



Executive Compensation and Governance Trends for 2021 and Beyond

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As the response to COVID-19 continues, healthcare organizations nationwide face an uncertain environment in the near-term as vaccination rates slow, virus variants appear, and operational recovery from the pandemic accelerates. Additionally, there are a myriad of intermediate and longer-term forces at play—such as reimbursement pressures, technology disruption, workforce burnout and labor shortages, new competitive threats, and regulatory changes—that require attention.

The complexity of healthcare organizations continues to increase as pressures mount for financial sustainability, diversification, efficiency, and new care delivery models. Leadership retirements and burnout brought on by the pandemic have exacerbated the limited supply of executive talent with the skills, experience, and competencies needed to lead these complex organizations through significant change. As healthcare organizations and their boards confront this environment, executive compensation programs, talent strategies, and governance will continue to adapt.

In this article, we recap the response of healthcare organizations in 2020 and outline priorities for 2021 and beyond.

Pandemic Response: Impact on Executive Compensation

Compensation committees and healthcare leaders took several actions during 2020 in response to the pandemic:

- **Prioritizing the broader workforce:** The healthcare workforce rose to the challenge of meeting community needs as the pandemic took hold. The workforce made extraordinary professional and personal sacrifices to ensure patient needs were met. There was a focus on ensuring the broader workforce

was supported through the implementation of special incentives and pay differentials, accommodations for childcare and other personal needs, and the delivery of base salary increases when financially viable (with budgets in the 2 to 3 percent range).

- **Lowering base salary budgets:** Executive salaries were impacted with many freezing, temporarily reducing, or moderating increases. Broad-based workforce increases were prioritized over consideration of executive increases. About one-third of healthcare executives did not receive a base salary increase between 2020 and 2021. Overall, the median base salary increase for healthcare executives was 2 percent, which was lower than the initially projected pre-pandemic 2020 salary increase budget of 3 percent.
- **Changing incentives to reflect the COVID-19 response:** Executive incentive plans changed. Performance measures and goals were adjusted by many organizations to reflect shifting priorities in response to COVID-19. The adjudication of incentives was holistic as business judgment was applied to consider performance, pandemic response, treatment of the workforce, and stakeholder perspectives. Approximately 15 percent of executives did not receive an annual incentive award. For those who did receive an award, the typical payout as a percentage of the target opportunity was lower than in prior years.
- **Rewarding positions leading COVID-19 response and transformation:** Higher-than-average salary increases were observed for a number of positions that led the COVID-19 response or longer-term transformation efforts (e.g., Chief Operating Officer, Chief Medical Officer, Chief Technology Officer, Chief Nursing Officer, and Top Facilities Executive). In addition, more organizations reported emerging leadership positions in key functions, including telehealth, ambulatory care, digital strategy, and diversity, equity, and inclusion.

Key Priorities for 2021 and Beyond

There are five priorities for compensation committees as pay determinations are made this year and the executive compensation program's effectiveness is considered.

1. Compensation actions: Plan for flexibility as 2021 compensation decisions are made, to recognize the ongoing impact of the pandemic on operations:

- Executive base salary increase budgets are projected to rebound to pre-pandemic norms of 3 percent, although some organizations may provide more significant increase budgets to respond to retention and competitiveness needs.

→ Key Considerations for Compensation Committees

As healthcare organizations and their boards address changing performance priorities and leadership recruitment and retention needs during this uncertain time, executive compensation programs, talent strategies, and governance will continue to adapt. Compensation committees should expect an active agenda in this environment, focusing on five priorities:

- Ensuring **compensation actions** (base salary increase budgets, market adjustments, and incentives for 2021 performance) account for the rebound in the industry, the highly competitive talent market, and the challenges of operating in the environment. Anticipate the use of business judgment as actions are determined.
 - Align the **compensation philosophy** to evolving needs and provide for the flexibility to recruit, retain, and reward talent in line with changing needs.
 - Adjust the **incentive compensation program** to ensure performance measures reflect evolving priorities and payouts align with meaningful performance outcomes.
 - Review executive **talent strategies and succession plans** to account for new skill requirements and expected emergency and long-term succession requirements.
 - Incorporate **diversity, equity, and inclusion (DE&I)** into the compensation strategy—review pay equity, consider the role of the compensation committee in DE&I governance, and determine how the incentives and other programs can further DE&I goals.
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- Additional salary adjustments are anticipated for select roles based on data from SullivanCotter's *2021 Health Care Management and Executive Compensation Survey* (e.g., physician leaders and executives in operations, technology, nursing, supply chain, and quality).
 - Business judgment may be needed when determining incentive awards for 2021 performance, to account for the unanticipated effect on performance goals and priorities, as well as competitiveness considerations and stakeholder optics.

2. Compensation philosophy: Ensure the executive compensation philosophy supports the organization's recruitment, retention, and motivation needs:

- Peer groups that reflect the potential for recruiting talent from outside of traditional healthcare peers, including broader industry peers.
- Flexibility so that compensation can be appropriately competitive rather than tied to a specific percentile, to allow for variation based on a role's organization impact, performance, and other factors.
- Allowance for variation in pay models for different business units (e.g., health plans, long-term care, and business ventures).

3. Performance and incentives: Examine the executive incentive plan to ensure it aligns with new performance priorities and measures of success:

- Measures and goals that capture operating and strategic objectives, such as financial sustainability, patient experience, community benefit, care access, and deployment of new delivery models (e.g., telehealth).
- The degree of stretch in performance goals to help ensure meaningful performance is attained for corresponding payouts.
- Consider long-term incentives that reward for attaining multi-year transformation objectives.
- Consider the impact of regulatory developments on incentives (e.g., actions to encourage more competition).

4. Executive talent strategy and succession: New skills and competencies will be required to achieve organizational goals. Plus, organizations should plan for executive turnover due to the competitive talent market and career/retirement changes accelerated by the pandemic:

- Expect to recruit from expanded talent markets (including for-profits) for select positions based on specific organizational needs (e.g., telehealth/digital executives from IT and population health executives from managed care organizations).
- Anticipate the need to provide highly competitive pay for new recruits.
- Refine executive succession plans (including the identification of emergency successors) based on the organization's talent needs.
- Ensure there is a strong talent pipeline and determine if talent will be developed internally or recruited externally.
- Assess organizational structure and spans of control to support the delivery of cost-effective and quality care using new operating models.
- Monitor the impact of regulatory developments (e.g., potential restrictions on non-competes).

5. Diversity, equity, and inclusion: Determine how diversity, equity, and inclusion (DE&I) priorities will impact the executive talent strategy, recruitment/retention, program design, and governance:

- Assess executive and broader workforce diversity through the use of governance dashboards and other committee reporting; understand how talent strategies and succession plans are considering DE&I.
- Ensure that pay equity is assessed and that processes and policies are in place to monitor and maintain pay equity over time.
- Consider the use of DE&I measures in annual and/or long-term incentive programs.
- Expect highly competitive compensation for DE&I leadership roles.

Conclusion

Healthcare organizations increasingly are focused on opportunities emerging from the pandemic. Compensation committees should expect continued refinements to the executive compensation program and talent strategies to support organization and performance needs.

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