

# Attract, Retain, Motivate...Educate?

## RETIREMENT & BENEFIT PLAN SERVICES

**Attract, retain, motivate.** This well-worn compensation and benefits mantra may need some tinkering, as new competitive realities in the worldwide workforce emerge. Competition for top-level talent in key areas is heating up, but most companies are not in a position to throw cash, benefits and shares at the problem. Companies seeking to pay for performance are introducing new, more complex equity compensation structures that challenge employee understanding. Should our modern formula for success now become, “Attract, retain, motivate...**educate?**”

## Equity plans and effective communication will play a key role in a renewed war for talent

Recovery from one of the worst recessions in history has begun. The World Bank estimates that global GDP, which expanded by 3.9 percent in 2010, will grow 3.3% in 2011, and reach 3.6 percent in 2012.<sup>1</sup> Bank of America Merrill Lynch estimates 2011 U.S. growth to be about 3.5 percent<sup>2</sup>, with more employment, more capital expenditures, an increase in exports, and continued monetary and fiscal stimulus.

Although overall unemployment in the U.S. remains stubbornly high, with uneven hiring across industries, early-warning signs point to the re-emergence of a war for talent. The 2010 Bank of America CFO Outlook reveals that 47% of companies expect to hire additional employees in 2011. Only 6% expect to reduce payrolls versus 9% a year ago.

### Consider the following:

- Corporate profits are strengthening and companies are holding significant positions in cash—a trend that is expected to fuel new job creation.
- A renewed focus on hiring has returned: 76% of companies in a recent survey report that budgets for talent acquisition will increase or stabilize in Q1 2011 — a 72% increase compared to 2010.<sup>3</sup>
- The number of companies expressing positive hiring plans is at its highest level in a decade. What’s more, 34% of firms surveyed reported larger workforces compared to only 13% in early 2010.<sup>4</sup>

### In this paper

- We will explore the renewed war for talent, and what’s different this time around.
- We will preview how new equity program configurations, with appropriate education, might give companies an edge in the battle, and help align employee behavior with business goals.

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For many who weathered the economic storm, company loyalty is waning and those unsatisfied in their current positions are beginning to seek “greener pastures.” According to a recent survey, 30% of Gen-X workers, 20% of baby boomers and 22% of workers aged 61 and older are considering a job move.<sup>5</sup> The war for talent has begun.

### A skills shortage is heating up the battle

Finding individuals with the right combination of skills, knowledge and experience has become challenging for many companies. According to Manpower’s fifth annual Talent Shortage Survey, 31% of employers worldwide cannot fill key positions. This situation has resulted from an apparent mismatch between applicants and the desired talent organizations require to drive their businesses forward.<sup>6</sup>

The talent shortage is most intense among highly skilled, educated professionals, technicians and managers. According to Mercer’s 2010 Attraction and Retention Survey, skills shortages in R&D/scientific engineering and sales, information technology and executive/top management are among those in greatest demand.<sup>7</sup>

#### Consider the following:

- 32% of industrial companies report moderate to serious skills shortages. Moreover, that number nearly doubles for biosciences.<sup>8</sup>
- The number of software engineers is projected to grow 32% between 2008 and 2018 fueling demand for key talent.<sup>9</sup>
- Mining engineering positions face critical shortages worldwide.<sup>10</sup>

Also, consider these converging macroeconomic forces:

- **Demographic trends:** Organizations will likely face significant knowledge loss as a wave of baby boomers retire or change jobs over the next decade. At the same time, research shows there will be a shortage of qualified younger workers to replace them.

- **Emerging power centers:** As more developing economies transition to developed status, the growing affluent middle class in countries such as China places greater demand on domestic markets. As a result, these countries will increasingly require more highly skilled workers than currently exist among their domestic workforce.
- **Employee power shift:** Power is moving from the employer to the employee as workers with coveted skills have greater leverage to demand flexibility and job mobility. Human capital is replacing financial capital as the engine of economic prosperity.<sup>11</sup>

By 2015, 60% of new jobs will require skills held by 20% of the population.<sup>12</sup>

### Retaining top talent is critical to success

Companies able to recruit and retain the best and the brightest will be in a position to drive innovation and maintain a competitive edge. The workforce of the future will demand that organizations become more agile in how they attract, develop and retain their employees.

In the global marketplace of tomorrow, talent will be the key differentiator. By 2015, 60% of new jobs will require skills held by 20% of the population.<sup>12</sup> The talent shortage is slowing recovery and growth for many companies — a situation that is likely to worsen as the economy continues to strengthen.

While the cost of replacing an employee, particularly a highly talented one, varies, one thing is certain: attrition can be costly. When these costs are multiplied by the number of employees who leave over the course of a year, the profit loss can be substantial.

### The increasing, shifting role of equity plans

Traditionally, equity compensation plans, such as stock options and restricted shares, have been a competitive necessity for companies to attract and retain key people. These plans demonstrate that the

company is trying to improve the alignment of pay, performance, and long-term shareholder value. It is reasonable to expect increased emphasis on equity plans as the renewed war for talent heats up.

Prevalence of performance-based plans	
Performance plan available	Percent of companies
2004	30%
2007	64%
2010	71%

Source: "Trends and Analysis from the 2010 Stock Plan Design Survey," NASPP/Deloitte, August 10, 2010.

However, as shown above, the structure of long-term incentive plans is undergoing a transformation, with more emphasis on non-market based, performance-driven rewards. Specifically, companies have begun to deemphasize the use of stock options in favor of restricted stock and other incentives with complex performance triggers—largely in response to the equity market downturn, accounting rules, and increased government scrutiny.

Companies are increasingly diversifying their equity compensation and long-term incentive programs with a portfolio mix of plans, rather than simply using a one-size-fits-all approach. Now companies are starting to grant performance shares beyond a narrow group of key executives who steer a company’s long-term success.

**Consider the following:**<sup>13</sup>

- In a recent survey, 91% of companies have an omnibus plan that provides multiple award grants under one plan.
- 53% of companies have increased their use of restricted stock.
- 71% of companies currently use performance-based awards as a portion of their total compensation plan.

While not surprising, it appears more changes are underway. According to compensation consultant Mercer, 65% of organizations introduced in 2010, or plan to introduce in 2011, new financial performance measures in their annual incentive programs.<sup>14</sup>

**Why educate?**

As equity compensation plans grow more complicated—designed around growth factors, revenue, return/margin and additional performance metrics—the need for education surrounding these awards has become essential. Given the growing complexities of these plans, there is increasing concern about participant understanding, specifically:

- Do they understand the metrics used to determine payout?
- Do they know how to coordinate awards with other financial programs?

According to Deborah Howard, a Senior Vice President - Investments and Financial Advisor with Merrill Lynch, “Many key employees are planning for college tuitions, a retirement home, a ‘second act,’ and other important objectives, often with a recently devalued financial portfolio. They are back to basics on situational planning and guidance. We need to help them achieve financial wellness by explaining the value of their mix of benefits and compensation. Specifically, what plans feed their objectives?”

**“We need to help employees achieve financial wellness by explaining the value of their mix of benefits and compensation.”**

—Deborah A. Howard, Senior Vice President—Investments and Financial Advisor, Merrill Lynch Global Corporate & Institutional Advisory Services

With heightened retention efforts at organizations around the world, it has become critical for employees to recognize, understand and appreciate how performance impacts compensation. They will want to view their total compensation program in an integrated way, making effective communication essential to motivating and retaining skilled people.

For more information about how we can help your company and its employees, contact your Bank of America Merrill Lynch representative or call **1.888.550.7705**.

Visit us online at **benefitplans.baml.com** or email us at **benefitplans@baml.com**.

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Broadly capable in virtually every type of benefits solution, Bank of America Merrill Lynch offers flexibility to plan sponsors. With experience across the spectrum of retirement, equity and other wealth accumulation plans, we are positioned to help American workers achieve financial wellness at all stages of life. We provide access to a full range of equity compensation plan choices, including:

- Stock Options—Nonqualified (NQ) and Incentive (ISO) based plans
- Restricted stock and restricted-stock units
- Performance awards and performance units
- Dividend-equivalent units
- Stock-appreciation rights
- Restricted cash awards
- Employee Stock Purchase Plans

<sup>1</sup> "Global Economic Prospects", World Bank, January 12, 2011.

<sup>2</sup> "2011 CFO Outlook Survey", Bank of America Merrill Lynch, January, 2011.

<sup>3</sup> "Recruiters Amp Up Hiring Budgets, But Are Challenged By Influx Of Resumes", www.talentdrive.com, February 2, 2011.

<sup>4</sup> "New NABE Survey Shows Signs Of A Strengthening Recovery", www.nabe.com, January, 2011.

<sup>5</sup> "Study Indicates War For Talent Back On In The Workforce", 2010 Survey by Adecco Group, PRNewswire, April 20, 2010.

<sup>6</sup> "Is Talent Holding You Back? Designing Workforce Strategy For Sustained Business Growth", Manpower 2010 Survey.

<sup>7</sup> "2010 Attraction And Retention Survey", Mercer.

<sup>8</sup> "People And Profitability—A Time For Change", Deloitte, Manufacturing Institute and Oracle, 2010.

<sup>9</sup> U.S. Dept. of Labor, Bureau of Labor Statistics.

<sup>10</sup> "Key Jobs In Mining Sector Facing Skills Shortages", Reuters, June 29, 2010.

<sup>11</sup> "Global Talent Risk: Seven Responses", Boston Consulting Group, January 7, 2011.

<sup>12</sup> "Hiring Is Getting Harder for Employers, Not Easier", Forbes, January 20, 2011.

<sup>13</sup> "Trends And Analysis From The 2010 Stock Plan Analysis Survey", Deloitte/NASPP.

<sup>14</sup> "Organizations Are Focusing On Measuring Performance Aligned With Pay", Mercer, January 19, 2011.

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