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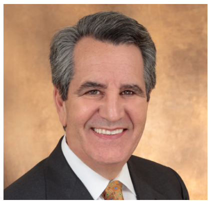

MICHAEL LASKY

Address economic motives to attract, retain, and reward talent

The owners of PR firms repeatedly say one of their biggest challenges is attracting, retaining and rewarding talent. It's a challenge made greater by the increased pressure from clients reducing budgets, bringing work in-house, and increasingly offering only project-based work.

Agency owners need to recognize that economic incentives can and do drive employee behavior. Increasingly, public relations firms are using two strategies to address the problem; long-term incentive plans and equity-based incentive arrangements.

Studies show that when implemented properly, both strategies can enhance performance, revenue, growth, and profitability. The best of these arrangements send powerful messages to all employees, even the non-participants.

Employees in the plans feel they benefit personally from the achievement of specific, objective goals over the long term. And non-participants aspire to participate in the programs when their level of responsibility and importance to the firm and its clients increases.

Long term incentive plans can be established for individuals or groups of employees and have been used for decades to motivate employees in a wide range of industries.

They often set annual key performance indicators or targets. The most common targets at PR firms are profit margin, profit growth and/or revenue growth, according to a Davis & Gilbert survey.

Typically, these plans vest and pay out in annual installments — two, three or more years, depending on the needs of the firm and design of the plan. But single payouts can also be made at the end of a three-year measurement period (or whatever period is established).

Long term plans promote retention because the unvested portion is typically forfeited if the employee resigns or is terminated. Employees tend to think twice about losing the benefit and the plans make it more expensive for competing firms to lure employees away.

Equity-based programs are designed to create bonds of ownership by aligning the objectives of the recipients with those of the owners. They also enhance compensation packages without expending cash or affecting profit margins.

Using equity to reward potential employees can contribute to a firm's long term health and, in the case of acquisitions, can be important to potential buyers looking to retain key employees. However, granting real equity can be difficult.

First, the grant of real equity often requires a payment of some amount by the key executive to the company. Also, in many instances receiving equity is a taxable event for the employee. And because stock in a privately-held firm is completely illiquid, the employee can't sell it to pay the taxes, like they can at publicly traded companies.

Second, real equity requires the preparation of a shareholder agreement with a buy/sell obligation upon the employee's termination. And finally, when employees receive real equity they have the right, under corporate law, to inspect the PR firm's books and financial records.

To avoid these difficulties, many PR firms use contract or "phantom" equity. Contract equity is very flexible. It can be customized with a relatively simple contract and doesn't require an investment by the employee. And employees don't have to pay taxes when they first receive contract equity, only when they actually receive funds from the equity. Those funds, however, are taxed as ordinary income and not at the lower capital gain tax rate.

The most common form of contract equity provides the employee the right to participate in the proceeds when the PR firm is sold, with certain restrictions. Other contract equity agreements offer the right to participate in the profits of the firm or of a practice area, division, or some other objective criteria.

Both long term incentive plans and contract equity agreements can be effective in attracting, retaining, and incentivizing the very best talent. And in today's competitive PR talent market, the design and implementation of the right compensation programs is vital.

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