



Strategies for Implementing, Evaluating and Communicating Compensation Programs

MACA Breakfast Briefing

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TOWERS WATSON 

Overview

- Impact of the recession
- Strategies to evaluate current programs
- Typical steps in compensation redesign project
- Developing supporting communication strategies for successful implementation

Impact of the Recession

The impact of the recession has been widespread and likely to continue



U.S. Job Satisfaction at Lowest Level in Two Decades

Jan. 5, 2010

THE WALL STREET JOURNAL.

WSJ.com

JANUARY 9, 2010

Wages Still Under Pressure

Rising Tide of Unemployed Lets Employers Keep Lid on Pay Amid Productivity Gains

THE WALL STREET JOURNAL.

WSJ.com

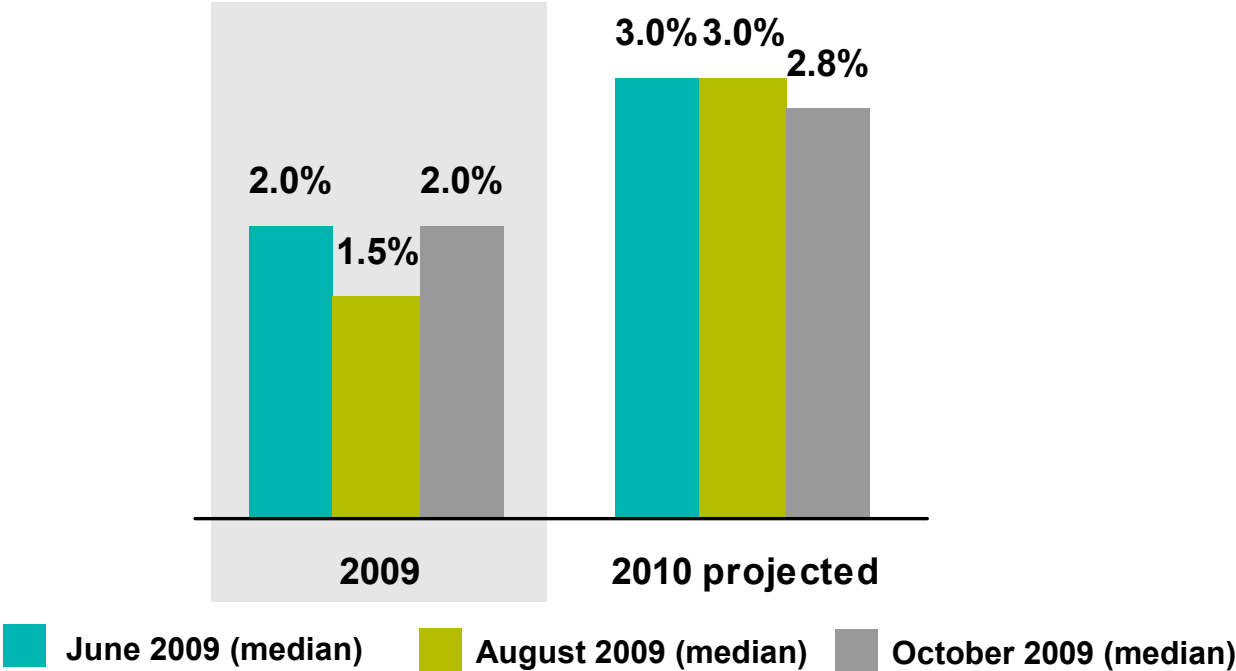
JANUARY 11, 2010

Economy Still Bleeding Jobs



Merit budgets remain low for 2009 but are expected to have some rebound in 2010

In October, 40% reported a 0% increase for 2009, and 10% reported a 0% increase for 2010. The median merit increase of those who did give raises was 3.0.



* As reported in the Effect of the Economic Crisis on HR Programs – Update: October 2009

Recession has reduced funding for annual incentive plans for broad-based employees

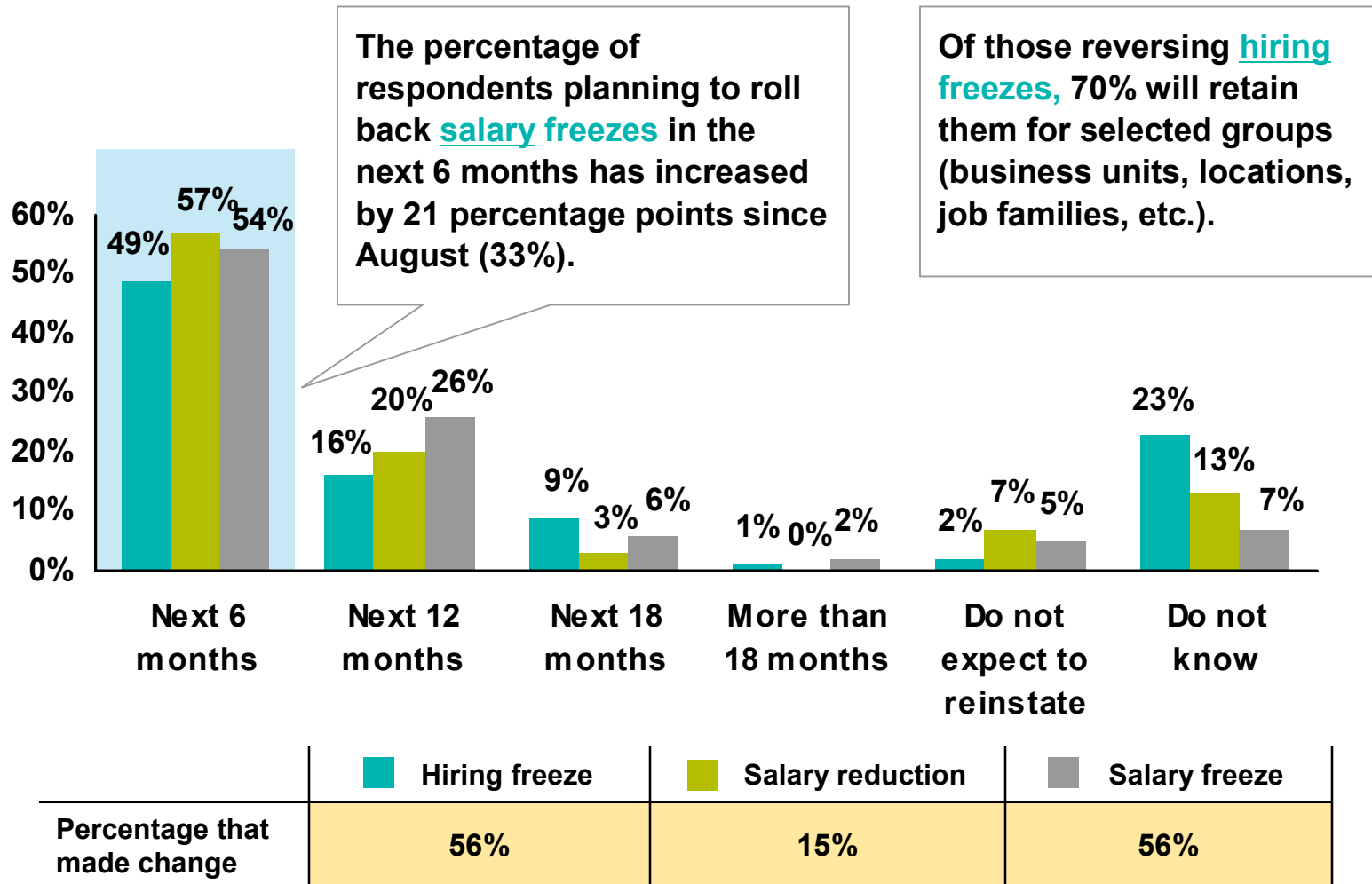
STI funding down over the past 2 years

STI funding levels down from 99% of target in 2007

	Funded last year	Expect to fund this year
Median STI funding	79%	79%
Mean STI funding	71%	68%

** As reported in the Effect of the Economic Crisis on HR Programs – Update: October 2009*

Most companies plan to reverse salary freezes, hiring freezes and salary reductions over the next 12 months



* As reported in the *Effect of the Economic Crisis on HR Programs – Update: October 2009*

Strategies to Evaluate Current Programs

Strategies to evaluate current compensation programs

- Define compensation mission/vision
 - Competitive View
 - Leadership View
 - Employee View
 - Business Objectives
- What's changed?
 - Increase Pay for Performance
 - Drive employee engagement and organization performance
 - Need to create more structured approach to compensation
 - Support M&A activities
 - Support containing/tracking compensation costs
 - Need to create consistent compensation processes
 - Support management of broader geographic operations
- Build the business case for compensation changes

Exercise – define mission/vision

Competitive View	Leadership View	Employee View	Business Objectives
<ul style="list-style-type: none"> • How externally competitive is: <ul style="list-style-type: none"> • Base Pay • STI • LTI • How equitable is: <ul style="list-style-type: none"> • Base Pay • STI • LTI 	<ul style="list-style-type: none"> • What works well with the current compensation system? • What is lacking in the current compensation or causes roadblocks to success? • Identify where compensation is critical in achieving business objectives. 	<ul style="list-style-type: none"> • What is the employee perception of: <ul style="list-style-type: none"> • Base Pay • STI • LTI • What pay components are most/least valued? 	<ul style="list-style-type: none"> • What are the current short term objectives? • What are the long term objectives?

Typical Steps in Compensation Redesign Project

Typical steps in compensation redesign project

- Conduct Gap analysis on current state versus future state to identify action steps
- Prioritize action steps based on mission/vision
 - Base Pay System Redesign
 - STI Redesign

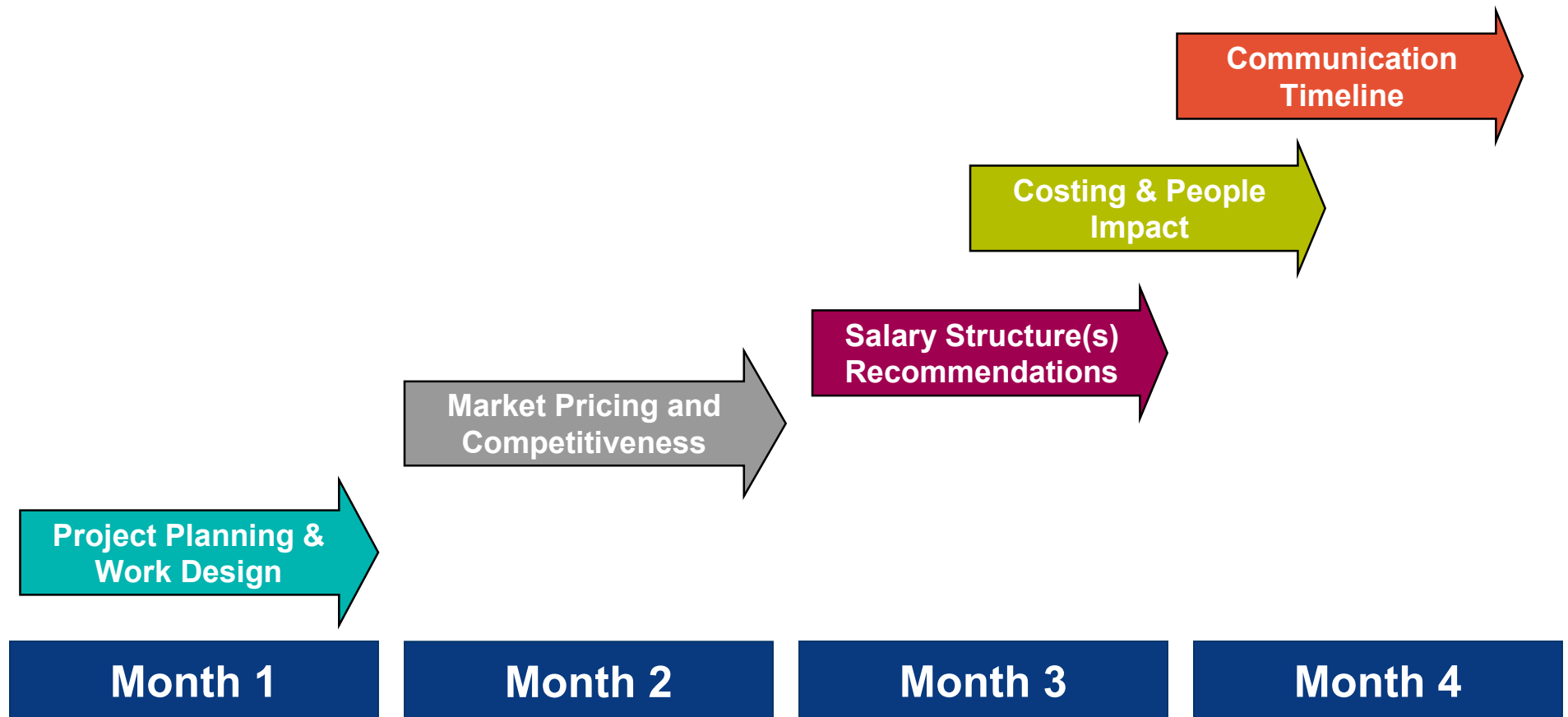
Typical Steps in Compensation Redesign Project

Base Pay System Redesign

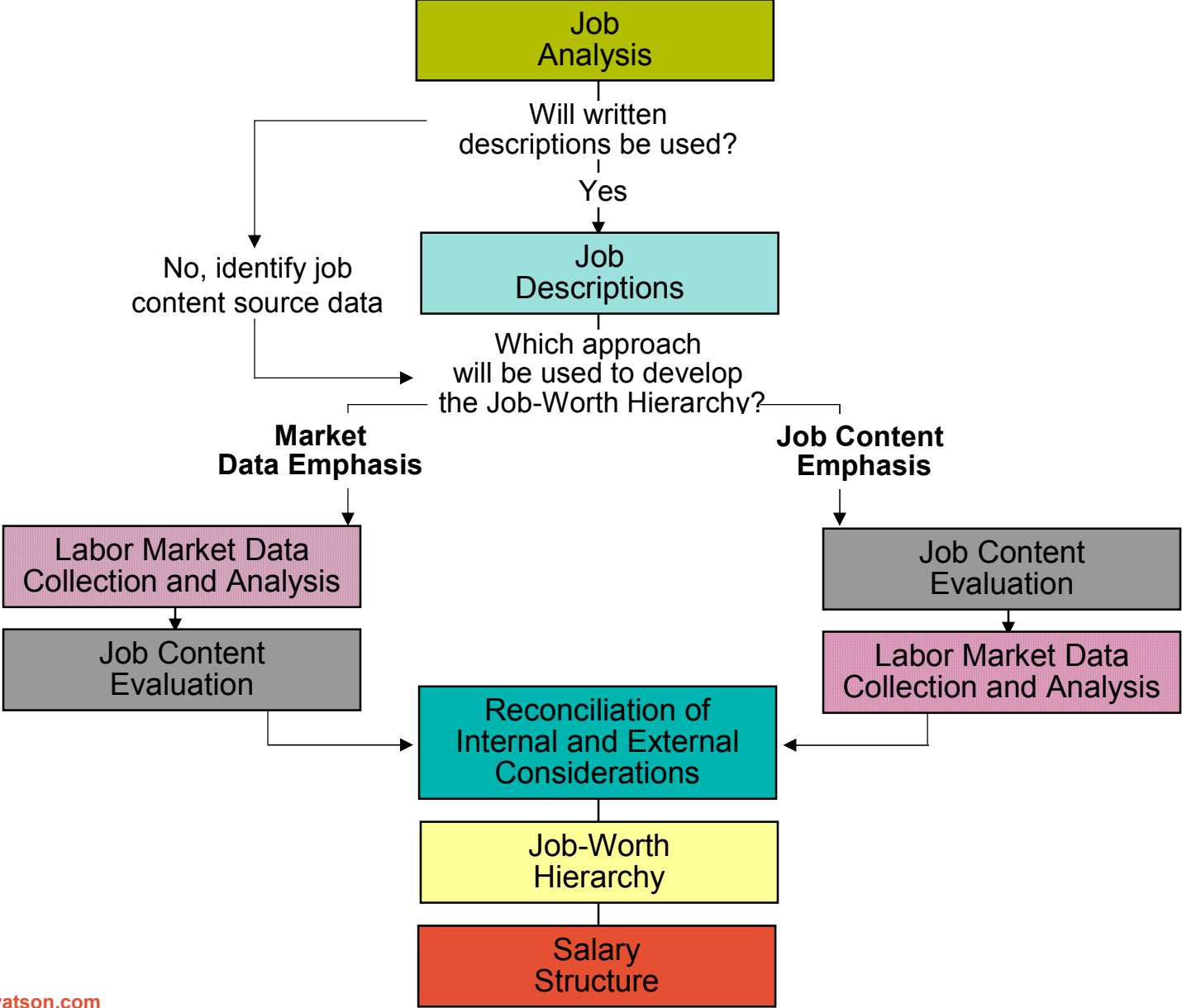
Sample project timeline – full redesign



Sample project timeline – update to current system



Market-based vs. job content evaluation



Market-based approach

- Step One: Analyze and document job content – job descriptions
- Step Two: Collect market data on at least 50% of jobs to be placed in the hierarchy
- Step Three: Develop structure of midpoints based on market data
- Step Four: Assign priced jobs to the structure based on market-to-midpoint comparisons
- Step Five: Slot remaining jobs into the structure based on whole-job comparisons or job classification

Job content approach

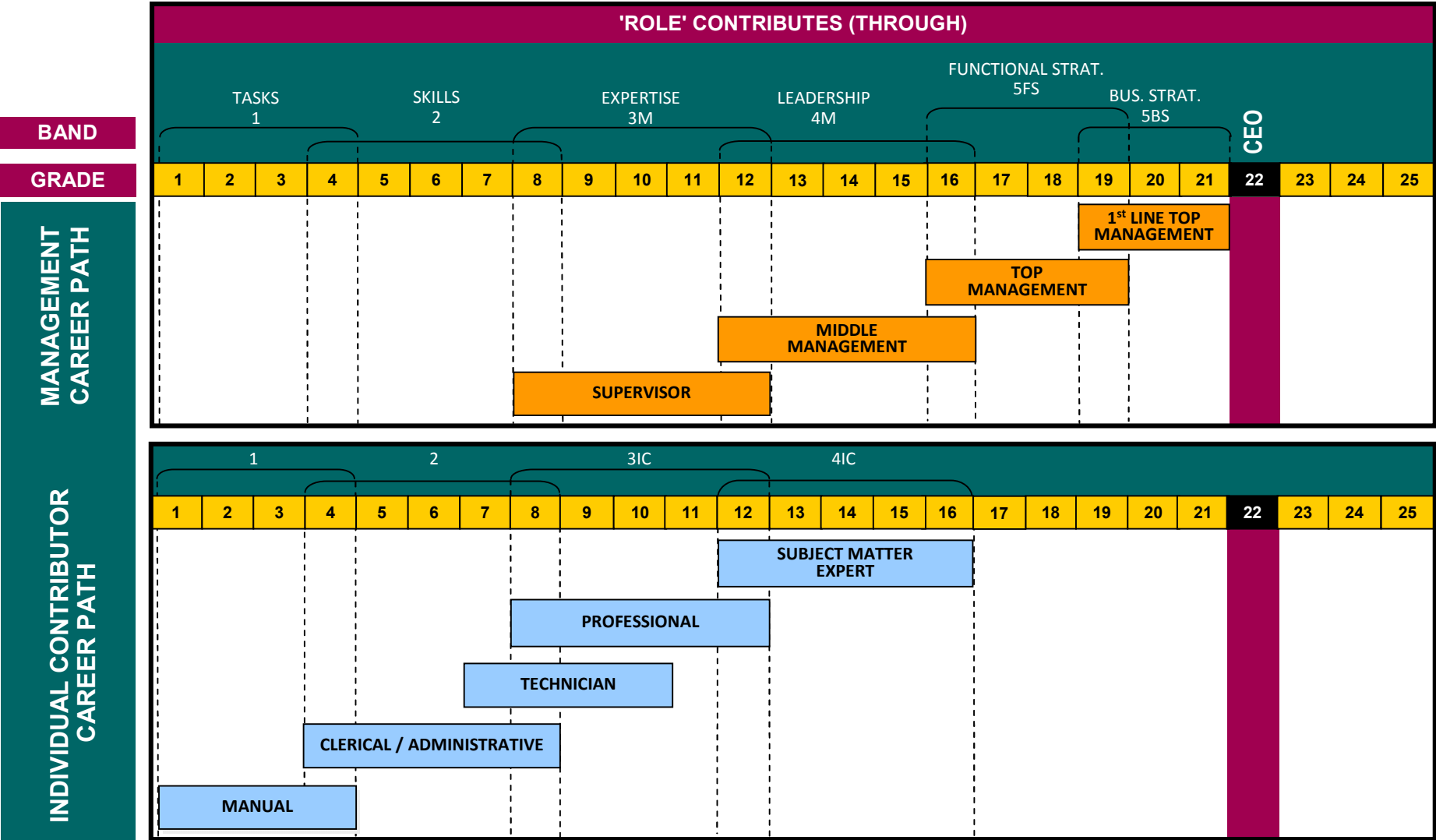
(These steps apply to building a compensable factor plan from the ground floor.)

- Step One: Select compensable factors
- Step Two: Weight compensable factors
- Step Three: Define factors and degree levels within each factor, and assign points to each degree level
- Step Four: Analyze and describe jobs in terms of compensable factors
- Step Five: Determine which degree the definition of each factor best fits the job and assign the respective point values
- Step Six: Sum points and arrange in a grade hierarchy

Global compensation issues

- Locally competitive pay structures
- Globally consistent “levels”
- Mechanisms for managing global career paths
- Mechanisms for managing variable pay and perquisites

Grade Map 22 CEO



Typical Steps in Compensation Redesign Project

Comparison of Market-based vs. Job Content Evaluation

Basic comparisons

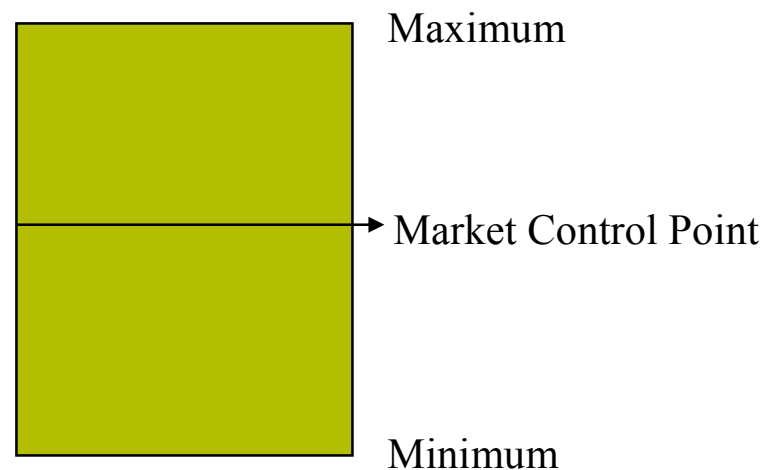
External Equity Emphasis	MP	PF	Internal Equity Emphasis
Emphasis/Focus			
Simple	MP	PF	Complex
Ease of Communication			
Low	MP	PF	High
Technical Complexity			
Low	MP	PF	High
Maintenance Cost of Program			

Frequently asked questions

1. Which system is best for managing costs?

Market Pricing is superior if more than 50% of jobs and 75% of incumbents can be matched to the market

2. How are salary ranges used in market pricing systems?



Frequently asked questions

3. Which system is more accurate?

- Market Pricing: each job is more sensitive to the external market
- Point Factor: each job is more sensitive to internal job relationships

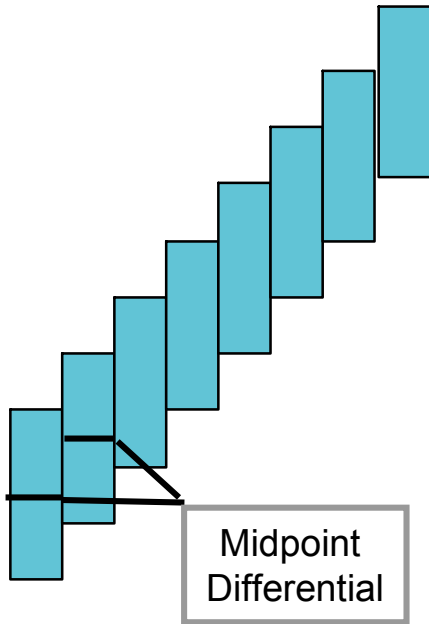
4. Can a company use both systems at the same time?

Every company has a “dominant” approach or emphasis supported by a secondary approach.

Salary structures

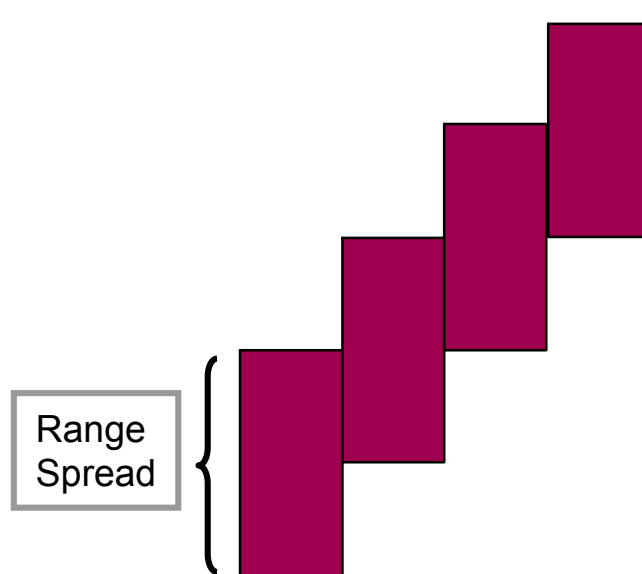
Traditional Structure

Range Spread: 30% - 50%
Midpoint Differential: 5% - 15%



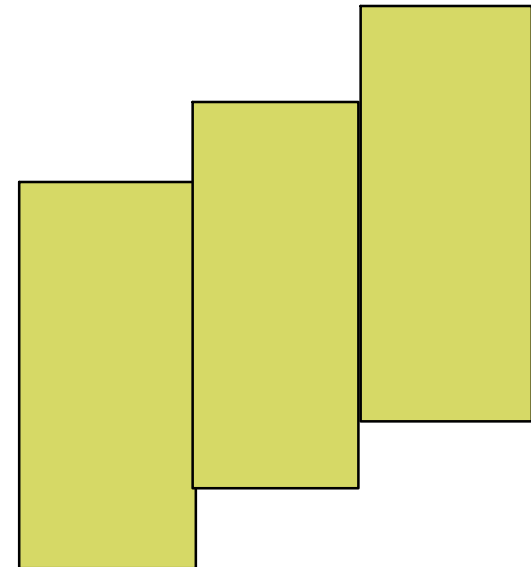
Broad Grades

Range Spread: 50% - 75%
Midpoint Differential: 15% - 30%



Broad Bands

Range Spread: Very Broad
Midpoint Differential: N/A

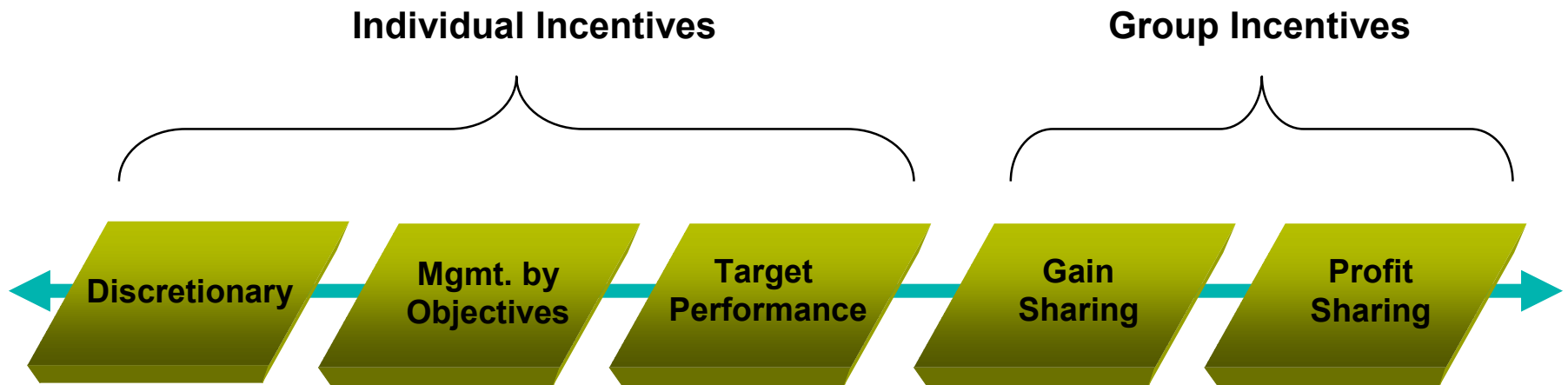


- **Range Spread:** The width, or spread, of the range from the minimum to the maximum
- **Midpoint Differential:** The difference between the midpoint of one grade and the midpoint of the next grade

Typical Steps in Compensation Redesign Project

STI Redesign

Common STI plan types



Anatomy of an incentive plan

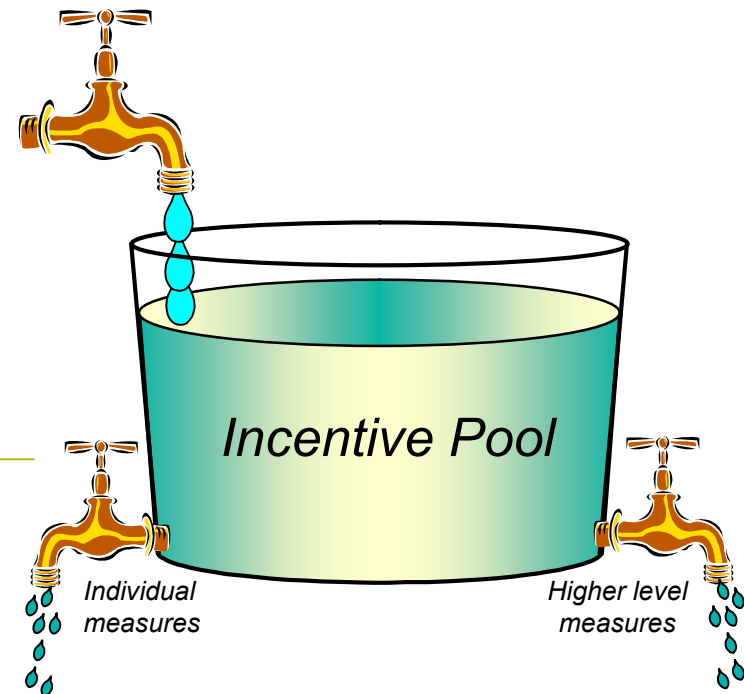
There are two components of an incentive plan:

1. Funding Mechanics

- How much gets put in the “bucket”
 - Measures
 - Triggers/thresholds

2. Payout Determination

- How to determine the incentive amount for each individual



Each component must be considered separately

Overview of best practices

Plan design elements

- Performance measures
- Payments
- Payout timing
- Sunsets
- Participation
- Payout structure
- Communication

Overview of best practices

Performance measures

Plan Design Element		Expected Outcome
Number of Metrics	✓ 3 – 5 (maximum)	<ul style="list-style-type: none"> • Too many measures with a small weight trivializes importance
Weighting of Metrics	✓ Avoid trivial weights	
Focus	<ul style="list-style-type: none"> ✓ Line-of-sight ✓ Line-of-impact 	<ul style="list-style-type: none"> • What I do has an impact on performance and financials
Ease of Achievement	<ul style="list-style-type: none"> ✓ Challenging but attainable targets ✓ Realistic minimum and maximum 	<ul style="list-style-type: none"> • Targets should be set carefully on an annual basis • Program should have boundaries which provide realistic ranges for goals
Commonly used Metrics Note: Best Practice plans drill down to departmental or group levels to identify measures that support the closest level line-of-sight measures	✓ Productivity: Output/Input	<ul style="list-style-type: none"> • Main basis for financial leverage • Focuses line-of-sight
	✓ Utilization	<ul style="list-style-type: none"> • Reinforces quality messages down to the line-of-sight level
	✓ Customer Satisfaction: External Index	<ul style="list-style-type: none"> • A critical measure to communicate messages about the external customer
	✓ Quality: Internal Index	<ul style="list-style-type: none"> • A measure which balances the productivity measure
	✓ Corporate Component: ROE; ROI; EBITDA; etc.	<ul style="list-style-type: none"> • Used to reinforce line-of-impact to the corporate level

Overview of best practices

Other design elements

Plan Design Element					Expected Outcome
Payments	✓ Fixed dollar amount				<ul style="list-style-type: none"> Creates a meaningful payout amount for varying levels of employees without over/underpaying
	✓ % of pay				
Payout Timing	✓ Monthly or quarterly with holdback				<ul style="list-style-type: none"> For short-term goals
	✓ Annually				<ul style="list-style-type: none"> For cyclical goals
Sunsets	✓ Annual renewal				<ul style="list-style-type: none"> Keep goals contemporary and challenging Avoids “yo-yo” effect
Participation	✓ Wall-to-wall				<ul style="list-style-type: none"> Reinforces total group effort (“one team, one dream”)
Payout Structure	Element	Min	Tgt	Max	<ul style="list-style-type: none"> Choice of Min/Tgt/Max levels is critical for sending messages about expectations Less than 5% target has potential for losing the attention of participants Target levels should be linked to external market pay practices and support internal equity
	Perf Measures	Threshold at minimally acceptable performance	Financially viable or self-funding	Highest expected reasonable performance	
	Pay Level	0%	5%	10%	
Communication	✓ Frequent communication that delivers a consistent message				<ul style="list-style-type: none"> Increased line-of-sight for employees Understanding of plan objectives

Developing Supporting Communication Strategies for Successful Implementation

Communication strategy map

- Articulate business objectives that will be communicated
- Identify key audiences and customized messaging requirements
- Identify methods of communication that will be utilized
- Define communication objectives and measures of success
- Identify challenges/barriers
- Create timeline

Exercise - Communication strategy map

Business Objectives	
Communication Objectives and Measures of success	
Challenges/Barriers	

Key Audience			
Method of Communication			
Timeline			

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