What does a Bad Executive Hire Cost YOU?

Self-Audit Estimates Your Costs

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Acadia Associates, Inc.

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What are your costs of a Bad Executive Hire?

Few companies know.

Paradoxically, while most companies don't measure the costs of a bad executive hire (they do for lower level employees), they believe the costs of a bad hire at the executive level are large and growing.

David Norton (co-author of *The Balanced Scorecard*) wrote in 2001,

- "Up to 85% of a corporations value is based on intangible assets and that in our New Economy, human capital is the foundation of value creation."
- "The asset that is most important (human capital asset) is the least understood, least measured, and least managed."

Experts estimate the Cost of a Bad Executive Hire ranges from 5 – 15 times salary.

What are your costs? Reputation Cost has increased the most in the last 5 years.

Read about the 5 Areas impacted and do the Self-Audit to define and estimate your costs.

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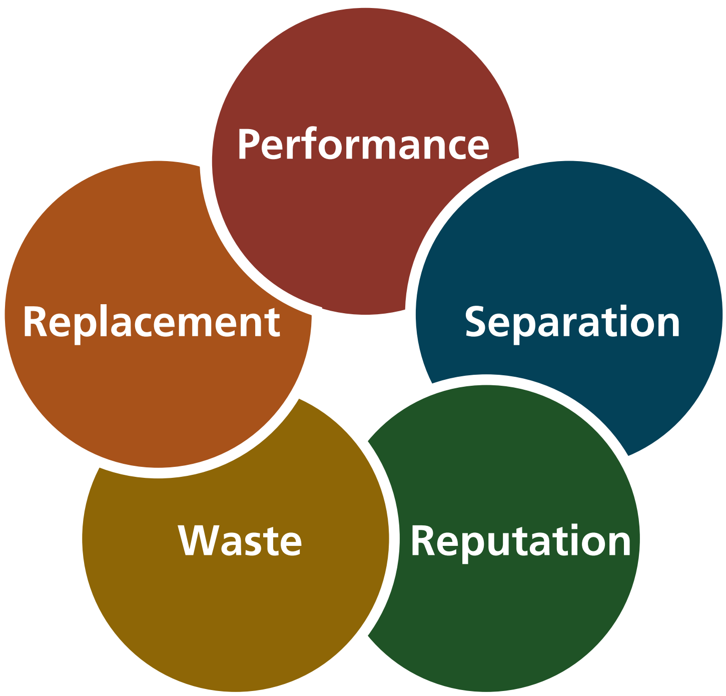
Five Areas are Impacted by a Bad Executive Hire



The following pages examine the impact of each area.

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Performance

I M P A C T

Bad Decisions regarding Clients

- Several internal clients now have new problems from bad decisions.
- 1 lost external client which effects current and future profit.
- Various negative effects from lost client on other departments.

+

Lower Productivity

- Executive hires "B or C" level employees.
- Those B or C players hire other B or C players and drive away "A" players.
- Some exising A players have lower morale and incentive for best effort.
- Effects of executive's own lower productivity, particularly during their 3 month Ramp-Down Period.*

+

Opportunity Costs

- Cost savings program never implemented.
- 1 missed new client.
- Employee retention program delayed.
- Reduced collaboration with other departments leading to fewer breakthrough ideas.

+

Increased Team Turnover Costs

- Several direct reporting A players quit, adding separation and replacement costs plus their unrealized future contributions.
- Several newly hired B/C players quit adding costs from their poor performance, separation, and replacement.
- Extra time and cost attracting new A players.

* "Ramp-Down Period" (when activity is scaled back prior to separation) = 3 months on average prior to separation. *Watson Wyatt. 2005.*

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Separation

I M P A C T

Direct Costs of Separation

- Possible severance (portion of salary and benefits).
- Outplacement services
- Legal expenses particularly if a lawsuit is involved.
- Extra time for HR and other departments.

+

Loss of Knowledge Capital *

- Some loss of company's knowledge from both executive bad hire and possibly other departing team members.
- Some sensitive company information shared with competitors by executive and others who leave.

+

Loss of Employees and Customers

- Several existing and potential employees are recruited away in the future.
- Several existing customers leave with executive while other potential customers never materialize.

+

Disruption to Team and Clients

- Lower productivity of executive's team during separation period.
- Lower productivity of other teams working with executive's group during separation period.
- Disruption and lower service to internal and external clients during separation period.

* "Knowledge Capital" (value of intangible assets) is thoroughly discussed in Baruch Lev's book *Intangibles: Management, Measurement, and Reporting.*

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Reputation

I M P A C T

Initial Marketing of Bad Hire

- PR costs announcing the newly hired executive (who became the bad hire).
- Time and production costs of updating marketing material when this executive was hired.
- Time and travel costs to visit employees, customers, suppliers, and partners to introduce this initial executive.

+

Negative Visibility

- Negative press to current and potential customers, employees, partners, competitors, suppliers, and investors when bad hire departs.
- Negative word of mouth from these groups, including from the bad hire.
- A lasting record of regative commentary in social media (Facebook, Glassdoor, Twitter, blogs) visible to future talent and customers.

+

Trust & Goodwill Impairment*

- Loss of trust in the enterprise and leadership team from inside and outside company affecting sales, share price, and stakeholder advocacy.
- Possible lowering of the company's Goodwill if acquired in the near term, leading to a lower sale price.

+

Effects on Hiring Team

- Some loss of respect toward hiring manager who hired executive, affecting how well others will work with this person.
- Hiring manager loses some confidence, which affects their leadership ability.

* 2015, 2017, and 2108 Edelman Trust Barometer which examines the trends in corporate trust.

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Waste*

I M P A C T

Initial Cost per Hire + **Bad Hire's Compensation** + **Direct Support Spent on Bad Hire** - **Bad Hire's Positive Contributions**

Initial Cost per Hire

- Time and administrative costs of HR and others involved with search.
- Outside services (psychological assessment, background checking, drug testing, legal).
- Travel (candidates, executives).
- Possible signing bonus and relocation.

Bad Hire's Compensation

- Base salary (x) number of years.
- Bonus (signing, possibly some performance) (x) number of years.
- Benefits (x) number of years.
- Stock or stock options realized.
- Other cash allowances (car, country club).

Direct Support Spent on Bad Hire

- Administrative assistant (x) number of years.
- Travel (air, car rental, hotel) & entertainment (meals, gifts).
- Training.
- Office space, furniture, computer, other equipment and services.

Bad Hire's Positive Contributions

- Maintained good financial planning?
- Successfully implemented IT system?
- Secured many small external clients?
- Worked well with 2 departments?
- Timely in all reporting?
- Champion of company's community outreach?

* "Waste" can also be called "Net Contribution" if the number is not negative. This concept is described in the following books listed in the References page: *HR Scorecard, The First 90 Days, and Topgrading.*

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Replacement

I M P A C T

More Expensive Cost per Hire

- Time and administrative costs of HR and others with the replacement search.
- Outside services (psychological assessment, background checking, drug testing, legal, plus executive search).
- Travel (candidates, executives, plus spouse).
- Signing bonus & relocation (more likely than Initial Cost per Hire).

+

Vacancy Period *

- Lower team productivity during vacancy period due to being short handed and leaderless.
- Team member(s) quit from being overworked.
- Lower service to internal and external clients resulting in complaints and lost sales.
- Several missed opportunities.

-

Cash & Benefits Saved

- Base salary (x) number of months without a replacement.
- Benefits (x) number of months without a replacement.
- Other cash allowances not paid (car, country club).
- Travel and entertainment not spent.

+

Ramp-Up Period **

- Time and travel costs to visit customers, employees, suppliers, partners, and investors to introduce replacement executive.
- Lower productivity of new hire until Ramp-Up Period ends.
- Longer sales cycle until Ramp-Up Period ends.
- Several opportunities missed.

* "Vacancy Period" (no one in position) assumed to be 4 months.
** "Ramp-Up Period" (new hire getting up to speed) assumed to be 6 months.

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5 Areas & Impact of a Bad Executive Hire

AREAS		IMPACT						
Performance	=	Bad Decisions regarding Clients	+	Lower Productivity	+	Opportunity Costs	+	Increased Team Turnover Costs
Separation	=	Direct Costs of Separation	+	Loss of Knowledge Capital	+	Loss of Employees and Customers	+	Disruption to Team and Clients
Reputation	=	Initial Marketing of Bad Hire	+	Negative Visibility	+	Trust & Goodwill Impairment	+	Effects on Hiring Team
Waste	=	Initial Cost per Hire	+	Bad Hire's Compensation	+	Direct Support Spent on Bad Hire	-	Bad Hire's Positive Contributions
Replacement	=	More Expensive Cost per Hire	+	Vacancy Period *	-	Cash & Benefits Saved	+	Ramp-Up Period **

Costs of a Bad Executive Hire ranges from 5 to 15 times salary according to research listed in References.
For instance, Dr. Bradford Smart in *Topgrading* and Dr. Michael Watkins in *The First 90 Days* believe 15 times salary is correct.
However, the U.S. Department of Labor Statistics's *The Cost of Mis-hiring* uses 5 times salary.

* Vacancy Period (no one in position) assumed to be 4 months
** Ramp-up Period (new hire getting up to speed) assumed to be 6 months.

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Next Steps

If:

- Your Costs of a Bad Executive Hire are unmeasured, unknown, and unmanaged
- Quantifying the impact of a bad executive hire would lead you to better solutions for this problem

Then:

- Complete the Self-Audit on the next 6 pages which provides a method to define and estimate these costs.
- If you need help with this process, please contact us.

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Costs of a Bad Executive Hire

Performance

Bad Decisions regarding Clients

• Number of internal clients with problems from bad decisions (x) cost per internal client problem.	+	$
• Number of lost external clients (x) current and future profit per lost client.	+	$
• Various negative effects from lost client(s) on other departments.	+	$

Lower Productivity

• Negative effects of executive hiring "B or C" level employees.	+	$
• Negative effects of those B or C employees hiring other B or C employees and driving away "A" level players.	+	$
• Number of existing A players whose productivity was affected by lower morale and incentive (x) effect of each case.	+	$
• Effects of executive's own lower productivity, particularly during their 3 month Ramp-Down Period before separation.	+	$

Opportunity Costs

• Number of programs planned but never implemented such as a cost savings program (x) value of each program.	+	$
• Number of missed new clients (x) future profit from each client.	+	$
• Number of programs delayed such as an employee retention program (x) cost of delay.	+	$
• Reduced collaboration with other departments leading to fewer breakthrough ideas.	+	$

Increased Team Turnover Costs

• Number of direct reporting A players who quit (x) separation & replacement costs plus unrealized future contributions.	+	$
• Number of newly hired B/C players who quit (x) poor performance & separation & replacement costs.	+	$
• Extra time and costs attracting new A players.	+	$

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Costs of a Bad Executive Hire

Separation

Direct Costs of Separation

• Possible severance (portion of salary and benefits).	+	$
• Outplacement services.	+	$
• Legal expenses particularly if a lawsuit is involved.	+	$
• Extra time for HR and other departments.		

Loss of Knowledge Capital

Loss of Knowledge Capital	+	$
• Some loss of company's knowledge from both executive bad hire and possibly other departing team members.	+	$
• Some sensitive company information shared with competitors by separated executive and others who leave.	+	$

Loss of Employees and Customers

• Several existing and potential employees are recruited away in the future.	+	$
• Several existing customers leave with executive while other potential customers never materialize.	+	$

Disruption to Team and Clients

• Lower productivity of executive's team during separation period.	+	$
• Lower productivity of other teams working with executive's group during separation period.	+	$
• Disruption and lower service to internal and external clients during separation period.	+	$

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Costs of a Bad Executive Hire

Reputation

Initial Marketing of Bad Hire

• PR costs announcing the newly hired executive (who became the bad hire).	+	$
• Time and production costs of updating marketing material when this executive was hired.	+	$
• Time and travel costs to visit employees, customers, suppliers, and partners to introduce this executive.	+	$

Negative Visibility

• Bad press to current/potential customers, employees, partners, competitors, suppliers, investors when bad hire exits.	+	$
• Negative word of mouth from these groups, including from the bad hire.	+	$
• A lasting record of regative commentary in social media, job sites, and blogs visible to future talent and customers.	+	$

Trust & Goodwill Impairment

• Loss of trust in company & leadership team both inside/outside affecting sales, share price, stakeholder advocacy.	+	$
• Possible lowering of the company's Goodwill if acquired in the near term, leading to a lower sale price.	+	$

Effects on Hiring Team

• Some loss of respect toward hiring manager who hired executive, affecting how well others will work with this person.	+	$
• Hiring manager loses some confidence, which affects his/her leadership ability.	+	$

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Costs of a Bad Executive Hire

Waste

Initial Cost per Hire

• Time and administrative costs of HR and others involved with search.	+	$
• Outside services (psychological assessment, background checking, drug testing, legal).	+	$
• Travel (candidates, executives).	+	$
• Possible signing bonus and relocation.	+	$

Bad Hire's Compensation

• Base salary (x) number of years.	+	$
• Bonus (signing, possibly some performance) (x) number of years.	+	$
• Benefits (x) number of years.	+	$
• Stock or stock options realized.	+	$
• Other cash allowances (car, country club).	+	$

Direct Support Spent on Bad Hire

• Administrative assistant (x) number of years.	+	$
• Their travel (air, car rental, hotel) & entertainment (meals, gifts).	+	$
• Training.	+	$
• Office space, furniture, computer, other equipment and services.	+	$

Bad Hire's Positive Contributions (You determine)

•	-	$
•	-	$
•	-	$
•	-	$
•	-	$

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Costs of a Bad Executive Hire

Replacement

More Expensive Cost Cost per Hire

• Time and administrative costs of HR and others involved with search.	+	$
• Outside services (psychological assessment, background checking, drug testing, legal, plus executive search).	+	$
• Travel (candidates, executives, plus spouse).	+	$
• Signing bonus & relocation (more likely than Initial Cost per Hire).	+	$
	+	$

Vacancy Period

• Lower team productivity during Vacancy Period due to being short handed and leaderless.	+	$
• Team member(s) who quit from overwork (x) separation & replacement costs plus any unrealized future contributions.	+	$
• Lower service to internal and external clients resulting in complaints and lost sales.	+	$
• Several missed opportunities.	+	$

Cash and Benefits Saved

• Base salary (x) number of months without a replacement.	-	$
• Benefits (x) number of months without a replacement.	-	$
• Other cash allowances not paid (car, country club).	-	$
• Travel and entertainment not spent.	-	$

Ramp-Up Period

• Time and travel to visit customers, employees, suppliers, partners, and investors to introduce replacement executive.	+	$
• Lower productivity of new hire until Ramp-Up Period ends.	+	$
• Longer sales cycle until Ramp-Up Period ends.	+	$
• Several opportunities missed during Ramp-Up Period.	+	$

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Costs of a Bad Executive Hire

Your Total Costs

AREAS	IMPACT							COST
Performance =	Bad Decisions regarding Clients $	+	Lower Productivity $	+	Opportunity Costs $	+	Increased Team Turnover Costs $	$
Separation =	Direct Costs of Separation $	+	Loss of Knowledge Capital $	+	Loss of Employees and Customers $	+	Disruption to Team and Clients $	$
Reputation =	Marketing of Bad Hire $	+	Bad PR $	+	Goodwill Impairment $	+	Effects on Hiring Team $	$
Waste =	Initial Cost per Hire $	+	Bad Hire's Compensation $	+	Direct Support Spent on Bad Hire $	-	Bad Hire's Positive Contributions $	$
Replacement =	More Expensive Cost per Hire $	+	Vacancy Period $	-	Cash & Benefits Saved $	+	Ramp-Up Period $	$

Your Total Cost of a Bad Executive Hire: $

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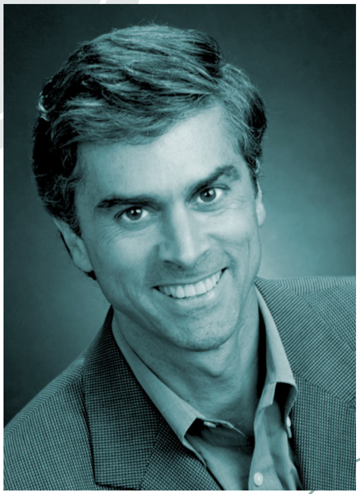
About the Author



Tom Mallory is a Partner of Acadia Associates, an executive search and job transition firm based in Atlanta, GA. He has been conducting executive searches since 1997 for B2B service companies, mostly family or investor owned ones where the CEO is often the Founder. Also, since 1995, he has been coaching executives who are planning for or in a job transition.

Tom started Acadia Associates in 2002 after four months of research with 50 CEOs revealed a different and better approach to executive seach.

Earlier in his career, Tom helped start two technology enabled service companies, served in marketing roles at UPS and Sea-Land Services, and was an Army Captain and paratrooper. Married with three children, he holds an MBA from Harvard and a BA from St. Lawrence University.

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