

> A Guide to Identifying, Assessing & Contracting with Executive Search Firms

Great people are critical to the success of every business.

Hiring them, however, is easier said than done. The best are rare, difficult to find and hard to attract. Competition for them is intense.

When companies need to recruit the best executive talent, they retain an executive search consultant. Executive search consultants identify the best candidates, thoughtfully assess their strengths and weaknesses, and artfully persuade them to consider the client's opportunity. When it is time to make an offer, they shepherd negotiations to a successful conclusion. A well-executed search results in hiring an executive who will significantly increase the value of his new employer.

The Downside: A High Risk of Failure

Unfortunately, executive search often fails to live up to its promise. Overall industry performance is stunningly poor. It is widely acknowledged that only 60% - 65% of searches conducted by the largest search firms result in a hire. With such results, it is no surprise that surveys report customer satisfaction below 50%.

The industry's poor performance is costly for clients. Failure to make a hire, or hiring the wrong person, has consequences that go far beyond executive search fees. A bad hire means wasted time, missed opportunities and damage to the organization.

Clients Share the Blame

Many companies continue to hire non-performing executive search firms. By rewarding failure, clients are complicit in the poor performance of the executive search industry. This is especially true in the case of the large, brand name executive search firms, which for a

variety of reasons (detailed later in this paper) are the worst offenders, but continue to thrive. Clients must demand results if they want change.

Getting Better Results from Executive Search

Companies can start by revamping the way they assess and contract with search firms. Many clients do not understand the executive search business, including the incentives and restrictions that drive its behavior and performance. As a result, they engage in a superficial and arbitrary selection process too often dictated by personal connections and brand recognition, rather than a serious review of executive search firms and their capabilities.

An Overview of the Executive Search Business

The structure and practices of the executive search industry drive the behavior of executive search consultants. Clients who understand these factors have a much better chance of selecting an executive search consultant who will perform well for them.

The Industry

Executive search consulting is big business. According to the Association of Executive Search Consultants, worldwide revenues for the executive search industry were \$10.41B in 2011. The industry is highly fragmented, with a handful of large global players, a few medium-sized firms, and many small firms.

The industry's giants (sometimes referred to as the *Big 5*) are Korn/Ferry International, Heidrick & Struggles International, Spencer Stuart, Russell Reynolds Associates, and Egon Zehnder International. The largest, Korn/Ferry, had revenues of \$776M in its 2011 fiscal year. These firms have hundreds of consultants, operate across many industries, and have a global presence.

On the other extreme are the boutiques. These small companies have one to five consultants, and often specialize in an industry or function. There are almost no barriers to entry in executive search, and many executive search consultants choose to operate their own firms. In fact, it is common for top performers at large search firms to establish their own companies, where they exercise more control over quality and keep more of their billings.

Limits on Growth on Executive Search Firms

Executive search firms do not recruit from their clients. This practice, known as off-limits, came about because clients wanted assurances that executive search firms would not use confidential information to recruit their personnel. The term of off-limits agreements varies, but the norm is two years.

As a practical matter, off-limits guarantees limit the growth of large search firms. The more clients they have, the fewer candidates they can access. Eventually, so many candidates are off-limits that it becomes difficult to deliver results.

In reaction to this problem, most of the Big 5 have begun to diversify beyond executive search into other areas of human resources consulting.

Fees

For decades, fees for executive search were uniform across the industry. The historical norm, which is still prevalent, is that the executive search firm receives one-third of the hired candidate's first-year cash compensation, paid in several installments starting at the commencement of the search.

Recently executive search companies have been under pressure to reduce or restructure their fees. Many firms, including some of the largest, have deviated from the old norms to accommodate their clients.

Off-Limits Practices & Their Implications for Clients

Off-limits commitments bar executive search firms from approaching some candidates. Clients need to understand how off-limits works, and how it affects execution of projects. Off-limits constraints, and clients'

ignorance of their implications, are the single largest contributor to the industry's poor track record.

Search Firms Cannot Approach Candidates Who Work for Clients

The off-limits guarantees described above handicap large search firms. Their long client lists preclude them from accessing many candidates. A firm that is doing business with half of the companies in an industry, for example, is probably unable to recruit roughly half of the employees in that industry.

Search Firms Cannot Approach Candidates Who Are Being Considered by Other Clients

Executive search firms cannot present the same candidate to multiple clients. To do so could result in

Off-limits guarantees handicap large search firms.

clients bidding against each other for the same candidate. Candidates who cannot be approached because they are being considered by other clients are said to be blocked by "in-process off-limits."

In-process off-limits is a serious problem for large firms, which usually have many active searches that are competing with each other for candidates. In combination with their inability to recruit from client companies, in-process off-limits compound the difficulty large firms have delivering results.

Executive Search as Consulting

An effective executive search practitioner is a consultant. He invests time and energy in developing a deep understanding of his client, its business, and the executives who will be involved in the search. Armed with this knowledge, he sells opportunities in a compelling way (thus bringing more candidates to the table), provides insightful assessments of candidates, and

offers helpful counsel when the search hits inevitable bumps in the road. The relationship of trust with the consultant that emerges from this process can be invaluable.

There is a common misperception that the primary value derived from executive search is access to candidates through a consultant's personal contacts. Most executive search professionals have outstanding contacts, but these are less important than ever before because the Internet has made candidate identification a commodity.

Firm Size & Structure Determine Who Works on Projects

Consultants at small executive search firms generally take a hands-on approach and do much of the work themselves, while consultants at large firms usually act as project managers.

The Big 5 and other large executive search firms are structured like other management consulting companies. Consultants focus on booking new projects. Junior associates do most of the project execution, while the consultants manage the client relationship. It is not uncommon for a consultant at a large firm to manage fifteen to twenty assignments at a time.

In contrast, consultants at small firms book and execute search projects. They carry fewer searches than their counterparts at large firms do, usually in the range of three to four at any given time. The hands-on approach of small firms can be advantageous because consultants develop a close relationship with the client. In-depth knowledge of the client's business and personnel enables them to be more effective at attracting and assessing candidates.

Identifying & Evaluating Search Firms

Choosing the right executive search firm for the job is critical. The process is time consuming, but identifying the right firm will pay off in a smoother, faster search, and ultimately in a superior new hire.

Define What You Want

Begin by making a list of the qualities a search consultant will need to be successful with the target assignment. Specifics vary depending on the company and the search, but typically include some or all of the following:

Industry Expertise.

Usually helpful, because it enables a consultant to quickly understand a client's business and present it with fluency to potential candidates.

Access to Candidates.

Consultants must be able to recruit from desired companies.

Geographic Reach.

Consultants must be able to recruit from the client's target geographies. For example, a global search calls for an executive search firm that has global reach.

Functional Expertise.

The consultant should understand the function and any special issues or challenges it might present.

Adequate Time.

It is rare for an executive search consultant to turn down a project. Clients must make sure a consultant can give their project enough time and attention.

Intelligence & Communications Skills.

Essential for any search, because without them a consultant cannot represent the client effectively, or provide trusted counsel.

If more than one person will be involved in selecting the executive search firm, make sure all participants understand the issues and agree on the qualities desired.

Identifying Search Firms

Begin by identifying a number of executive search firms that might be a good fit. Trusted colleagues in the industry may be able to recommend a search firm that meets the necessary criteria. Usually they can also give helpful insights about their experiences with the firm.

If more firms are needed, consult an industry directory. The best is the *Directory of Executive & Professional Recruiters*, published by Kennedy Information. It identifies firms by specialty, size and geography. Further information can be found in the *Resources* section at the end of this paper.

After building a list of potential partners, conduct telephone screenings with the each of the firms.

Determine if they meet the basic criteria, and if they are interested in talking further about the project. Invite the top two or three for an in-person meeting at your company.

Questions to Ask

Face-to-face meetings are an opportunity to learn more about each search firm and the specific consultant who would be responsible for the project. Here are some suggested questions:

Who Will Work on the Search if I Hire Your Firm?

Early on, find out if the consultant at the meeting will work on the search. If the answer is yes, what will his role be? Specifically, will he make phone calls to present the opportunity to potential candidates, do phone and in-person interviews, write candidate assessments, and perform other critical tasks? If the answer is no, find out who will. Form an opinion about the person's ability to convince top candidates to consider the job.

What Have You Done Recently in My Industry?

A consultant needs to understand the client's business well enough to present the opportunity to candidates in a knowledgeable way. Ask the consultant to name specific projects he has worked on in the industry. The consultant's personal experience is what matters, so be careful to distinguish between the consultant's personal experience and that of the firm.

Have You Worked on Searches in This Function?

Ask for specifics on projects for which the consultant was personally responsible. Try to get a sense of the consultant's understanding of the function and any special recruiting challenges.

Do You Have Time to Give My Project the Attention and Focus It Needs?

Ask the consultant who will handle the assignment how many projects he is working on. Executive search consultants seldom turn down a project, even when they are very busy, so it is up to the client to form an opinion on whether a consultant has enough time to focus on a new search.

If I Hire You, What Companies Will You Be Unable to Recruit From?

Understand exactly which companies will be off limits to the search. Search firms, especially the largest ones, are

reluctant to admit off-limits issues. Be prepared to ask about specific companies that may be good sources of candidates, and don't settle for vague assurances.

Are You Doing Any Similar Searches Right Now?

This question is an attempt to figure out if the search firm has other projects that will compete for candidates. It is reasonable to assume that the larger the search firm, the greater the likelihood that the firm will be unable to show you candidates who have already been assigned to other clients. With the largest firms, it is almost a certainty.

In What Percentage of Searches is One of Your Candidates Hired?

If a consultant answers this question by citing the firm's completion rate, ask how it defines a completion and dig into the underlying data. Hiring rates above 90% are usually not credible, simply because some searches are stopped when clients lose funding, suffer a business setback, or change strategies.

How Will You Communicate With Me During the Search?

There should be a plan for regular communication with the client during the search. This could include regular teleconferences, meetings, written status reports, or all of the above. Most consultants will tailor the frequency and type of communications to the client's preferences.

Who Can I Talk to About Your Work?

Obtain names of three clients who can speak to the specific consultant's work. Follow through and ask specific questions about their satisfaction with the search process and the end result. If possible, supplement the consultant's own references with others who can speak about his work.

Who will work on the search if I hire you?

During the discussion, observe the consultant. Does he ask intelligent questions about the company and the

position? Does he listen attentively? Can he talk credibly about the industry? Is he intelligent and articulate? Finally, is he someone with whom those who will manage the search can work effectively?

If the consultant and his firm appear to be a viable option, ask for a written proposal. This should take no more than five business days.

Negotiating the Agreement

Written proposals give clients an opportunity to compare how different firms will approach a search. Proposals also enable clients to compare terms and conditions from multiple firms, which can be helpful in negotiations.

What to Expect in Written Proposals

A written proposal serves two purposes. First, it outlines the search firm's understanding of the client company and the opening, and details how they will approach the project. This information helps the client judge how well the consultant understands the company and its needs as reflected in the specifics of the proposed search.

Second, it serves as a contract and specifies terms and conditions such as fees, payment schedules, expenses, off-limits commitments, and guarantees.

Evaluating the Search Strategy

Proposals should include a clear and concise summary of the position to be filled, candidate specifications, the search strategy (including a partial list of target companies), search firm staffing of the project, and an estimated timeline for achieving key milestones.

The proposal is the search firm's opportunity to put its best foot forward. Look past fancy formatting and focus on content. Look for a thoughtful and well-written presentation that demonstrates the firm has researched your company, listened to you, understands the position's responsibilities, has a clear vision of the experience and personal qualities desired in candidates, and has defined a sensible strategy for getting the job done.

Proposals that are unduly long or padded with boilerplate are a red flag. They often indicate a cookie-cutter approach to clients and search execution that suggests the search is less likely to succeed. Likewise,

proposals that are sloppy, not thoughtful, or otherwise weak demonstrate a lack of attention to detail that suggests the firm will provide equally poor service if hired for the search.

Evaluating Terms & Conditions

Terms and conditions in executive search contracts used to be fairly standard, but that is no longer the case. The most important terms and conditions are described below, with some thoughts on how industry norms are changing. In addition, several abusive practices are identified.

Fee Percentage

The historical norm for search fees is one-third of first year cash compensation. Most search firms still use this figure, but in practice the fee percentage has become negotiable in recent years, as search firms compete for a smaller number of assignments. In some cases, search firms have moved to flat fees so clients know their costs in advance.

Clients should attempt to negotiate the fee, seeking an outcome that is fair to all parties. Keep in mind that a good search firm will invest considerable money and resources in an aggressive, time-consuming search effort. Low price will be an empty victory if the search firm does not have adequate resources to make the project a success.

Fee Basis

If the fee is based on a percentage of first-year compensation, the contract must also define what first-year compensation means. Does it mean base salary, or does it also include target bonus?

When a bonus is guaranteed, search firm and client usually agree to include it in the fee calculation. Opinions diverge when the bonus is not guaranteed. Search firms argue that the bonus should be included because it is an integral part of compensation. Clients correctly point out that the candidate may never earn the money. Both sides have reasonable points of view, and usually it is possible to find a middle ground.

Some search firms argue that the fee basis should also include money paid for relocation assistance. This can add an enormous amount to the fee. Most clients find this practice unreasonable and do not accept it.

Payment Schedules

In the past, fees were always paid in three or four installments over the first ninety days of the search. That is still often the case, but it is no longer universal.

Today many clients negotiate payment schedules that are based on achievement of milestones. There is no standard approach, but a fairly common example is payment of one-third of the fee at the start of the search, one-third when an agreed number of candidates are presented, and one-third on completion.

Billing of Expenses

Nearly all search firms bill clients for expenses related to execution of the assignment, such as travel and meals. Clients who are concerned about expense management can ask the search firm to seek approval before incurring major expenses.

Some executive search firms also charge an “administrative fee” of up to 10% of the search fee. In effect, these search firms are charging clients for their overhead. Although common, many clients find this unreasonable and do not accept it.

Term of the Contract

The majority of search firms will make a written commitment to work until the search is successfully completed. However, some search firms attempt to limit their commitment by fixing an end date to the search (often six months) after which they have no obligation to continue unless the client agrees to pay additional fees. Most clients find these terms unacceptable.

Off-Limits Commitment

Most search firms commit not to recruit from clients for two years from completion of the search. If no hire is made, off-limits still applies and usually begins on the date the search was cancelled.

Some search firms try to narrow their off-limits commitment by making it apply only to a subset of the client, like a division or department. As a general rule,

companies with less than \$1B in revenues should expect their entire company to be made off-limits.

What’s reasonable at larger companies is open to debate. Larger companies should demand, at minimum, that the client division be off-limits.

Guarantee

Search firms guarantee their work. A typical guarantee obligates the search firm to conduct a new search for no fee if a hire leaves within one year. A shorter guarantee, or none at all, is cause for concern.

Conclusion

Without exception, educated clients get better outcomes from executive search. Those who undertake a rigorous assessment of executive search firms and negotiate a fair search agreement have built a foundation that is likely to result in a smooth, painless search and achievement of the ultimate objective: a great new executive who will add value to the company .



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