retention of this individual was considered critical to the success of the deal, but this transaction provided an unintended incentive for the executive to resign, claim 'Good Reason', and collect 1.5x base salary and target bonus severance (under the terms of her agreement). In this case, Buyer took this unintended incentive off the table by providing a one-time cash-based retention incentive equal to 1.5x base salary and bonus, as well as an attractive go-forward long-term compensation package

How to retain: Financial retention

Financial retention awards can be a very powerful tool during fast paced transformations and are the primary lever most companies pull to support short-term retention efforts. There are various approaches to consider based on unique circumstances of the transformation. Below is a summary of the most common, including when they are typically used, and some of the key benefits.

	One-time	Re-vest[5]	Earn-out[6]
Common use Case	Used in all types of transformations	Transactions where the talent being purchased has unique knowledge that needs to be retained	Transactions where there is a difference in opinion on valuation and / or future performance expectations between Buyer and Target
Mechanism	A one-time financial award is provided to individual employees, with vesting typically time-based	Target management agrees with Buyer that a portion of the purchase price is paid at a later date, typically to founders and senior leadership. Vesting is time-based	A future payment is made based on achievement of agreed upon performance milestones
Benefits	Simple to design and implement. Incentivizes individuals to stay through critical transformation milestones	Provides immediate alignment of interests between Target and Buyer leadership	Motivates participants to achieve key milestones built-in to the transaction rationale
Timing / Vesting	Typically pays out 100% at the end of the retention period, or in multiple tranches throughout the retention period	Time-based at an agreed upon date post-close. Graded or cliff vesting may be used	Paid out following achievement of agreed upon milestones
Additional considerations	Cash most common for short-term retention periods (<18 months). Equity used for longer-term needs, if available	Increasingly common in transactions where primary deal rationale is acquisition of talent and / or technology	If structured correctly, earn-outs may be able to benefit from Capital Gain tax treatment, which can provide an additional incentive for participants

Individual income and social security tax implications should be vetted when exploring each of these financial retention vehicles. It is also important not to overlook the implications for global participants, where country-specific considerations need to be carefully researched; tax-efficient structures may save the employer and employee significant amounts.

Failure to manage tax considerations properly can materially impact plan participants (and, possibly, their employers), including:

- Changes in the character of income can not only impact the timing of taxation, but can drastically reduce net take-home income, since compensation is generally taxed less favorably than capital income (if a difference in tax treatment exists)
- Creating employment tax compliance obligations for the employer, where one may not exist if the plan participant's income is characterized as investment income.

[5] How Revesting Has Changed M&A in Silicon Valley and Beyond, 2018

[6] Earn-outs with continued employment, 2019

Communication: customize and target

The use of financial and non-financial retention strategies will always be most effective when supplemented by a frequent and transparent communication strategy. Employees experience varying levels of uncertainty at different stages of a transformation. Shaping their perception through targeted communications is key to minimize uncertainty and anxiety. Furthermore not only do you need a strategy to communicate your financial and non-financial retention efforts, but you need to consider how the broader transformation itself is being communicated and supporting the employee experience.

More and more, these strategies are evolving from the traditional organization-wide communication approach, into customized, employee-centric communication strategies. This means recognizing that different groups of employees absorb important information in different ways, and that to expect everyone to read the email or attend the townhall just won't be effective. For example, a group of critical IT specialists may digest information through email communications and leadership podcasts, whereas critical workers in warehouse operations may not have access to email and may absorb information best when communicated by their line manager in their morning team meetings. Taking the time to understand who your key groups of employees are, how they process information, and tailoring your strategy accordingly has been shown to significantly improve employee engagement and provide an important yet underused lever in promoting retention efforts.

Closing

Talent retention during a transformation is most effective when the strategy includes financial, non-financial, and communication considerations. The cost of turnover is simply too high to not think proactively about your talent retention strategy.

Data analytics is allowing companies to more quickly and objectively identify critical talent and to quantify risk factors that influence attrition rates. While a balance of financial and non-financial allows the flexibility to tailor your approach according to the wants and needs of your workforce. It is likely financial awards will remain the predominant way of promoting short-term retention during times of uncertainty. However, using the time financial retention 'buys' to design and implement more customized approaches that prioritize career development, culture, and well-being is increasingly common as companies look to move from short-term, reactive retention strategies to long-term, pro-active approaches.

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