Council Perspectives™
Insights from The Conference Board Councils on Compensation and Benefits

Compensation & Benefits: A Global View

by Diane Palframan, The Conference Board

High performers worldwide have much in common. They have increased expectations for pay and benefits; they demand meaningful career development and learning opportunities; and they want access to their leaders. What are the best strategies for recruiting and retaining this high-performing talent when it's a sellers' market?

Globalization and its Impact on Human Resource Management

Companies in both Europe and the United States see clear advantages in being early entrants to emerging or high-growth markets. But local talent is often limited, and younger and less experienced than required, making leadership positions the most difficult to fill. It can also be difficult to fill these positions with expatriates because some of the new market opportunities are in what are considered to be hardship locations.

Obtaining compensation and benefits data in new markets is another challenge for companies making it difficult to decide on the best compensation and benefits approach to attract and retain key talent. In addition, a growing portion of the workforce is becoming more mobile, either globally or within the same geography, which can be particularly problematic in retaining a qualified workforce in markets where local talent is scarce.

(Editors' Note: The first joint meeting of The Conference Board's U.S. managed International Compensation and Benefits Council and its European Compensation and Benefits Council took place in Brussels in October 2007. Discussions were wide-ranging, providing insights into issues such as global rewards, long-term incentives, and expatriate pension options, as well as how to attract and retain talent in China, Eastern Europe, and the Middle East. The highlights of those discussions are presented in this report.)

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Traditional compensation and benefit approaches may not be effective in addressing the issues. Employees across the globe want more choice in their compensation and benefits packages and have elevated expectations for pay for performance, career development, learning opportunities, access to technology, and interactions with their leaders. This requires more flexibility and integration across all areas of human resource and talent management.

Changes in Global Rewards

One U.S-based manufacturing company with tens of thousands employees worldwide and experiencing HR and talent management challenges as it globalizes its operations, is successfully addressing them by making changes in its approach to global rewards. The changes include compensation plan design modifications, driving common global philosophies, processes, and tools deeper into the organization, and changing the compensation and benefits organizational structure.

The company focused on establishing and building understanding of a common global compensation and benefits approach further down into the organization. Previously it had concentrated primarily on ensuring a common global approach to compensation and benefits for top executives globally. Work began with compensation "basics" such as the company's pay and benefits philosophy, common use of the company's level and grade structure, building global career ladders for each of the functions, providing guidance in the use of titles, and developing global job descriptions.

The company is currently developing an in-house compensation and benefits certification program to ensure in-country compensation administrators are consistently trained in areas such as benchmarking, merit fund and pay range development, and establishing promotional guidelines. A longer-term goal is the implementation of a common annual incentive plan design for all salaried employees that mirrors that already used for executives globally. These changes are being supported by an overall increase in communications with employees which include global webcasts, greater availability of materials on-line, and use of common global templates for country communications.

The company also found it necessary to modify some of its compensation plans so there is less volatility in payouts, especially important in high-growth markets and for employees with critical skills. The annual incentive plan measures were modified to include a portion that will pay out even when corporate financial objectives are not met. Stock option usage has also been reduced and restricted stock units introduced as a replacement.

Other changes include a more rigorous approach to pay for individual performance not linked to company financials and the availability of off-cycle base increases to provide greater assurance of retaining key talent. Premium salary structures have also been introduced in countries where local pay structures are not sufficient to retain key talent.

Another focus for the company has been building a more globally integrated HR network to maximize the organization's performance across the board. The company believes that over time, the network will increase its ability to support quick start up of new operations, and eliminate redundant or inconsistent activities across more mature markets. As part of this effort the overall HR structure has changed so that corporate centers of expertise have more team members located in non-U.S. locations.

Managing Employee Mobility

Scandinavian countries are often ranked among the best in the world for their quality of life, but for one large telecommunications company that is based in the region and rapidly expanding into emerging markets in Asia, Scandinavia's attractiveness is creating two major challenges. The first is that it is difficult to persuade high-potential employees in the region to accept long-term (up to three years) overseas assignments outside Scandinavia, and particularly in Asia. Often, the people who are prepared to relocate are not the ones the company has identified as candidates for exposure to international markets and new business perspectives.

Table 1: Trends in Executive Long-term Incentives: Europe Versus the United States

LTI	*United States* Trend	*United States* % of total	*Europe* Trend	*Europe* % of total
Share options	↓↓	50	↓↓↓	25
Time vested restricted shares/share units	↑↑	30	↑	15
Performance vested restricted shares/ performance shares	↑	15	↑↑	35
Performance units/cash bonus	↑	5	↑	25

Source: Rein Pikaart, Vice President, Executive Compensation for Royal DSM N.V

While the company now makes it clear to aspiring top managers that they must have some international experience as part of their career development, it remains an area of contention. One of the difficulties is that many of the current executives in the company were not required to complete an extended overseas assignment (arguably because then the company was far less global in outlook). Another is the increase in dual-career couples and the reluctance or refusal of one partner to jeopardize his/her career prospects for the other. In the company in question, this is especially true of couples and families being asked to move from Scandinavia to Asia.

Solutions include the use of more non-traditional expatriate management models such as short-term assignments of three to six months, international commuting (in some cases to Asia) for six to 24 months, globetrotters (people who move from one overseas assignment to another and are managed through a global employment company, like traditional long-term expatriates) and virtual assignments (using the latest communications technology to help manage international operations and international teams remotely, dramatically reducing the need for travel).

In contrast, high-potential employees in Asia are more than willing to transfer to Scandinavia under Scandinavian terms and conditions. In this case, the challenge is persuading the employees to return to Asia and then managing their repatriation.

Changes in Long-Term Incentives and Some Thoughts on their Effectiveness

Long-term incentives are widely used in U.S. and European companies (although less so in those in eastern and southern Europe) to attract and retain executives. However, there continues to be major differences between the two markets in both grant levels (with U.S. executives generally being offered higher grants than those in Europe), and in the mix of incentives. As can be seen from **Table 1** share options are currently more popular in the United States than in Europe, although in both cases the trend is to switch to other vehicles, namely time-vested restricted shares/share units, performance-vested restricted shares/performance shares or performance units/long-term cash bonuses.

In Europe, the already high use of performance-vested restricted shares is expected to go higher still, reflecting companies' attempts to more closely link pay and performance. Council members at the meeting estimated that 85 percent of long-term incentive plans in Europe have performance conditions attached. In contrast, there was general agreement among the Council members that in the United States the dominant trend is toward the use of more time-vested restricted shares.

While members at The Conference Board meeting agreed with the general shift in focus of long-term incentive plans in Europe and the United States, they were less in concert about the effectiveness of these incentives. The view of a major industrial company based in continental Europe that has undergone considerable change during recent years because of several mergers and acquisitions and divestments, is that they frequently fail to meet their objectives.

According to this company, it is a myth that performance-related, long-term incentives have a significant impact on individual behavior, especially at lower levels of the organization. In other words, they are not motivating employees to meet business objectives. Similarly, the company says there is no clear link between employees' activities and shareholder value, yet one of the prime objectives of these incentives is to enhance shareholder value.

The company also insists that the expected value of the incentives is rarely a good measure of the employee's perceived value. Finally, it says that equity compensation for executives often has little value as a retention tool, arguing that top talent can usually be tempted with the right compensation package, with little thought about the incentive plan they may be leaving behind.

That said, the company in question developed a new long-term incentive plan a few years ago aimed at its worldwide executives. The plan is based on stock options and stock appreciation rights, a strike price that is based on fair market value at the date of grant and is partly performance related. Grants are made annually and the level is based on the executive's position within the company. The plan has a term of eight years, a vesting period of three years and vesting criteria that are partly time-based and partly related to the achievement of predefined performance targets. Performance measures are linked to total shareholder returns.

From both the employer and the employee's perspective, the plan is a success, despite the reservations about many of the attributes of such plans expressed by the compensation executive from the company who attended The Conference Board meeting. The plan is cost effective for the company, using dynamic hedging, and, as part of a remuneration package, has succeeded in attracting many executives.

Pension Challenges for Globally Mobile Employees

Pensions are another integral part of a remuneration package that has some influence on attracting, retaining, and motivating executives, especially mobile executives. While different companies adopt different approaches to retirement benefits, one U.S.-based industrial multinational, typically with hundreds of expatriate executives, told the meeting that its provisions vary depending on the career path taken by the expatriate.

For traditional expatriates who relocate to a host country from one to five years and expect to return to the home country, pension arrangements are relatively straightforward. These people continue on the home country plan. This is a common approach and one used by some companies for all of its expatriate community—traditional and non-traditional.

The company decided to use the proration method where applicable because it is the one that is most in line with its global benefits principles. According to these principles, pensions are designed to meet the competitive market, rather than other plans within the company.

They are also part of a total rewards package and coordinated with social security systems, both of which vary by country. The company also has a strong bias toward defined contribution plans.

Home Country Plan

Advantages

- Maintains ties with home country and equity with home country peers
- Keeps social security and compensation mix aligned
- Reinforces the temporary nature of the assignment

Disadvantages

- Expensive and administratively complex
- Not always tax deductible/excludable
- Inconsistent with host colleagues

The company in question, however, has considered a number of options for its non-traditional expatriates and compared their advantages and disadvantages. For those who relocate permanently to the host country and have no intention of being repatriated or moving to another country, it examined four options:

Project and Prorate – in which the benefit in each plan at retirement/termination is calculated as if the individual was in the plan for his/her entire career at company, and prorated according to actual service in the plan.

Advantages

- Equitable
- No defined benefit (DB) or defined contribution (DC) issues
- Copes with all types of design
- Consistent with social security
- Consistent with pension being a career accrual of deferred compensation

Disadvantages

- Complex administration
- May result in some unfunded or non-qualified benefits where a pension cannot “roll up” pay
- Benefit shortfall at career end difficultto allocate

Leaving Service Benefit – in which benefit at termination from each plan is calculated and individual is treated as a new hire in their new plan.

Advantages

- Simple
- Easily administered
- Works for transfers to pension equity plans
- Transferring business/function pays upon transfer, not years later

Disadvantages

- Inequitable for transfers to traditional DB plan
- Inequitable for transfers to single contribution DC plans
- Potential shortfall at retirement
- Potential barrier to mobility

Full Service in New Plan with Offsets – in which individual receives past service with company as additional years of service in new plan, offsetting any other benefit received for the same period.

Advantages

- Easy to communicate
- Works well for permanent transfers
- Qualified funding maximized
- Great for going to a rich plan

Disadvantages

- Creates many winners and losers
- Requires details of offsets
- Not effective for transfers to DC plans
- Horrible for going to a poor plan

Computed Service in New Plan Based on Relative Formulas – in which individual receives.

Advantages

- Equitable
- Qualified funding maximized

Disadvantages

- Complex to compute
- Not effective for transfers to DC plans

For other types of expatriates, namely "global nomads" (employees who permanently leave the home country for a series of expatriate assignments) and "international orphans" (employees who are unable to continue in the home country plan and their career path is unclear), the company has devised international pension plans. One, designed for mobile, high-potential employees with at least three consecutive moves and expectation of future moves, is a combined unfunded pension equity plan and a funded defined contribution (DC) plan.

Another, designed for "international orphans", is a savings plan that comprises a funded DC plan (to which the company contributes and the employee contributes voluntarily) and investments that are self-directed through a third party financial services organization.

Attracting and Retaining Talent in New Markets[1]

The rapid and continuing growth of emerging markets, like Eastern and Central Europe, the Middle East and China, is creating a demand for local talent that is difficult to meet, especially at the executive and management level. Companies in Europe and the United States that are investing in these markets often find they are competing with each other as well as with local companies for the best people. If they are successful, they then face the additional challenge of developing and retaining their new recruits in the long term.

To better understand the role of compensation and benefits practices in attracting and retaining managers in these regions, three simultaneous workshops were held in Brussels during the joint Council meeting. Their aim was to provide some universal insights into each of the markets by tapping into the experience of multinational companies that are already operating in them. In every case the findings emphasize the need to provide potential employees in a region with a vision of the future and personalized (and often rapid) development.

Central and Eastern Europe

Challenges

- Growth in demand for executive talent
- Many companies searching for employees with a similar profile
- Cultural differences that become more pronounced the further east traveled
- Reliable data on compensation and benefits is difficult to ascertain, partly because the market changes so quickly
- Employees often distrust the information that is provided

Strategies for Attracting and Retaining Employees

- Offer retention bonuses at least equal to (or more than) the annual salary to the top 10 to 15 percent of key individuals if they stay for a period of two to three years.
- Adopt a proactive approach by improving the attractiveness of the company and its proposition by stressing such issues as career and leadership development, compensation and benefits, employer branding, and work-life balance
- Use competitive advertising to attract people and create a long-term bond with the company
- Recognize differences between eastern and central Europe in the type of remuneration package that attracts: typically in eastern Europe people are motivated by cash rather than long-term incentives, often questioning the upward potential of western shares, while in central Europe the trend is towards a more standardized approach, similar to the package deals offered in western Europe
- Be prepared to offer employees loans for homes or to pay their rent (a practice that is common in Russia)

Middle East

Challenges

- Growth of both traditional sectors (like oil and gas) and non-traditional sectors (like finance) causing talent shortages across industries and at all managerial levels
- Many infrastructure projects are underway to support growth in the economy, creating a demand for engineering and construction professionals, many employed from overseas
- A high proportion of the workforce in the region is expatriates from countries like Pakistan, India and Egypt, creating diverse organizations
- No one company is providing market data on all countries in the region

Strategies for Attracting and Retaining Employees

- Joint ventures with local partners offer opportunities for sharing talent and gaining a greater understanding of cultural differences
- Provide well-designed compensation and benefits packages that include long-term incentives, although recognize that strong focus should still be on cash remuneration rather than performance-based incentives
- Offer allowances for housing, education and transport and, in some cases, be prepared to find accommodation for employees
- Offer employees long-term career growth opportunities through training and skills enhancement
- Empower employees and be prepared to offer them responsible jobs

China

Challenges

- Very small multi-lingual pool of talent
- As a result of the cultural revolution the choice of suitable candidates is generally limited to those below the age of 40, although the one-child policy has led to a rise in the “quality” of children in terms of improved health, chances of survival, levels of educational attainment, and eagerness for responsibility
- Chinese executive talent is still germinating
- The executive education market is growing with more MBA courses being offered, although the quality of education is not high in some cases
- Confucian values drive loyalty to family first
- Provincial diversity is vast and much more complex than in Europe, although this does offer the opportunity for deal-making in terms of labor agreements and tax breaks for example
- Salary (and skill) differentials exist between different tiers of cities (with tier one cities like Beijing and Shanghai receiving the highest pay) and between local Chinese nationals, returnees from Hong Kong, Taiwan and Singapore, and expatriates (with expatriates receiving the highest remuneration)

Strategies for Attracting and Retaining Employees

- Offer strong career and development opportunities, including overseas secondments, and ensure that an individual’s career path is transparent
- Develop a coaching and mentoring culture that fosters mutual training of expatriates by Chinese nationals in the Chinese market and Chinese nationals by expatriates in international management standards
- Develop individuals’ self-awareness of their leadership styles, which tend to be focused too heavily on command and control, and the sort of environment they are creating for employees
- Recognize that job titles, status, and what appears on a business card are of great importance
- For wholly foreign-owned companies, it is possible to design a reward system from scratch, although it will need to reflect the different salary scales of tier one to tier three cities
- Employee stock ownership and employee stock purchase plans are now allowed
- Retirement benefits, housing loans and transport are other benefits that employees increasingly expect

1 For a more detailed discussion of global employee retention strategies please see the forthcoming report from John Gibbons of The Conference Board on Global Employee Engagement. Gibbons finds that some components of employee engagement are culturally specific, while others are universal across the globe. Indeed, Employee Engagement is driven by different combinations of dimensions of the overall employee experience, called drivers, in each country. However, the following drivers have been shown to apply in nearly every country in the study: 1) variety and challenge of the work, 2) an interpersonal relationship with one’s immediate manager, 3) a sense of shared values with the organization, and 4) career growth opportunities.

Council Perspectives™

Members of The Conference Board Councils are among the most experienced and savvy executives in the world. Their private deliberations produce rich insights on the most challenging business and societal issues of our time. With their permission, we have channeled their energy and expertise into Council Perspectives, a new platform to voice their views.

Council Perspectives is based on sessions from selected council meetings, post-meeting interviews, and other pertinent data, and may sometimes include original content written by council members. It is not intended to be a research report; rather, Council Perspectives provide a unique look into the minds of executives from leading global organizations as they assess, analyze, and develop ways to address critical issues.

About This Report

When organizing the first joint meeting of the International Compensation and Benefits Council and the European Compensation and Benefits Council in Brussels in October, 2007, The Conference Board was aware of the difference in approaches in European and U.S. companies towards human resource management across their global operations. Nevertheless, it believed that by providing an opportunity for council members to discuss their practices and experiences in dealing with a diversity of geographies and cultures, some insights might emerge. This proved to be the case.

Commercial priorities mean that there are broad similarities in some of the strategies being devised in Europe andthe United States for attracting and retaining talent around the world. The joint event encouraged council members to exchange their views and ideas, and to share the challenges they all face as their companies move into new and emerging markets in Asia, Eastern and Central Europe, and the Middle East.

This event was groundbreaking in that it was the first time these two "partner councils" have met face-to-face, and also the first time the international group has convened outside of North America. The occasion was attended by 44 council members – 30 based in Europe and 14 based in the United States – representing 42 different organizations from a cross-section of industries, including oil and chemicals, automotive, communications, financial services, logistics, and information technology.

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About The Conference Board

The Conference Board is a global, independent business membership and research association working in the public interest. Our mission is unique: to provide the world's leading organizations with the practical knowledge they need to improve their performance *and* better serve society.

The Conference Board creates and disseminates knowledge about management and the marketplace, conducts research, convenes conferences, makes forecasts, assesses trends, publishes information and analysis, and brings executives together to learn from one another. The Conference Board is a not-for-profit organization holding 501 (c) (3) tax-exempt status in the United States.

About The Conference Board Council Program

Membership in one of our councils affords entrée into a select and trusted community of 2,500 executives from a broad array of industries, functions, and regions—executives who know the value of this rich source of insights and new approaches.

Enduring relationships are the cornerstone of the Councils experience. Enhanced by our global, enterprise-wide reach, these relationships span the world and extend value across your organization. Confidential peer dialogue combines broader perspective, specific knowledge, and shared experience to save you precious time and public missteps.

To learn more, contact Katie Plotkin, Councils Membership Manager, +1 212 339 0449 or katie.plotkin@conference-board.org. Council participation is by invitation only and is an exclusive benefit for The Conference Board member organizations.

About the Councils

European Council on Compensation and Benefits

The formation of the Council on Compensation and Benefits in 1995 recognized the complexity of cross-border remuneration issues for companies operating across Europe. The rapid pace of change in regulations and management strategies make it increasingly important to compare management experiences with colleagues from other companies with similar responsibilities. Regular features of Council meetings are roundtable discussions in which members update each other on developments in Compensation & Benefits in their countries

Council on International Compensation and Benefits

Founded in 1970, this council is composed of executives from very large companies with extensive global operations. This requirement ensures a vibrant ongoing network of peers, who share ideas and best practices electronically as well as during face-to-face biannual meetings. Discussions focus on the policies and challenges connected with the salaries and benefits of international personnel, including local nationals as well as expatriates.

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