

Freiberg, T., Horak, S., & Bonchev, B. (2024). Sustainable Talent Acquisition: Five Best Practices for Referral-based Hiring. Mercer White Papers, Mercer, New York.

## **Sustainable Talent Acquisition: Five Best Practices For Referral-based Hiring**

### **Abstract**

Sustainable talent acquisition (TA) through informal networks, such as employee referrals, is widely regarded as an efficient and effective approach. While this practice can save both time and money, it also has potential downsides. Referral-based hiring can perpetuate homogeneity, reinforce biases, and exacerbate inequality, among other negative consequences. Through interviews with HR leaders and recruiters in the Greater New York City Metro Area, we gain insights into the TA practices of various organizations. We find that many organizations favor some level of referral-based hiring, often using it as a primary recruitment tool. However, others are mindful of the potential for bias and strive to minimize its use. Hiring through employee networks is a delicate and potentially risky TA practice. Based on these interviews, we propose five best practices for a sustainable approach to referral-based hiring.

### **Keywords**

Talent Acquisition; Informal Networks; Best Practices; Sustainability; Referral-Based Hiring; Environmental, Social, and Governance (ESG); Diversity, Equity, Inclusion, and Belonging (DEIB).



Sustainable Talent Acquisition:

# five best practices for referral-based hiring





**Sustainable talent acquisition (TA) emphasizes long-term retention, employee development, and the minimization of turnover. It prioritizes sustainable and socially responsible operations, playing a pivotal role in a company’s Environmental, Social, and Governance (ESG) and Diversity, Equity, Inclusion, and Belonging (DEIB) strategies.**

Consequently, the intensified focus on sustainability in TA today enables organizations to critically assess their future hiring goals and methodologies. Notably, according to a survey conducted by Mercer, of over 400 TA leaders and HR professionals, the number one priority for the near future was to ‘increase the use of inclusive or diverse candidate pools,’ closely followed by ‘improved candidate

sourcing capabilities’ (see Table 1). Both challenges are, in practice, conventionally addressed by an organization’s TA approach, including the utilization of employee referrals, or referral-based hiring. Referrals are widely considered to be an efficient and effective TA sourcing approach, particularly in sustainability regards.

Table 1: Priorities for 2024

## Improving candidate sourcing, especially diverse candidates in financial services and life sciences

	Financial services including fintech	Healthcare Providers	High-tech and other technology	Life sciences, medical devices, pharma and related health industries	Manufacturing	Total
Improved candidate sourcing capabilities	31%	58%	37%	33%	51%	<b>40%</b>
Attracting, nurturing, and converting leads into applicants	29%	29%	22%	21%	29%	<b>26%</b>
Increasing the use of inclusive or diverse candidate pools	66%	19%	48%	58%	37%	<b>43%</b>
Shortened overall recruitment cycle	23%	29%	24%	21%	25%	<b>28%</b>
Enabled right candidate evaluation mix	6%	4%	7%	6%	10%	<b>7%</b>
Enabled better data management and reporting	66%	19%	48%	58%	37%	<b>43%</b>
Cost containment or cost savings	23%	29%	24%	21%	25%	<b>28%</b>
Facilitated unbiased (data-based) hiring	29%	29%	22%	21%	29%	<b>26%</b>
Improved company reputation and/or Employee Value Proposition via social media and/or corporate branding	66%	19%	48%	58%	37%	<b>43%</b>
Create an irresistible career page	23%	29%	24%	21%	25%	<b>28%</b>
Build a better new hire onboarding experience	6%	4%	7%	6%	10%	<b>7%</b>
Create a seamless experience for our candidate	66%	19%	48%	58%	37%	<b>43%</b>
Create seamless experience for our recruiters	23%	29%	24%	21%	25%	<b>28%</b>
Create a positive experience for our hiring managers	66%	19%	48%	58%	37%	<b>43%</b>

Source: 2023 US State of Talent Acquisition, August 2023.

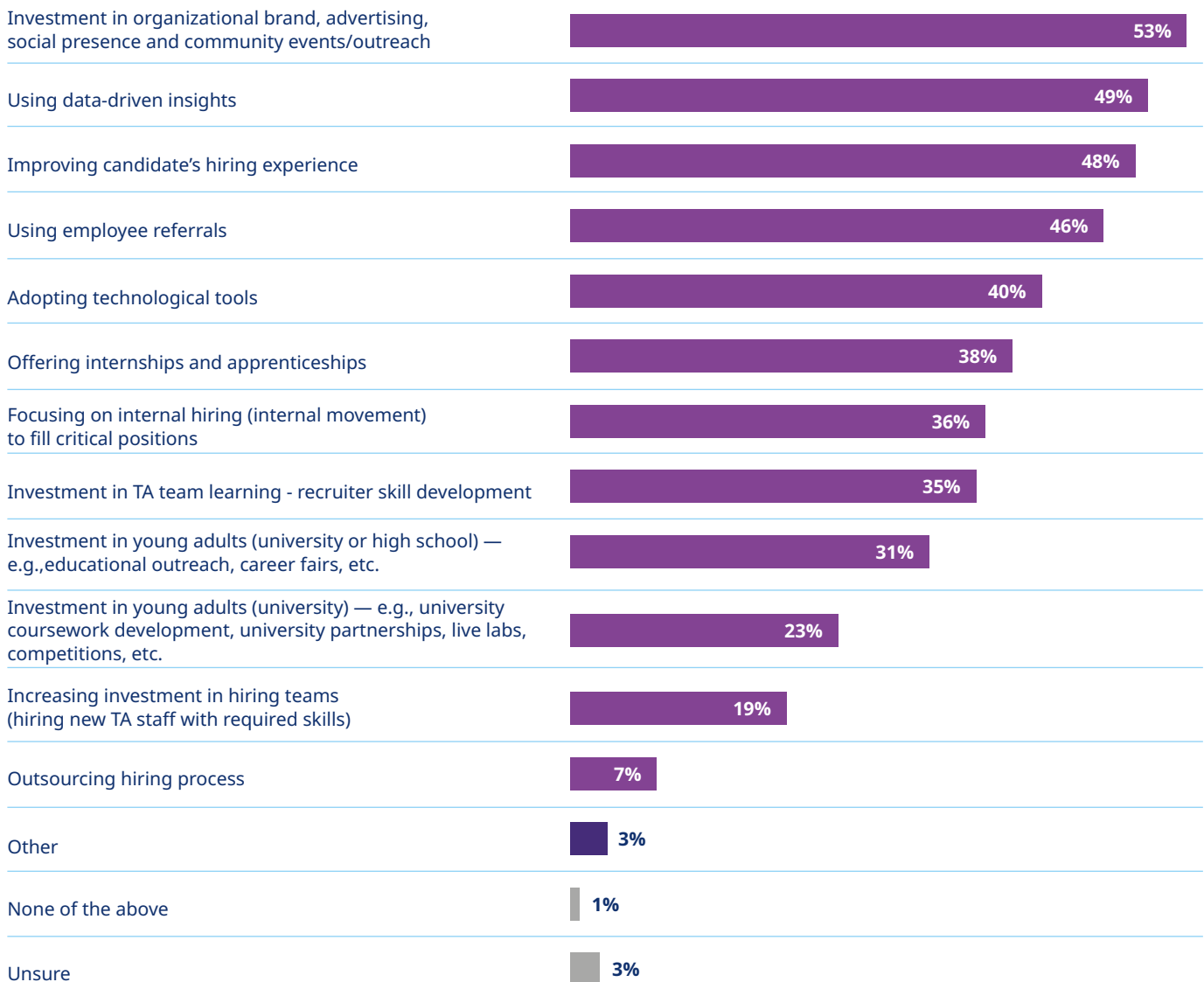
Referral-based hiring is a popular TA practice in today's job market, primarily because it can save businesses time and money when selecting and recruiting new staff. In the same survey, utilizing employee referrals was named among the top 5 solutions to overcome future hiring challenges (see Figure 1).

However, while HR professionals often point out the advantages of referrals, these practices can have

downsides. Specifically, referrals can perpetuate homogeneity, amplify biases, and exacerbate inequality, among other negative consequences. Such drawbacks can undermine a company's DEIB efforts as well as its TA-related sustainability initiatives aimed at improving ESG performance. Both DEIB and ESG are increasingly important pillars of corporate governance today and as such, a central principle in an organization's approach to TA.

**Fig. 1: Solutions for Hiring Challenges**

## How did you overcome (or plan to overcome) the hiring challenges you face?



If not properly controlled referral-based hiring can potentially have contradictory effects on the principles of ESG as well as DEIB. At the same time, though, it can also yield positive and contributory outcomes. To raise awareness about the detrimental tendencies of referral-based hiring, we will discuss its downsides and upsides in TA. Furthermore, to gain a more nuanced understanding of the impact of referrals in the context of a sustainable TA strategy, we conducted interviews and consulted recruiters and HR leaders in the greater New York City area. Based on these discussions, we have developed five best practices for sustainable TA in relation to referrals. These recommendations aim to make the hiring process more effective, sustainable, and equitable.



## The Bright Side of Employee Referrals

It has been long established that one's personal networks are a vital source of getting a job. Personal networks consist of family members, friends and acquaintances including colleagues at the workplace or from former jobs.<sup>1</sup> Hence, since employees usually maintain social connections outside of the workplace, recruiters may utilize networks to fill open positions. Such relationships assist many hiring managers in recruitment processes as it decreases search time and costs for qualified candidates.

Referrals can decrease search costs within the TA process, minimizing overall costs for recruitment. Specifically, referrals minimize costs associated with onboarding a new employee. For example, while referred employees earn higher wages on average, they also have high productivity which decreases monitoring costs and quit rates, supporting sustainability.<sup>2</sup>

There are additional benefits beyond cost reduction when hiring through referrals, particularly in terms of referral value and relational value. Referral value refers to situations in which the hiring manager is familiar with the abilities of network members and can screen these individuals as being above average. On the other hand, relational value is the nearly altruistic

incentive for referred employees to perform better for their network, as opposed to when they work with strangers.<sup>3</sup> When informal networks are used in the TA process, companies leverage social or emotional connections within networks to form implicit contracts between referred employees and their sponsors, often resulting in increased profits for the business and longer tenured employees.<sup>4</sup> Further, smaller firms are more likely to use referrals, in addition to a higher probability of using less formal search processes.<sup>5</sup> As such, the value of employee referrals is undeniable as a common practice in TA, which explains its popularity. Nevertheless, employee referrals do not fully alleviate the risk associated with a new hire and can jeopardize a sustainable TA strategy if the dark sides of employee referrals are ignored.

<sup>1</sup> Granovetter, 2018.

<sup>2</sup> Heath, 2018; Kugler, 2003.

<sup>3</sup> Chandrasekhar et al., 2020.

<sup>4</sup> Heath, 2018; Loury, 2006.

<sup>5</sup> Rebien et al., 2020.

## The Dark Side of Employee Referrals

While personal networks provide ample reason to use referral-based hiring, recruiting within one's network may promote homogeneity across a workforce, perpetuating inherent biases at a company. Specifically, personal networks are found to trend towards gender and racial bias.<sup>6</sup> An individual's network tends to include people from the same ethnic group, race, or social class, who also may know each other.

The differences in informal networks across individuals in a labor market may lead to a disparate distribution of information about jobs, and therefore workforces denoted by similar types of people. It's equally important to investigate hiring discrepancies between different types of firms. One experimental study revealed the prevalence of discrimination when using referrals, where discrimination is observed as the likelihood of hiring employees from a single group type (i.e. gender, university major).<sup>7</sup> Specifically, demand for so-called high-quality workers resulted in increased discrimination, as did the presence of employee referrals.

It is important to note that the discriminatory use of referral-based hiring in TA can be a potential contributor to wage gaps across demographic groups such as gender or race. Research shows that in the United States, there is evidence to suggest minority groups experience significant barriers in the employment process versus the majority group.<sup>8</sup> Further, as the case of Brazil indicates, referral hiring processes can exacerbate racial disparities in labor market outcomes such as wages or employment.<sup>9</sup> The implications of referral-based hiring extend past the hiring process and into the organizational structure of the company, where homogeneity of ideas may limit productivity and other business outcomes.<sup>10</sup>

<sup>6</sup> Tassier and Menczer, 2008.

<sup>7</sup> Takács et al., 2018.

<sup>8</sup> Pedulla and Pager, 2019.

<sup>9</sup> Miller and Schmutte, 2021.

<sup>10</sup> Huning et al., 2015.





## What HR Leaders and Recruiters Think About Referral-based Hiring

Through interviews with HR leaders and recruiters in the greater New York City Metro Area, we find that although referral hiring is a common and heavily utilized practice, the perceived usefulness of referrals varies in the type of position — references seem to be more successful in specialized or niche jobs or industries, and for higher-level management positions. Also, referrals are used more for ad hoc hiring demands. Within our interviews, we discover that many organizations are in favor of some level of referral-based hiring, and many utilize it as their dominant recruitment tool. Others, on the contrary, recognize the potential for bias and try to minimize its usage.

Overall, the picture continues to be heterogeneity. Some organizations, aware of the potentially detrimental aspects of referrals, have formal anti-nepotism policies in place to curtail referrer-bias. Other companies have no formal policy or guidelines for referral-based hiring within their TA strategy and rely heavily on the personal networks of current employees. We also find easily accessible tools such as LinkedIn are increasingly utilized resources when used in conjunction with formalized employee referral programs. Further, we find preliminary evidence to suggest that incentives tied to specialized referral programs (i.e., referral bonuses) are minimally effective —

the fact that an incentive exists is more powerful than the magnitude of that incentive.<sup>11</sup> Also, to be sustainable, a responsible referral-based hiring strategy must look beyond hiring and into retention strategies. For example, onboarding processes can include proactively connecting new employees to internal networks, which helps to reduce employee turnover.

**In the following, based on the interviews with recruiters and HR leaders from a variety of industries, we suggest five best practices for a sustainable referral-based hiring approach.**

<sup>11</sup> The result echoes the diminishing effectiveness of referral bonuses over time (Friebel et al., 2023).



## Sustainable Referral-based Hiring:

# Five best practices



### Best Practice 1:

## Develop a Referral-based Hiring Policy

Acknowledging the beneficial aspects of referral-based hiring, companies should consider formalizing the use of referrals, with the goal of minimizing favoritism and preventing a uniform workforce. It's important that such a policy should consider DEIB targets. An efficient way to develop, implement and monitor this policy would

be under the guidance of a Chief Equity Officer, who should ensure that the policy is not just implemented, but also followed. Adopting such an approach could help companies create a more inclusive working environment and diverse teams, which is beneficial not just for the employees, but for the company.



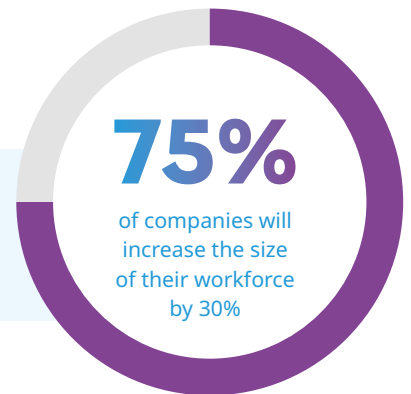
### Best Practice 2:

## Define a Post-hiring Process

**Mercer's survey shows that nearly 75% of companies planning to hire will increase the size of their workforce by up to 30% of their current headcount.**

For companies engaged in large hiring initiatives, retention must be seen as a part of the process. The post-hiring phase is crucial, carrying with it the power to significantly bolster employee retention and satisfaction. Workforce cohesion can be disrupted due to divisions emerging from the ways in which employees have landed their jobs — some through personal connections, others through traditional recruitment processes. For those belonging to the latter group, it is not just important, but vital, to create an onboarding process

that does more than just acquaint them with the company's operations. A post-hiring strategy should involve proactive measures to integrate new employees into the company's informal networks, such as linking employees with Employee Resource Groups (ERGs).<sup>12</sup> This approach has the potential to significantly enhance retention rates and strengthen feelings of belonging, which has positive ripple effects for the company.



<sup>12</sup> Employee Resource Groups (ERGs), also known as affinity groups or business network groups, are voluntary, employee-led groups within an organization that aim to foster a diverse, inclusive workplace.



### Best Practice 3:

## Referrer Incentive Policy

While incentives can be a powerful tool for motivation across functions, it is essential for companies to rethink the tradition of offering cash bonuses to employees who successfully recommend a new hire. We recognize such financial rewards can stimulate the referral process, but alternatively, more innovative rewards can create a win-win situation that benefits both the employee and the broader organization. For example, one seemingly effective and forward-thinking approach is to reward successful referrers with donations to a charity of their choice, made in their name. The method not only aligns with corporate social responsibility initiatives but also fosters a culture of giving and community engagement within the organization. In terms of benefits, as much as 80 percent of

companies in the State of TA 2023 survey report the use of fringe benefits and flexible working arrangements as successful non-financial compensation schemes for new employees.

We had the opportunity to interview a company that has successfully implemented the charitable donation approach. The company representative indicated that the charity donation incentive not only increased employee participation in the referral program but also boosted morale, fostered a sense of purpose, and positively impacted their brand image. Such innovative reward systems can, therefore, enhance referral-based hiring, simultaneously reinforcing a company's values and contributing to wider societal good.



### Best Practice 4:

## Fostering a Culture That Encourages Meritocracy Rather Than Favoritism

For other than family businesses, firms must rigorously contemplate the implications of hiring employees' spouses and close relatives to steer clear of potential nepotism.<sup>13</sup> A sensitive and thoughtful approach is necessary when making such decisions, considering both the professional qualifications of the potential hire and the potential social impact within the organization. Moreover, it is

essential for companies to guard against the emergence of an unhealthy culture of favor exchange. When employees are hired through referrals, there could be a tendency for them to feel indebted to their referrer, creating a possible imbalance in professional relationships and the potential for bias, in addition to resentment from other employees.

<sup>13</sup> Minbaeva et al., 2023.



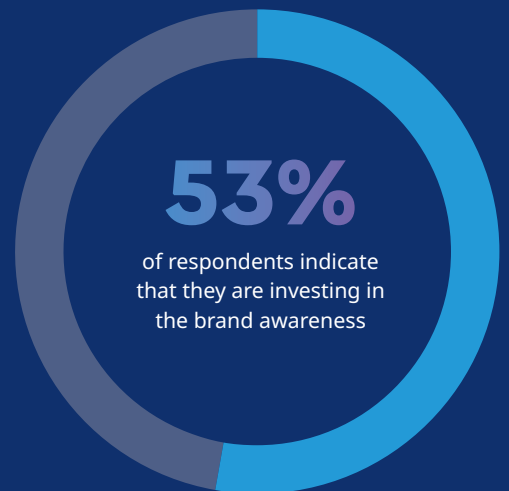
**Best Practice 5:**

## **Increase Transparency — Involve Multiple Parties in the Hiring Process**

While the hiring manager is often the best judge of the skills and experience required for a particular job, if we want to emphasize company-related goals of DEIB and a cohesive workforce, involving other parts of the business in resume reviews or interviews can strengthen the internal community within an organization. It can contribute to more transparent recruitment and selection decisions and thus increase objectivity. For example, in one of our interviews, the company representative indicated that a recruitment team consults with the hiring managers and provides coaching to new hires and their teams on successful employee integration, which also ties back to the main company values and mission. In terms of viewing sustainable TA as a component of business strategy, Mercer's survey data reveal there is room for improvement for many organizations.

**Currently, a bit more than half (56%) of survey respondents report placing a high priority on aligning TA goals with overall business strategy, with again a half (53%) indicating that they are investing in the brand awareness, social presence, and community outreach of the company to help attract talent.**

When a new hire has already interacted with several people from different parts of the business, a community-centric onboarding process is easier to attain. Furthermore, collecting multiple insights also involves multiple recruitment channels including LinkedIn. Most of our interviews indicated LinkedIn continues to develop increasingly heavily utilized by today's recruiters and will most likely continue to do so. When companies keep an open mind as to how potential employees find job openings, they will be more successful.



# Concluding Remarks

TA has transformed from a reactive to a proactive function, shifting from mere recruiting to strategic business alignment. It's no longer solely about filling roles but building a targeted and skilled workforce that will transform organizational capabilities. Sustainably built workforces can deliver future innovation and anticipate customer value while becoming a self-reliant skills organization.

Moving forward towards sustainable TA, it is essential to train and inform recruiters and employees about guidelines surrounding informal networks, ensuring all parties understand that professional advancement is based on their skills, contributions, and performance, rather than personal connections or perceived debts. By implementing such practices, organizations can leverage the benefits of referral-based hiring while minimizing potential drawbacks.



This research was a collaboration between St. John's University of New York and Mercer (US) LLC.

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