

Generating Value with an Outside View

by Matt Slepín

The real estate world has developed a reputation for being insular, as most of the top REIT executives—and a high percentage of board members—have spent their entire careers in real estate. As REITs seek to broaden their investor base, the need to dispel this negative perception has become a top priority. Many real estate companies have begun to look outward and incorporate best practices from corporate America, and hiring talent with perspective from outside of the industry has become an imperative.

While the hiring of a chief executive or chief operating officer from outside the real estate industry is still a rare occurrence, the elevated role of chief human resources officer (CHRO) offers companies a way to incorporate the desired “new blood” in an impactful position that benefits the company’s strategic direction and shareholders alike.

Traditionally, the role of HR director has been a lower-level function dealing with the legal and technical aspects of hiring and personnel issues. An important position, but not exactly one that shareholders would have thought twice about. However, the CHRO is an executive-level position, usually reporting to the CEO or COO, dealing with more strategic and tactical concerns. In most cases, CHROs are being charged with changing the corporate culture from within—something very paramount to shareholders’ concerns.

Companies like Boston Properties, Inc. (NYSE: BXP), AMB Property Corporation (NYSE: AMB), Equity Office Properties Trust (NYSE: EOP) and Equity Residential (NYSE: EQR) have all hired CHROs from other industries with positive results.

Role Playing

The CHROs are, each in their own way, among the most thoughtful and forward-looking people I have spoken with in the REIT world. This contrasted with the “old school model” of the HR director as a legalistic, administrative officer buried several levels down in the organization. In many ways, their out-of-the-industry perspective gives them more credibility to effect change and implement the long-term vision that shareholders like to see.

In a recent Business Week article, the CHRO from Toys “R” Us, Mike D’Ambrose, summed up the increasing importance this role is taking. “We will continue to see greater recognition for the CHRO as the shaper and protector of the company’s culture and values. The CHRO needs to go to work everyday ready to be the voice of what’s right, no matter what. You’re responsible for assisting the CEO in carrying the integrity message into every level of the organization.”

Impact Position

All publicly traded companies, including REITs, are dealing with a myriad of corporate governance issues and the CHROs are in the thick of it. The Sarbanes-Oxley Act of 2002, which established new regulations for public company financial reporting and corporate governance, and other post-Enron initiatives have been on the top of their agenda. The most visible issues include executive level as well as overall compensation policy, board structure and composition, and succession planning.

Compensation, including treatment of options moving forward, is one of the most immediate issues for the CHRO. Several CHROs I spoke with cited the need for increased transparency and fairness in their compensation plans, while others have used the updating of their compensation structure to help move the organization in new directions. John Powers, who joined Equity Residential from the consumer products industry, says, “compensation structure drives behavior and we are using a new performance management program to reward people at all levels who best display the values of the company.”

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CEO succession is clearly a bellwether of change throughout the industry. Succession planning, however, goes beyond merely replacing the CEO. The first requirement is to put succession plans in place for each of the top executives (no matter what their age). But, to build corporate culture as well as enable overall generational succession, several CHROs have put in place formal programs for “knowledge transfer” at their companies.

AMB, for example, has implemented an ongoing brown bag lunch program for the senior executives to meet with groups of senior managers on an ongoing basis to talk about both organizational culture as well as share more direct, experiential real estate knowledge. Boston Properties has a similar program where the “veterans” formally partner up with junior professionals on key projects and then prepare formal case studies to debrief on the project to larger groups.

HR's Role In Growth

Achieving the benefits of size and scale is an imperative of the larger REITs. Douglas Crocker II, recently retired CEO of Equity Residential, has said that, “given our size, we are now essentially an operating company. New deals can only make a difference at the margins. Making a difference on the operational side is the way to achieve our vision.” This sentiment was echoed in my conversations with the CHROs and reflects another way an executive from outside the REIT industry can bring something extra to the table.

Larry Krema, who became CHRO at Equity Office after a career in the retail sector, says, “We must prove that a national platform of this scale can be more effective. Early on, we had been an acquisitions company. Now we must find ways to use the management platform to achieve these goals. HR is called upon as the strategic partner to make this happen. We are looking at corporate America for state of the art practices to best leverage our size and scale.”

As companies grow and seek synergies and efficiencies, they find new balances between centralized and decentralized functions. A key challenge for the corporate group is to find the nuggets in the field by developing mechanisms to identify and implement best practices. Development and implementation of standards is also key, but an interesting question for a company like EQR is how to develop standards that also recognize the varying qualities of properties in its large portfolio.

The REIT Attraction

There are clear reasons why a REIT would want to bring in someone from another industry as CHRO, but why are these executives so eager to join the real estate industry? Values, vision and corporate culture are at the top of the list, according to the CHROs. Nancy Hemmenway left the telecom industry and joined AMB as its CHRO “because of its vision, core values, superb corporate governance, and commitment, especially by the CEO, to create a company of enduring excellence.”

“We want this company to be around in 100 years. I was given the role to make sure we are aligning our actions with what we say we want to do,” Hemmenway says.

One interesting selling point raised by several CHROs was cooperation among the competition. Charlene Rothkopf, who joined AvalonBay from the hospitality business, uses the Human Resources Forum at the National MultiHousing Council as a place where HR directors of the major apartment companies have been able to share best practices and promote increased professionalism in their industry.

Another example of the shared knowledge base came from Adele Schlotzkauer, CHRO of Boston Properties. When we spoke, she had just returned from a meeting of HR execs organized by the Office Technology Consortium. That meeting helped provide her with perspective and an outlet to share information, which she says is critical because “my board always wants to know what the other office REITs are doing”

The anecdotal data seems to show that the CHROs brought in from other industries are making an immediate impact. How will this impact shareholder value? Only time will tell, but for those REITs with an empowered CHRO, it is another step in the right direction. With the transparency issues required by Sarbanes-Oxley and the imperative to take a company beyond a collection of assets to a company built for the long term, this might just be the place within an organization to make that happen.

(Author Credit: Matt Slepian is an executive recruiter based in the San Francisco Bay area.)