

TCS Commentary – Adaptive Compensation Under COVID-19

COVID-19 has put tremendous strain on compensation plans for essential workers in the healthcare industry. It has raised the question how and when is it appropriate to adjust salaries and grant bonuses? In response to these concerns, Total Compensation Solutions (TCS) compiled information from a variety of Industry Pulse Surveys conducted by major consulting firms. These surveys and our own proprietary studies indicate that there are a variety of actions that Boards of Directors and management will need to consider in reaction to the COVID-19 crisis.

Industry sectors most significantly impacted by the crisis, including the healthcare continuum (acute, long-term and assisted living), are adapting to the crisis by offering higher compensation to staff to get them to come to work; and recruiting health care workers with open hiring requisitions. With premium pricing on equipment as well as services, this translates to significantly higher operating expenses for 2020 which the management team needs to address.

In line with these observations, TCS suggests an alternate course of pay actions for the healthcare industry to consider – we refer to this alternative as Adaptive Compensation. The following options allow healthcare industry boards and management to review the impact of COVID-19 on their business throughout calendar 2020 and react in a fair and equitable manner:

- Executive Pay – TCS observes that the healthcare industry, which is bifurcated into for-profit and non-profit entities, does a good job of self-regulating executive pay practices. Typically, these institutions offer merit-based adjustments in base salary at the start of the year. Maintenance of current base salary levels for executives in healthcare would seem to be prudent given the experience of these individuals, the competitiveness of the market, and the current level of economic activity due to the crisis. However, market-based adjustments should continue to be considered.
- Staff Compensation – Many healthcare institutions report that they must increase base salaries for staff positions simply to get people to come to work. TCS suggests that these institutions should maintain their current hiring ranges and use Hiring Bonuses to onboard needed resources.
- Short-term bonus/incentive – Most healthcare institutions evaluate performance at year-end and award bonuses/incentives within Q1 of the following year. Awards under formal incentive plans for 2019 have already been made and logically cannot be clawed-back. These are the same awards that critics disparage as excessive even though they were for past performance.

Short-term plans for 2020 performance will depend on how the year turns out. For 2020, the downturn in economic activity is palpable. While many institutions face rising expenses, it remains to be seen whether this will have widespread impact on the major performance metrics for the year. It also remains to be seen whether there will be a rapid, moderate, or slow turnaround in economic activity. Any of these scenarios will impact performance results differently and decisions regarding annual bonuses should be delayed until the results are in.

That stated, there are alternative approaches that boards and management should consider:

1. **Cut the bonus/incentive payouts** by a random percentage (e.g., 10% reduction in payouts). This appears to be a viable approach and may reflect the results for 2020. However, a well-designed bonus/incentive plan will already have a reduction of award (threshold) built in if results are not achieved.
2. **Adjust the performance targets** to better reflect the current economic environment. Formal bonus/incentive plans are frequently designed to allow mid-year adjustments in the performance plans due to conditions beyond the control of the executive team. An effective bonus/incentive plan can modify goals mid-year.
3. **Consider using the discretionary element** that most bonus/incentive plans include in their design. Strategic use of the board's discretion in reviewing the performance of the institution and making awards under the plan at year end is an effective method of showing the board's appreciation for the hard work of the executive team.
4. **Pay Spot bonuses** even if the institution does not achieve targeted results (due to factors beyond staff control). This is a great way for the board to show their appreciation for hard work. It recognizes the entire healthcare team (executive, management, and staff) for their efforts even though performance fell short of the threshold incentive level. The amount paid in Spot Bonus is typically one-third to one-half of the typical incentive plan threshold level.

Finally, if bonus/incentive payout becomes a cash management issue or even an optics issue, some healthcare institutions may opt to defer the payout into the next fiscal year. The total compensation package is a motivator for executives and staff largely because of the potential for significant incentive payouts. Denying these payouts when all pre-established performance metrics have been missed might be a demotivator. Deferral allows the institution to grant awards and spread out the expense over a longer period while ensuring employees this portion of their total pay package. TCS advises clients to ensure there is a substantial risk of forfeiture associated with deferred awards.

Healthcare institutions need to consider a variety of factors when evaluating the impact of COVID-19 on their pay programs. At this point in time, results for 2020 are not known. **Adaptive Compensation** can guide decisions on salaries and bonuses. TCS is prepared to assist with research on best practices in the industry, identifying the appropriate alternative for each unique organization, and presenting the potential alternatives to the stakeholders of the organization.

For questions on this and other compensation topics, please contact either Matt Leach dmleach@total-comp.com or Tom Bailey tbailey@total-comp.com or call us - 914-730-7300.