

Human Resources Professionals Association of Niagara

The Drive for Strategic Rewards



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Strategic Context

Pay plans that

- reinforce key organizational strategies and values
- motivate employees to maximum performance
- appropriately recognize and reward contributions to the success of the organization

...can help your organization maximize the return on your investment in people



Variable Pay ... The Compensation Linkage

- Employee remuneration represents a major expenditure, if not the largest expense, for most employers.
- An underlying assumption is that variable pay is simply another form of remuneration - another “cost of doing business”.
- However, variable pay programs can be **much more** when you consider they enable real change to occur, and can influence organizational performance and growth

The New Employment Deal

- Just as the nature of business is changing, so too is the unwritten contract that forms the basis of the employment relationship

Old Deal

“A fair day’s pay for a fair day’s work”

Performance equals ...

- effort

New Deal

“A fair exchange”

Performance equals ...

- contribution to organization success (results) **and**
- personal development (skills and knowledge)



Variable Pay Defined

- Any form of compensation that rises and falls in value with organization or team or individual performance
- Common types of cash variable compensation:
 - Incentive Plans
 - Short term / annual
 - Long term
 - Discretionary / Bonus Plans
 - Profit Sharing Plans
 - Sales Compensation Plans
 - Project Incentives



The Case for Variable Pay

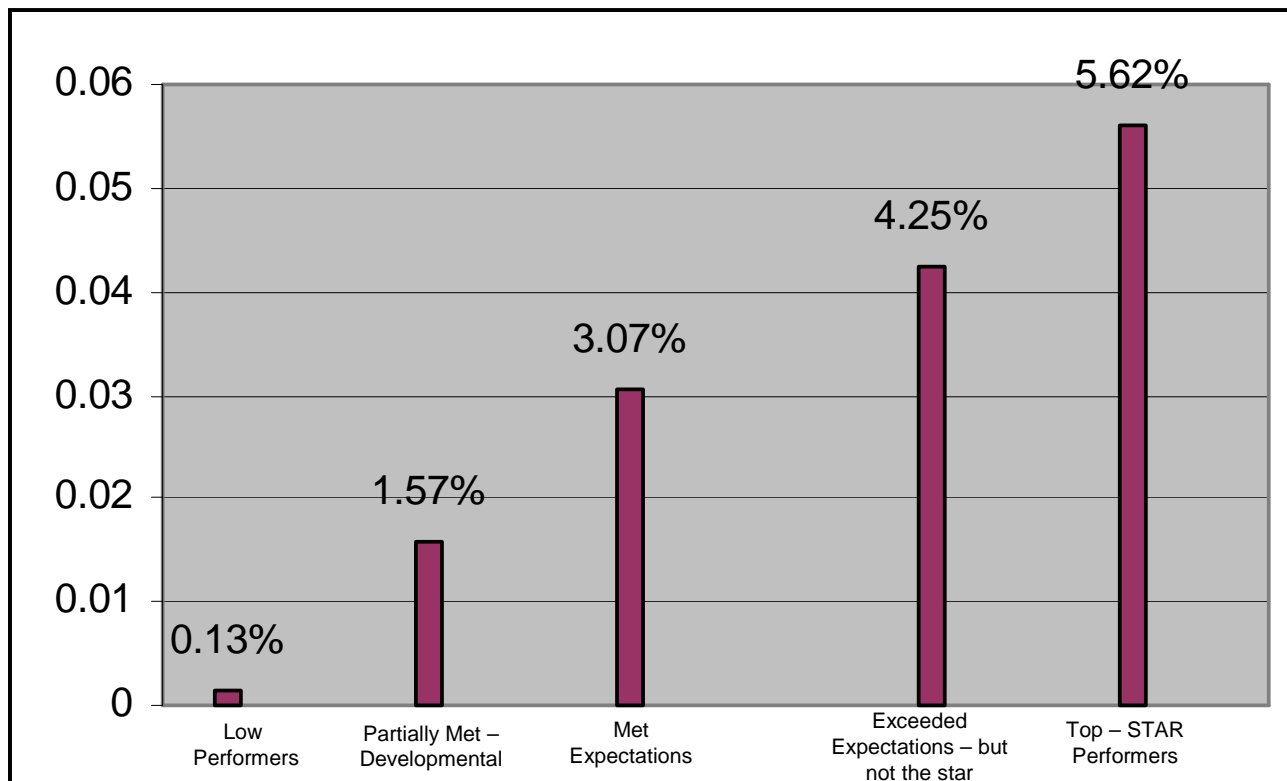
- Traditional salary increase programs are lacking
 - Small budgets
 - Not enough differentiation upside to reward top performers
 - Broadly perceived as an entitlement but views are changing



Merit Pay

- 73% of survey respondents indicated that they pay for performance.

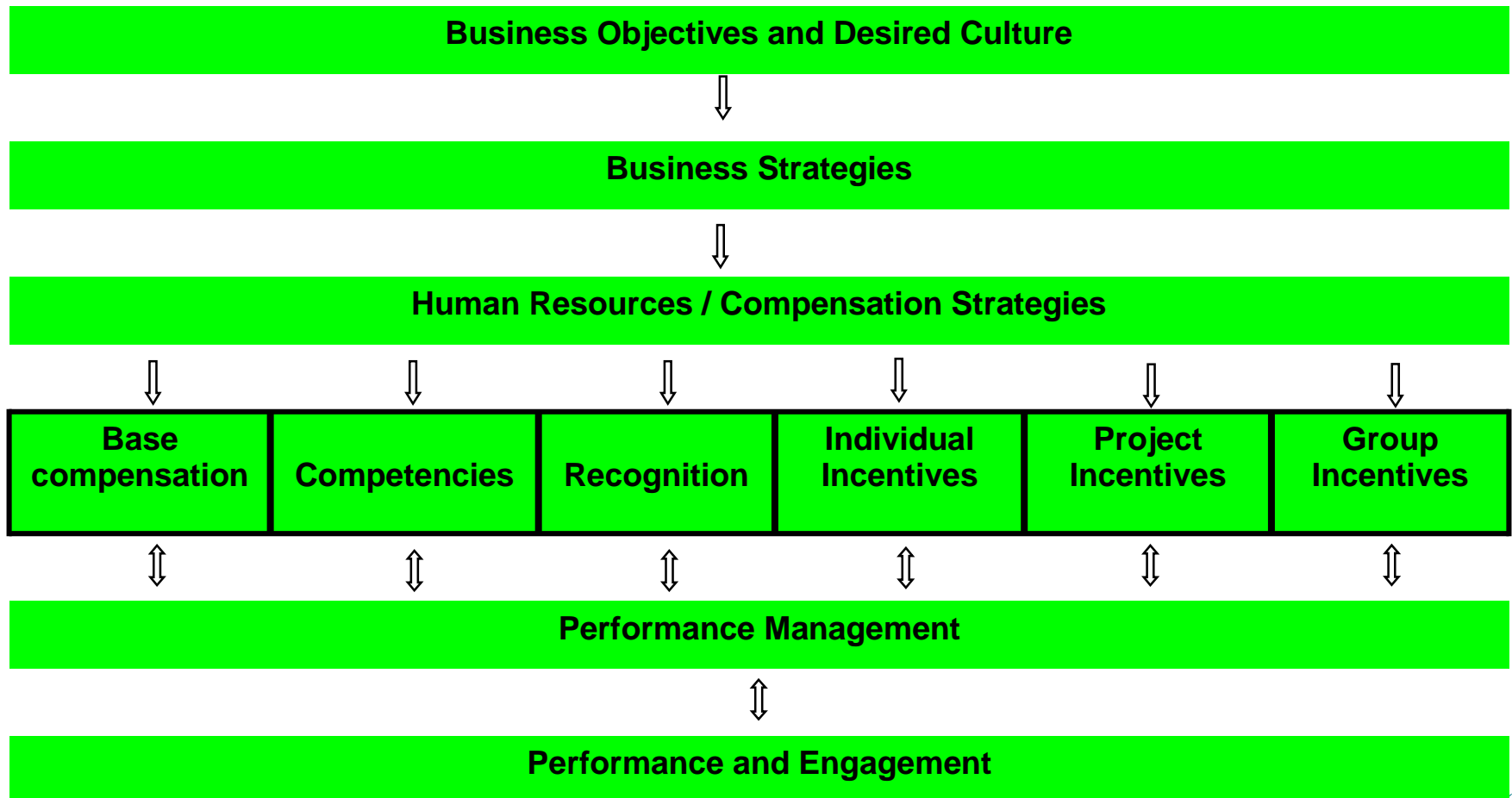
Average Merit Pay Increases – by performance rating



The Case for Variable Pay

- **Demographic Changes**
 - Employment Market
 - Shortage of employees
 - Harder to attract and retain
 - Organizational
 - Impact of Mergers/Acquisitions - merging different practices
- **Market Pressure - Institutional Investors**
 - Looking for stronger link between compensation and organizational performance (e.g. stock performance, total shareholder return)

Strategic Rewards Model



Trends In Variable Pay

- 89% of respondents to Watson Wyatt's annual survey of compensation trends indicated they have some form of incentive plan in place for at least one employee group.
- 20% of respondents who have a plan are considering and/or are in the process of making changes to their plan
 - Tying incentive plans to performance and performance management systems
 - Changing the weighting of performance factors (i.e., between corporate and individual performance)
 - Aligning incentive programs to market
 - Stronger alignment to strategic goals (i.e., balanced scorecard)
 - Adjusting bonus target levels (both increasing and decreasing % targets)
 - Examining eligibility for participation, adding or restricting

Trends In Variable Pay

- use of multiple performance measures
 - financial **and** non-financial measures
 - balance between “*lag*” measures (what has been done, e.g. financial results) and “*lead*” measures (drivers of future performance, e.g. customer service)
- evolution to more of a “risk/reward” culture
 - increasing emphasis on pay tied to results (vs. guaranteed pay)
 - total rewards package more balanced (base and variable)
 - willing to pay for increased return to shareholder
 - less willing to tolerate (or pay for) poor performance
- extension of variable pay further down into the organization
 - not just for executives anymore

Readiness Checklist

Is your organization ready for variable pay ?

Business readiness:

- | | | |
|--|--------------------------|------------|
| Has your organization articulated its vision/mission ? | <input type="checkbox"/> | <u>yes</u> |
| Are key business strategies and goals defined ? | <input type="checkbox"/> | |
| Are key business drivers identified and understood ? | <input type="checkbox"/> | |

Cultural readiness:

- | | | |
|--|--------------------------|--|
| Do you consider your “people strategy” a competitive advantage ? | <input type="checkbox"/> | |
| Is your base compensation program competitively positioned ? | <input type="checkbox"/> | |
| Are your reward plans linked to business strategy ? | <input type="checkbox"/> | |
| Do you currently link individual performance to pay ? | <input type="checkbox"/> | |
| Are you prepared to share financial / operational results with employees ? | <input type="checkbox"/> | |

Operational readiness:

- | | | |
|---|--------------------------|--|
| Do employees understand your business model and how they contribute to success ? | <input type="checkbox"/> | |
| Do you have the ability to measure (and report) on the key metrics, key drivers ? | <input type="checkbox"/> | |



Design Process

Discover

Assess Current Plan

- perceived strengths
- perceived weaknesses

Identify Desired State

- what to recognize/reward
- what are drivers of organization success

Best Practices



Mandate/direction for change

- objectives for plan (why)
- principles for design

Invent

Plan Design

- eligibility/participation
- measures
- risk/rewards
- administration

Test/Model and Refine

Deliver

Implementation

- Program tools
- Communications
- Employee Education
- Guidelines (policy and administration)

Program Maintenance

Program Review

Best Practices In Variable Pay

- Align with organizational strategy:
 - vision/mission, values, (desired) culture
 - key objectives / goals
 - reinforce organizational values and culture
 - consistent with messages
 - maintain “line of sight”
- Relevant measures:
 - drivers of success
 - balance organizational, unit and individual performance
 - measure results that participants can affect
- Ensure fair processes for setting goals and measuring performance:
 - fair and reasonable individual performance objectives/goals
 - fair and consistent performance assessment/evaluation and rating
 - consistent application
 - *perception* of fairness (as important as reality)

Best Practices In Variable Pay

- Reward desired behaviour
 - *what gets rewarded, gets done*
- Keep it simple !
 - easy to understand - *what is not understood cannot motivate*
 - easy to administer
- Communicate, Communicate, Communicate
 - intent / objectives of plan
 - drivers of success
 - how the plan works (measurements, timing, pay opportunities)
 - expectations of employees
 - specific goals
 - values
 - timing - of measurement, of payment
 - progress towards goals - throughout the year

Conclusion

- When effectively designed and implemented, a variable pay program is a valuable lever:
 - to reinforce desired behaviours
 - to motivate performance and commitment; and
 - to help attract and retain quality employees
- The end results:
 - a more focused and productive workforce
 - a positive contribution to the bottom line