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# Don't shy away from equity compensation as reward

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Attracting and retaining top talent may be at the forefront of management's minds these days, but many companies don't practice what they preach when it comes to equity compensation. Surprisingly, recent studies found that midsize companies are decreasing equity compensation to top talent as part of an overall trend of reducing stock for most employees below the senior management level.

Market conditions are forcing these cutbacks, including: increased cost of expensing options under federal regulation FAS 123R, growing pressure by boards of directors to limit shares of stock issued, and the belief that employees don't truly value this benefit.

Reducing equity compensation doesn't come without a cost. Even if stock is not highly valued by employees, eliminating it could affect employee commitment and increase turnover. Companies should be careful they are not sending the wrong message to employees. While executives say they value performance, they are actually decreasing the link between employees' pay and company performance.

The following are guidelines in developing a cost-effective equity compensation plan:

- Align equity compensation with business goals. An equity compensation plan should reinforce your overall business plan and leadership philosophy. Identify the talent you need to grow your company and establish compensation and other reward programs that tie people directly to achieving company goals.
- Use equity as a strategic tool to attract key talent. Smaller companies are often strapped for cash and therefore need to rely on equity compensation more than larger companies that can offer higher salaries. Equity plans can give people a compelling reason to join and remain at a company.
- Consider both long-term and short-term goals. Because equity gives employees a share in the future value of a company, it motivates and rewards them for achieving long-term business goals. Bonuses and salaries, however, are focused on today's performance and operational issues. A blend of short- and long-term compensation will strike the right balance, encouraging people to take the right actions.
- Determine the relationship you want to create between equity and performance. To use equity effectively, consider the linkage you want to create between equity awards and performance. Should equity awards be based on one's position and continued employment in the company or the contribution one provides? Are the performance metrics short-term results or ones that impact the long-term value of the company?

- Develop innovative approaches. There are creative ways to decrease the costs of equity while still offering value to employees. Restricted stock units (RSUs) enable companies to decrease the number of shares they are awarding and provide similar growth potential as stock options. Consider tying RSUs to the achievement of business goals or project milestones, and awarding shares to employees based on strategic performance measures or providing them as spot awards for special projects or accomplishments.

Before you opt to decrease equity compensation because "everybody else is doing it," consider the impact it will have on your organization. Determine the overall human resource and compensation strategy you need to achieve your business goals. Assess industry benchmarks to see where your organization fits vis-à-vis the marketplace and look for opportunities to make your company distinctive. By providing high-impact compensation programs that reward top talent and superior performance, you can stake out your competitive advantage and be a winner in the talent wars.

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