

Equity Methods Resolves Data Complexities, Performs Rigorous Expense Forecasts For Financial Services Giant and TARP Recipient

- *Global financial services company issuing equity compensation to 10,000 employees*
- *Significant recipient of TARP money creates non-trivial ad hoc forecasting and what-if questions*
- *Considerable exploration of performance-based awards in order to strengthen pay-for-performance*

BACKGROUND AND CONTEXT

Our client is a Fortune 100 financial services firm with a global presence and a recipient of TARP money.

This firm grants a variety of equity compensation awards to over 10,000 employees. Whereas historically this firm granted plain vanilla stock options and restricted stock units, the plan was recently redesigned to include performance-based awards. However, more relevant than the types of awards granted is the firm's significant data management challenges stemming from its use of an antiquated administration system.

In addition to data management issues, this firm has extensive forecasting and planning requirements as a result of being partially government-owned and under considerable scrutiny. The need to constantly forecast expected future compensation cost and perform detailed what-if analyses necessitates a flexible and agile process.

SPECIFIC REPORTING CHALLENGES AND EQUITY METHODS SOLUTION

As noted, this firm relies on an antiquated administration system and is not in a position to transition away from this system. Because Equity Methods is agnostic to the source of administrative data provided, Equity Methods can customize a process to load, validate, and adjust administration data to be suitable for financial reporting purposes.

The first problem resided with this client's administration data is that only outstanding awards can be delivered to Equity Methods. This means that complete transactional exercise and cancellation data are not natural exports from the administration system. Instead, Equity Methods' process involves comparing grant-level outstanding award balances in the current period to outstanding award balances in the prior period. The difference between the two produces grant, exercise, and cancellation records. These automatically produce values that are then reconciled by the client to data stored in their HRIS system.

After creating data records where such data are not seamlessly available in the pre-canned administration system exports, Equity Methods performs a series of data validation tests. For example, grants are occasionally reinstated, which would invalidate the aforementioned process; this requires cross-referencing all historical incremental files to determine whether a given grant ID has ever existed in the past. Equity Methods also generates a variety of control totals and other validation reports for its client to compare to data viewable in its administration system and/or HRIS platform.

Once the client expresses comfort with the data validation reports, Equity Methods proceeds to generate the core financial reporting deliverables¹. The structure of the firm’s new performance-based awards, however, inserts complexity into the calculation process. Specifically, the firm has approximately 100 different award “pools.” A pool refers to a group of awards with identical provisions, where the only difference is the quantity granted. For example, if 10 employees in division A receive the same award structure and 20 employees in division B receive the same award structure, two pools would exist. In this client’s case, 100 different performance multipliers are assessed each reporting period.

The final area of complexity concerns the detailed nature of reports provided. As a TARP recipient, this firm is subject to particularly rigorous planning and forecasting exercises. Difficult questions with rapid requisite turnaround times are the norm. As a professional services firm that serves over 20% of the Fortune 100, Equity Methods is accustomed to demanding deadlines and expectations, although Equity Methods’ experience with its TARP clients sparked a different innovation. Specifically, this experience prompted Equity Methods to evaluate why it couldn’t build sufficiently robust, comprehensive, and understandable reports that would enable its clients to find the answer to 95% of their questions without ever picking up the phone.

The goal was not to discourage clients from calling Equity Methods or force them to get lost in spreadsheets, but rather to empower them to independently answer, ad hoc, all of the foreseeable “what-if” forecasting and planning questions that may potentially arise, and to do so in as little as 10 minutes time. This is achieved by the proactive and frequent delivery of up-to-date reports with deep granularity. This level of detail means:

- Grant-level information;
- Compensation expense shown monthly from the date of grant to vest on each grant; and
- All necessary indicative data shown for each grant.

Imagine, if monthly (past present, and future) expense data are shown for each grant, and each grant can be linked to a cost center, division, P&L line item, country, LOB, etc., then a great deal of ad hoc questions from senior management are rather easily addressed. This is naturally an oversimplification of the process, but describes an important innovation in how clients are served who are subject to rapid turnaround times on unusual, ad hoc requests.

CONCLUDING REMARKS

Equity Methods has replaced a risk-prone Excel process with a fully automated financial reporting process. This client’s risk stemmed primarily from extensive data management challenges, complexity in new award terms, and a constant barrage of what-if questions (from the US federal government and senior management) due to its being a TARP recipient.

¹ The duration of monthly/quarterly financial reporting processes varies. Equity Methods’ clients are all subject to accelerated filing deadlines, and Equity Methods establishes clear accountability with its clients with regard to required report due dates to ensure expectations are met.