



A New Era in Compensation: Modernizing Base Pay

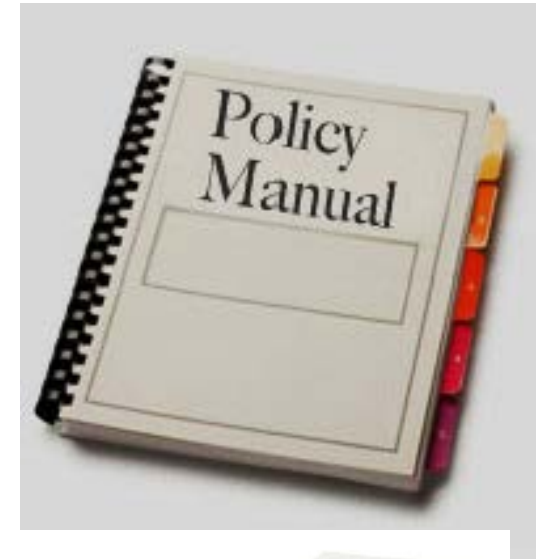
Alabama State SHRM Conference

May 17, 2017

Remember the days...




Remember the days...



The number of text messages sent in the US each day



6 billion



**Baby Boomers are retiring
at the rate of
1 every 9 seconds
between now and 2029.**

**The average U.S. student
today will have 10 to 14 jobs**



**before
the age
of 40**

Percent of children entering school today who will end up in jobs that do not exist yet





What percentage of the U.S. population has a LinkedIn profile?





Our world has and continues to change



**Always
online**



Connected



**Ready
access to
information**



**Everything
is personal**

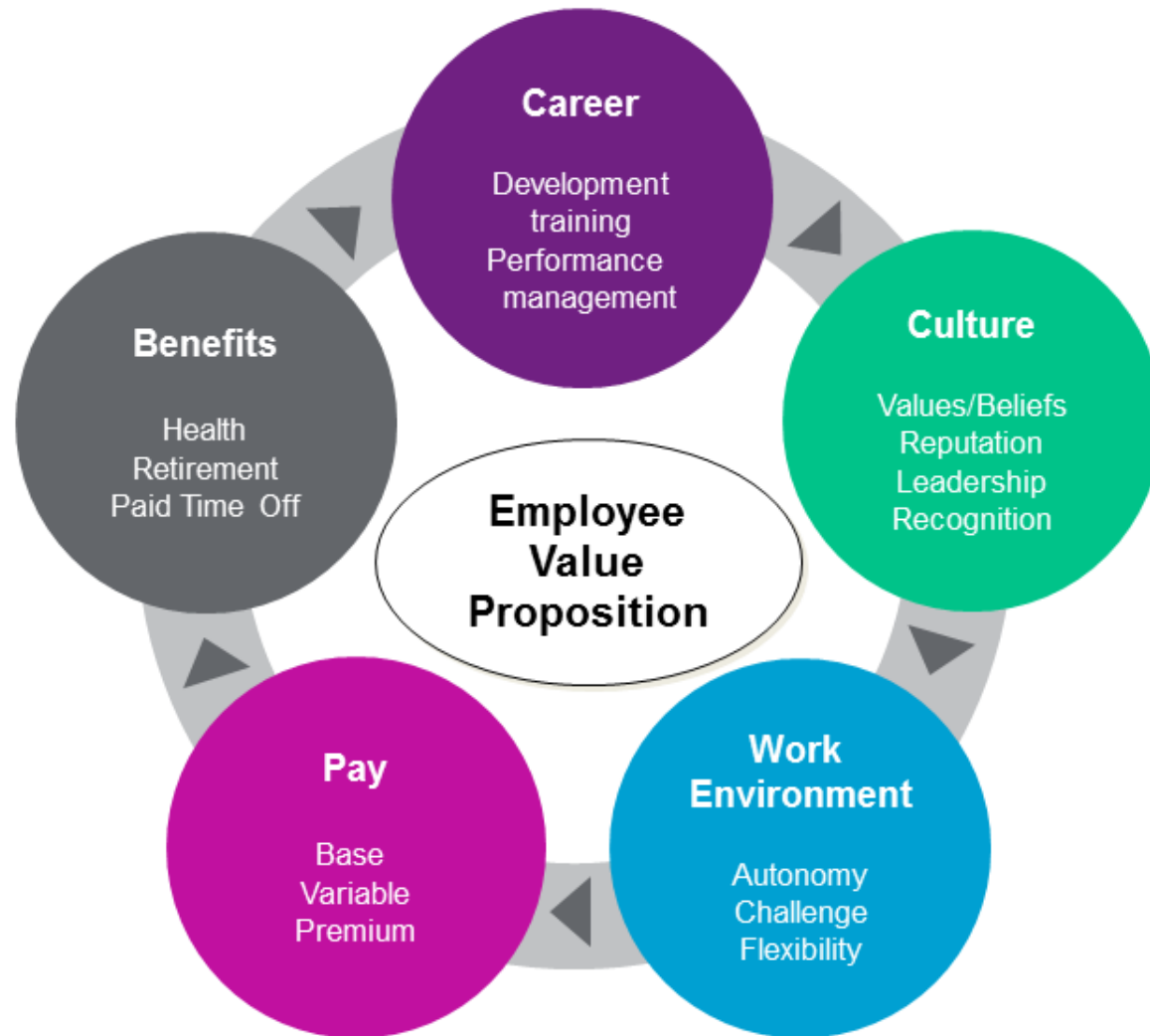


**Technology
is everywhere**



Our world has and continues to change

Total rewards and employee value proposition





Market trends and realities

Modernization and relevance

Fast-changing market



Fast-changing technology



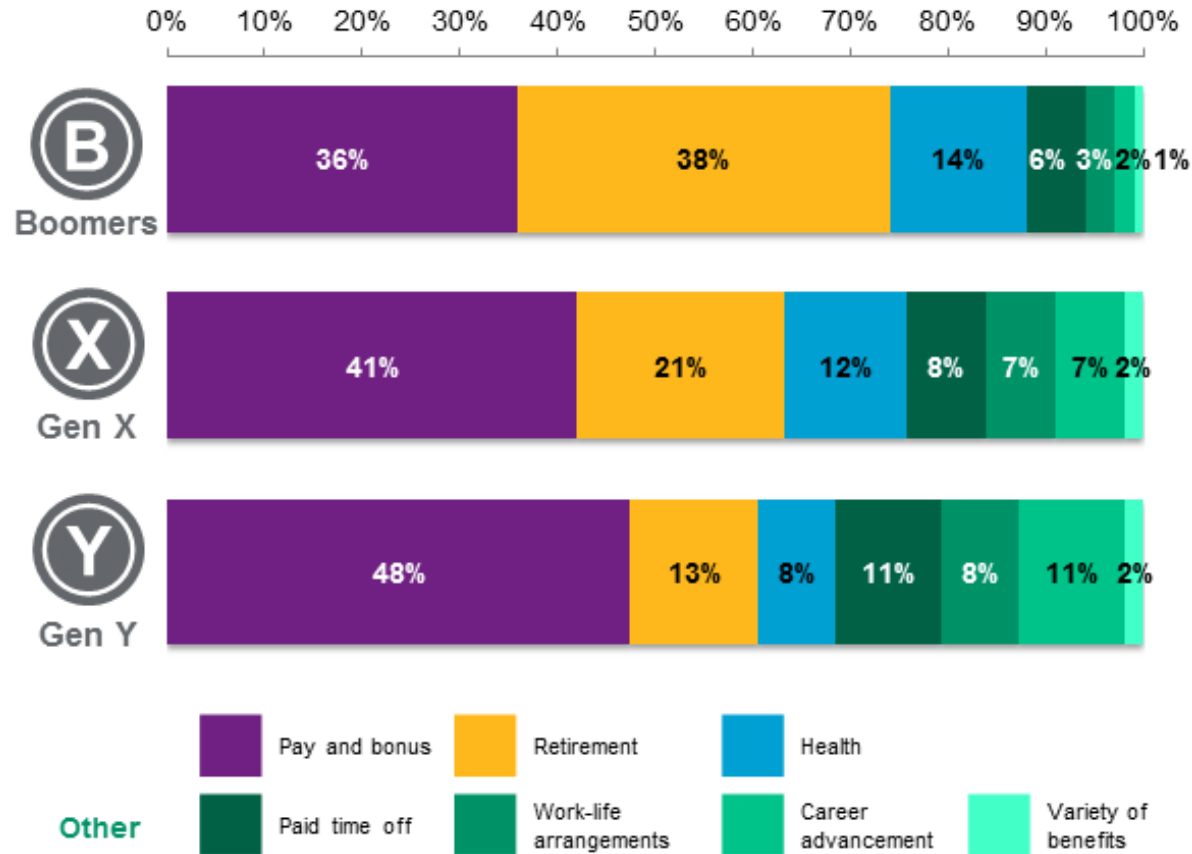
Demographic shift – It's really happening



Expectations of transparency and individualization



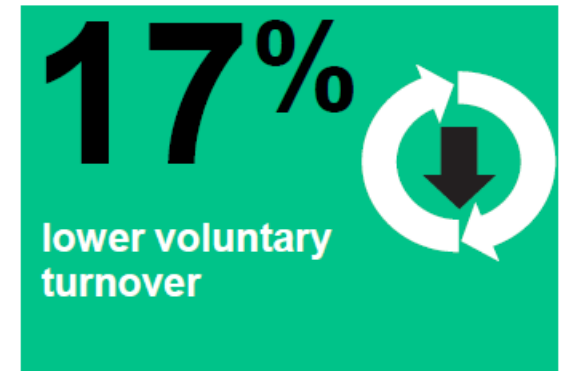
Generational shift and reward preferences



Source: 2015/2016 Global Benefits Attitudes Survey, U.S.
Sample: Full-time employees only.

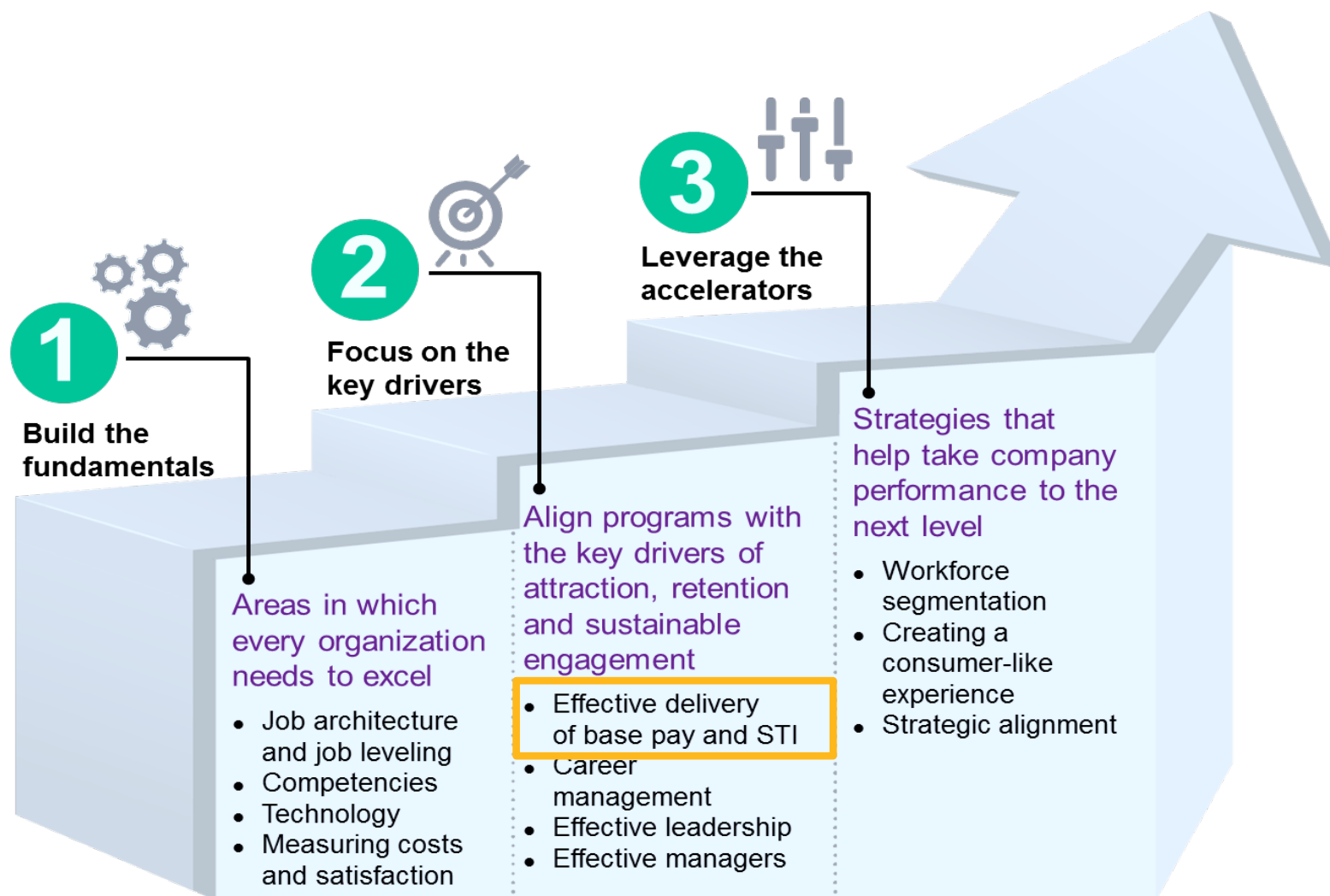
The business case for having a superior EVP

Best practice EVP companies achieve better outcomes



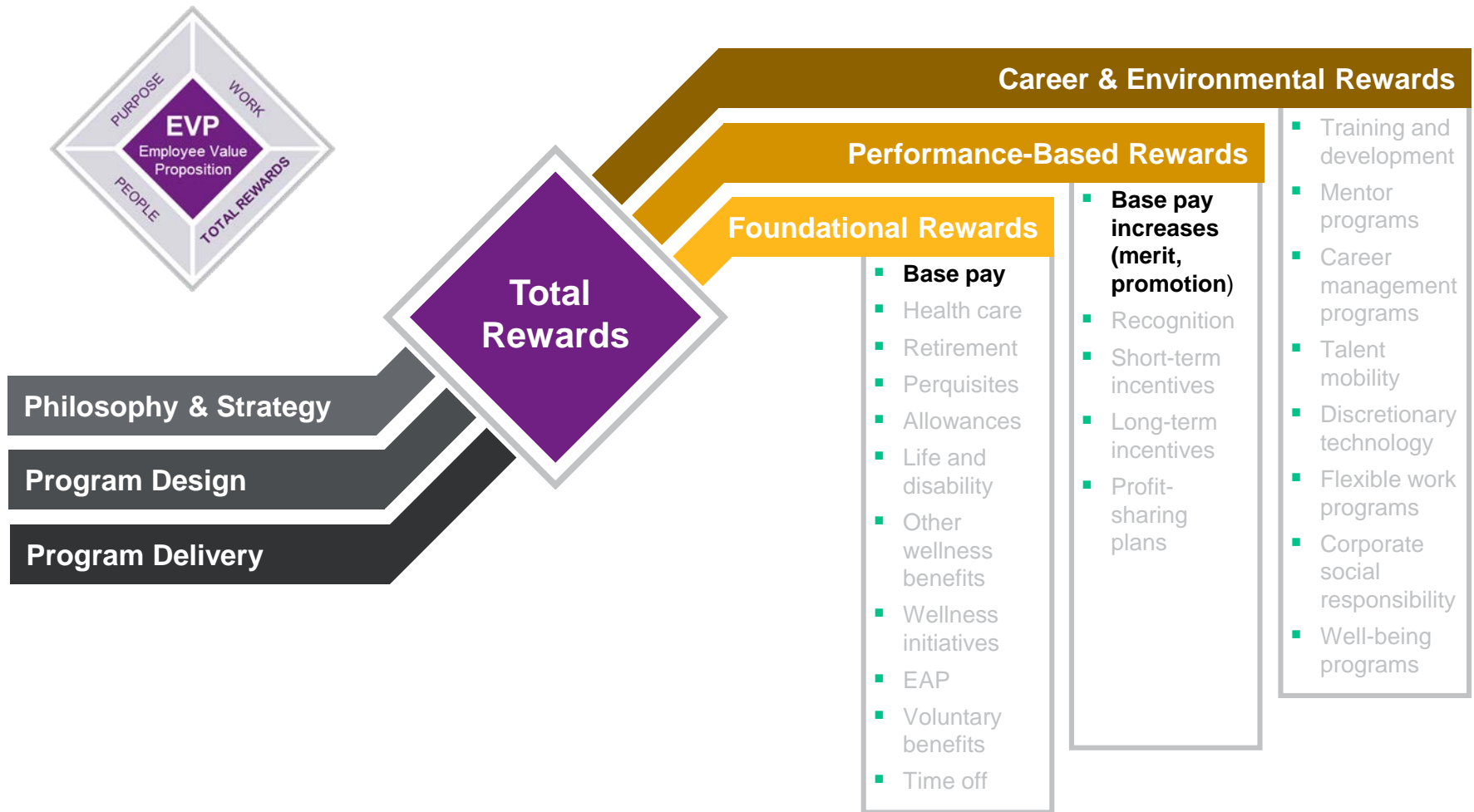
Source: 2016 Towers Watson Global Talent Management and Rewards Study

Base pay remains a critical component of your EVP



Before and now ... integrated total rewards

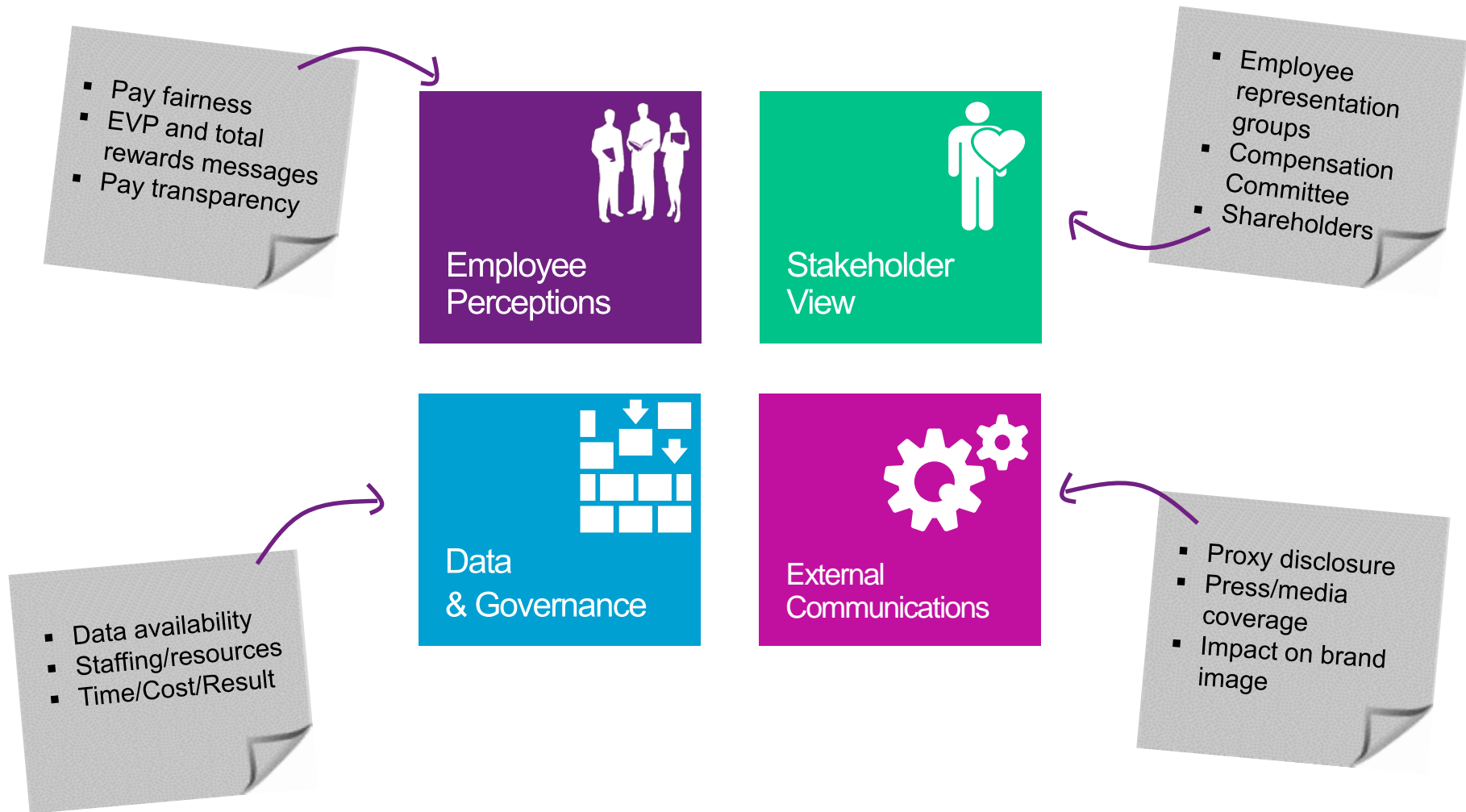
Base Pay – foundational and performance based reward





Base pay administration

Heightened pressure



When it comes to modernizing base pay

Our clients are asking...

That's all well and good that merit matrices seem outdated but what replaces them

How can we better differentiate merit awards... or **SHOULD** we?

Are we really setting the right salary budgets? 2% – 3%... the business says the market is not moving that fast

Scrapping annual increases, seriously?

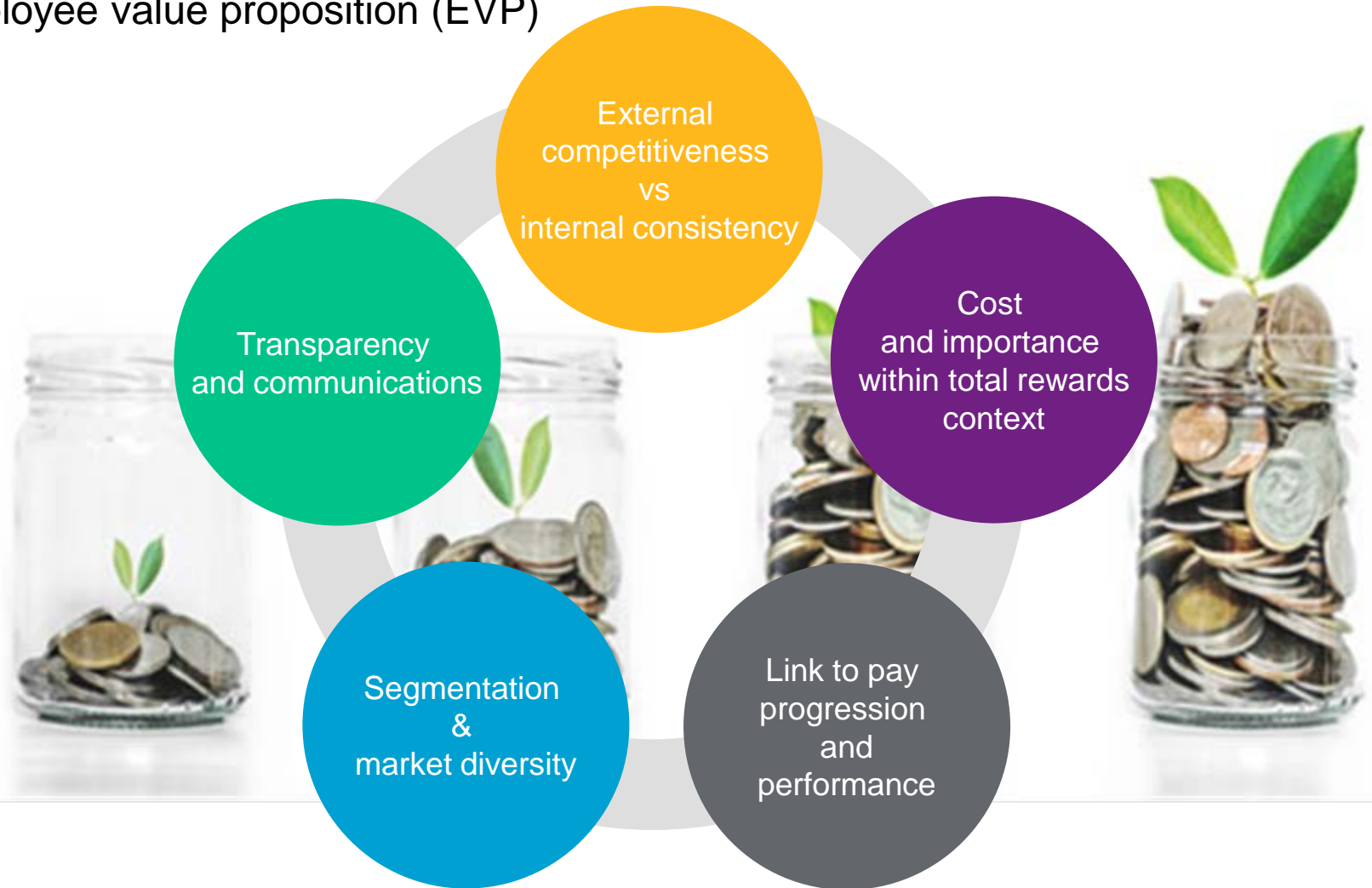
How can we make substantial base pay increases more meaningful to employees?

How do we determine the marketplace when jobs and the workforce are rapidly changing?

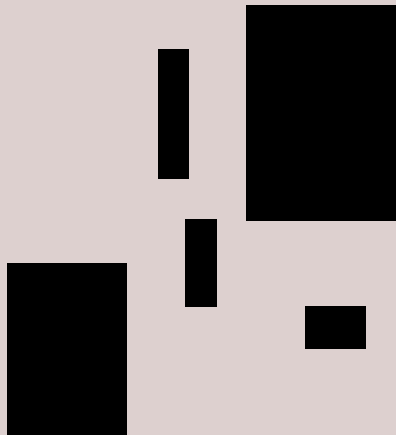


To design and deliver an effective compensation program...

An organization must understand how their compensation program fits into their employee value proposition (EVP)





Base Pay Philosophy, Design and Delivery



There's no escaping the fundamentals

The key drivers of attraction and retention have remained fairly steady over the past two years and continue to reflect the fundamentals – *base pay, and career advancement opportunities*

No	Attraction Driver 	Retention Driver 
1	Base pay/salary	Base pay/salary
2	Job Security	Career advancement opportunities
3	Career advancement opportunities	Physical work environment
4	Challenging Work	Job Security
5	Opportunities to learn new skills	Ability to manage work-related stress

Sources: 2016 Global Talent Management and Rewards Study – Employee View

Fundamentals ... determining market position

What is your Market Position?

Considering the need to pay

- Business plans/HR strategy
- Turnover/ease of recruitment
- Feedback from employees/ industry comparisons
- Geographic location





Considering the capacity to pay

- Company profitability
- Social/political sensitivity
- Future forecasts
- Company life cycle
- Base vs. Total Cash position

Market Position

Factors influencing positioning strategy

External Factors (Market Specific)

Supply of Talent	High		Low
Talent Mobility	Low		High
Industry Stability	High		Low
Industry Attractiveness	High		Low

Internal Factors (Company Specific)

Role Criticality	Low		High
Company Image	Good		Poor
Performance Targets	Low		High
Workload	Low		High
Employee Value Proposition	Strong		Weak
Hiring Needs	Low		High
Impact of Turnover	Low		High

Potential Position in the Market:

40%

50%

75%

90%



Fundamentals ... job evaluation methods

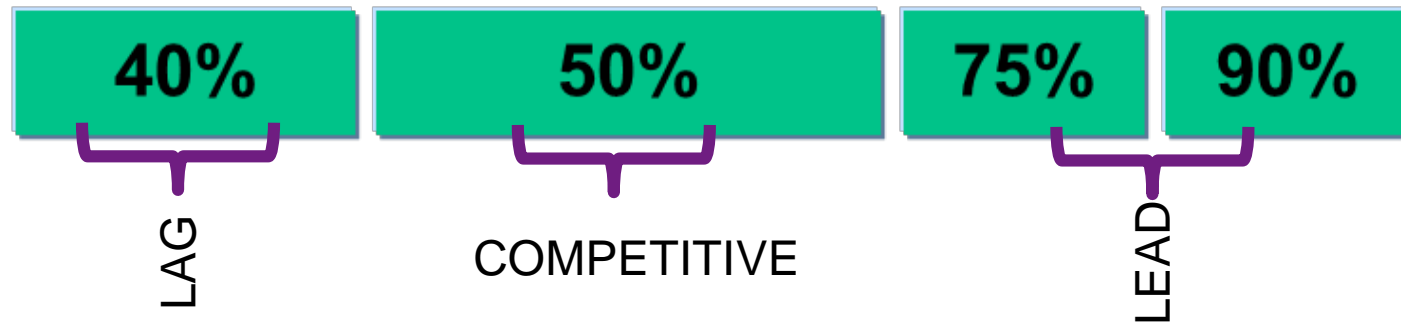
	Ranking	Classification	Point Factor	Job Component	Market Pricing
Senior Mgt (n= 616)	3%	6%	16%	2%	74%
Mid-Mgt (n=625)	3%	7%	19%	2%	70%
Professional (n=625)	2%	7%	20%	2%	69%
Sales (n = 552)	2%	7%	17%	2%	72%
Administrative (n= 623)	2%	8%	20%	2%	68%
Production (n = 543)	3%	10%	17%	2%	69%

Source: World at Work Job Evaluation and Market Pricing Practices Study – 11/15



Lead, meet or lag strategy

Is it the same for all or different for key segments



Legacy Skills, High
Supply Talent



Critical Skills, High
Demand Talent

Fundamentals ... market pricing

Why survey the market?

- Helps organizations understand the influence of supply and demand on the cost of labor
 - Where is the market shifting, how quickly and by how much? Are we able to respond to 'hot' jobs – those with critical skills
- Provides data to assist with pay decisions; helps to eliminate guesswork and emotion
 - remember compensation is an art not a science
- Assists in identifying and/or establishing career levels and reward practices



Determining market position

How to collect Market Data?

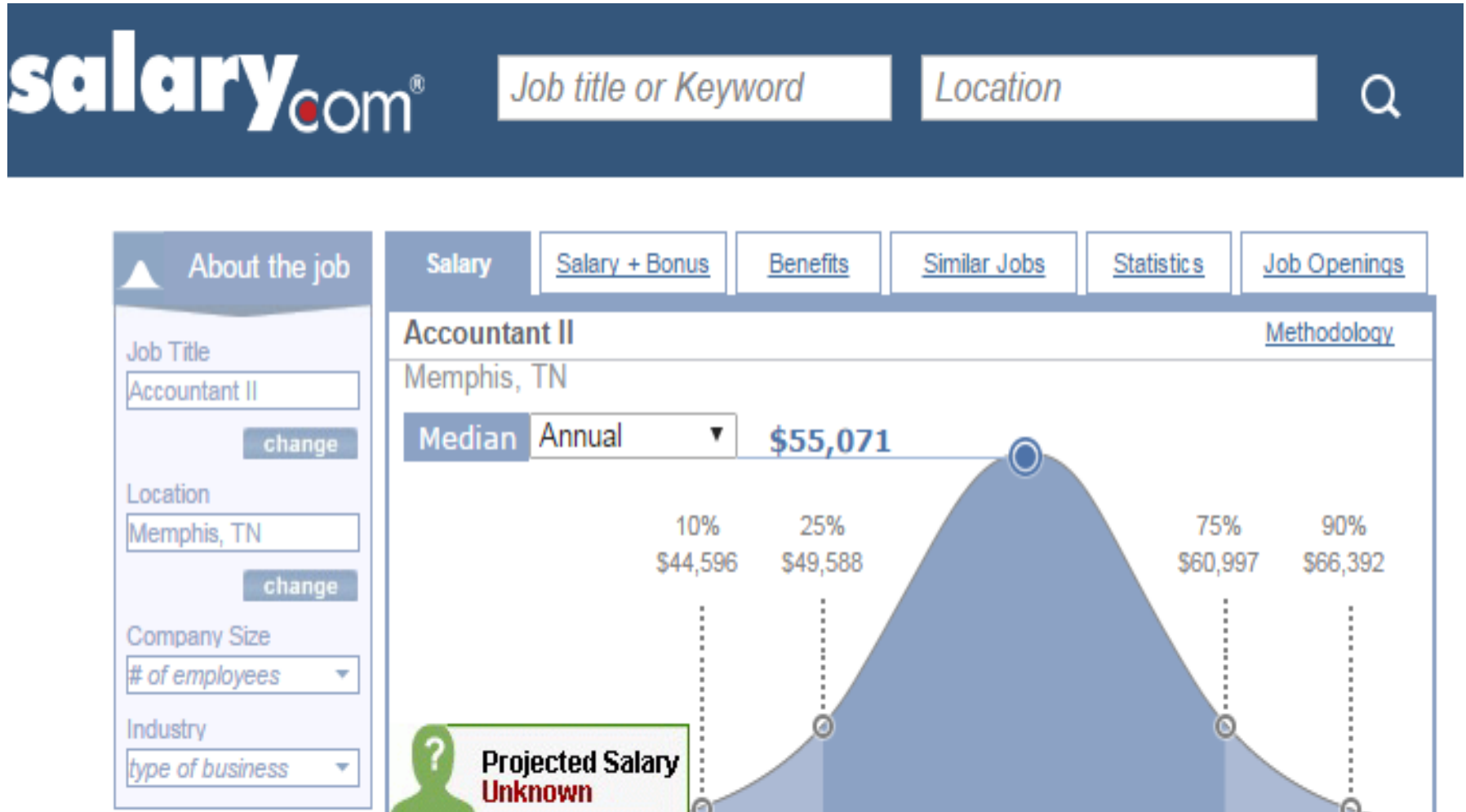
- Informal networking
- Conduct own survey
- Buy data off the shelf
- Subscribe/Participate in independent third party survey
- Sponsor an independent survey

What to look for:

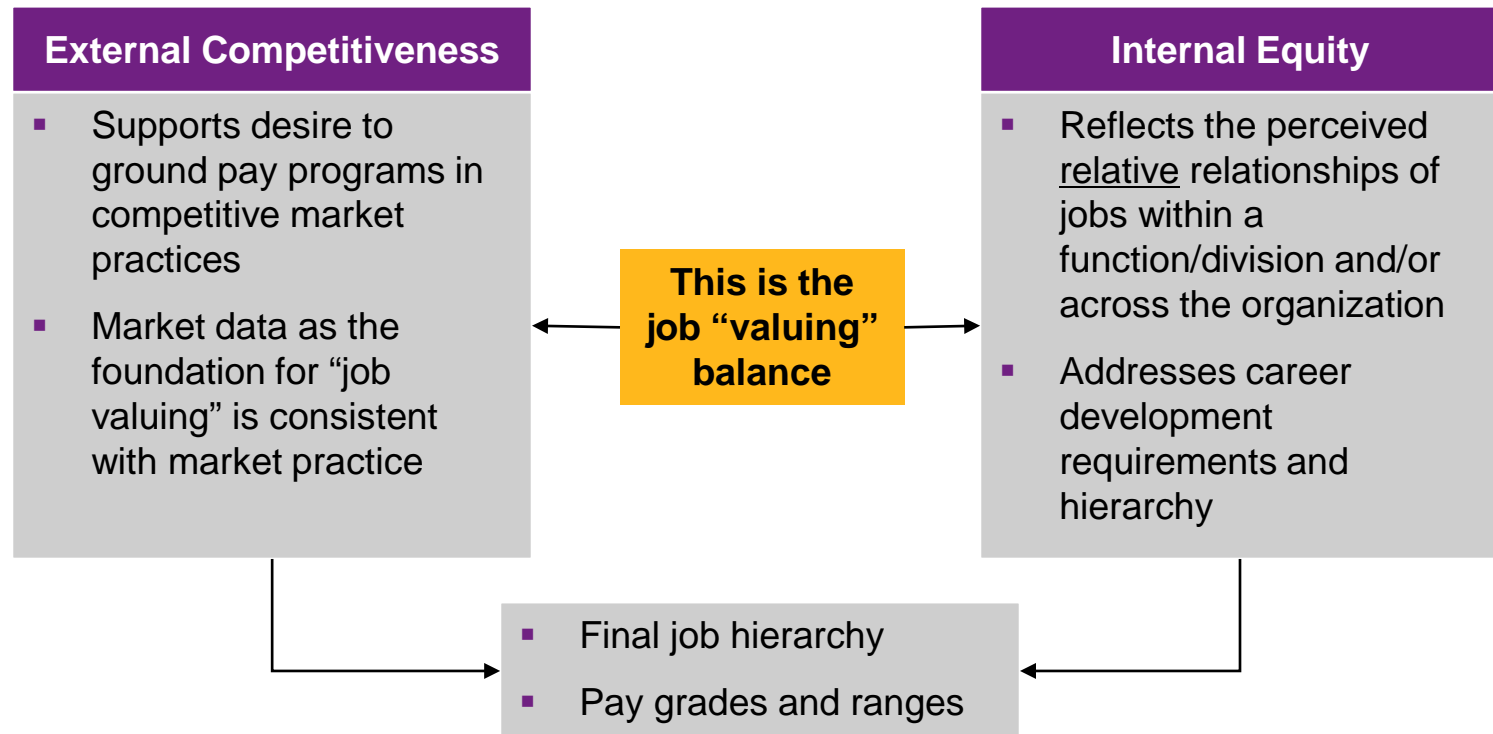
- Methodology
- Benchmark Jobs
- Participation
- Sample size & data collected
- Sector focus & geographic representation
- Value (quality, cost, timeliness)
- Confidentiality & consultant expertise
- Service quality

Surveys – the good, bad and ugly

Data is everywhere yet quality sources are scarce.



Balancing external market competitiveness and internal job equity




Fundamentals ... pay structures

A formal salary structure is an important component of an effective compensation program

<div> <div>Focus on Internal Position Value</div> <div>Blended</div> <div>Focus on External Market</div> </div>					
Pay range per grade	Market referenced Pay range per grade	Job Families	Job Families with Dual ranges	Market anchors	Broad Bands
<ul style="list-style-type: none"> No market reference, purely internally driven 	<ul style="list-style-type: none"> Market informed Pay ranges constructed with reference to selection of market data points 	<ul style="list-style-type: none"> One range per level, per job family 	<ul style="list-style-type: none"> Use of standard and premium ranges Those with a high rate in the market in premium ranges One set of each per job family/level 	<ul style="list-style-type: none"> Market data gathered for as many roles as possible Jobs in a ladder level clustered based on market pay rate Typically 3-4 per job family/level Ensures no individual more than 10% beyond their market reference point Default position 	<ul style="list-style-type: none"> Individual rate for the job Purely market data driven

How do we pick which type of structure to use?

- A salary structure should reflect an organization's structure and management values
- One key question is how much the organization emphasizes managing its people vs. managing its costs

	Companies with this type of organization structure...	...and these management values...	...tend to use this approach to base salary
	<ul style="list-style-type: none"> ■ Hierarchical ■ Multiple layers ■ Many jobs/titles ■ Finite distinctions between grades/bands 	<ul style="list-style-type: none"> ■ Centralized control ■ Focus on jobs more than individual employees ■ Focus on promotion vs. career growth ■ Internal equity ■ Greater emphasis on managing labor costs 	<ul style="list-style-type: none"> ■ Analysis-heavy job evaluation models ■ Multiple, narrower grades/ranges ■ Pay is an administrative function
	<ul style="list-style-type: none"> ■ Flatter organization ■ Fewer levels/layers ■ Fewer jobs/titles 	<ul style="list-style-type: none"> ■ Decentralized control with greater emphasis on line manager accountability ■ Person based ■ Focus on career growth vs. promotion ■ Externally focused ■ Flexible 	<ul style="list-style-type: none"> ■ Competency-based plans ■ Fewer, broader grades/bands ■ Flexible salary increase guidelines ■ Pay is a strategic lever used to drive business objectives and reinforce cultural norms

Structure development process

Remains relatively traditional in nature

Step 1 Organize jobs into grades or levels

Step 2 Review the market rates for benchmark jobs in each level

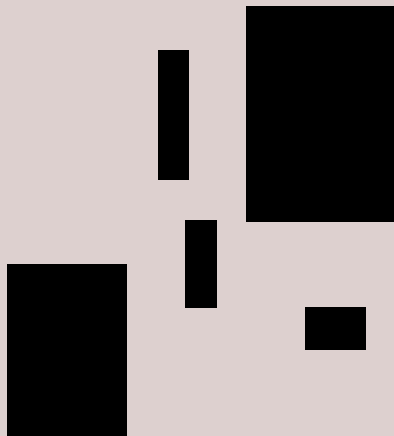
Step 3 Determine midpoints and midpoint progressions

Step 4 Determine range spreads

Step 5 Calculate range overlap

Step 6 Impact analysis and costing

Merit Increases and Pay for Performance



Pay for performance and merit increases

Current state



Pay for performance includes any total reward element that is differentiated on the basis of performance delivered (however performance is defined) at the enterprise, team and/or individual level.

It may feel like the odds are stacked against us:

- Increased disclosure and governance requirements put pay under a laser-sharp spotlight
- Countless hours spent managing 2.5% - 3.0% merit budgets to achieve differences that are nominal

Source: 2016 Willis Towers Watson Global Workforce Study

Don't give up – you know why?

- **Boards and Compensation Committees**
- **Significant financial and resource investment in programs**
- **Employees - those with a positive view of pay for performance are more likely to be highly engaged**



Highly engaged

- **All** respondents..... **37%**
- My organization **does a good job explaining** our performance management process..... **50%**
- People are **held accountable** for their performance at my organization..... **56%**

Source: 2016 Willis Towers Watson Global Workforce Study

Have merit increases outlived their purpose?

We know our research tells us...

40%

of companies say **base salary or “merit” increases** are effective at driving higher levels of individual performance

55%

of companies say that **merit increases are effective at differentiating pay** based on individual performance

99%

of employers **deliver base pay increases on an annual cycle**, versus tailoring delivery to the business model

70%

of employers determine **merit budgets by local market rates**, versus organization performance

1/3

Over one third of employers expect **to pay more for employees with certain critical skills over the next three years**





Base salary increases

Same headline, different story?

The Reality:



Limited financial resources – companies cannot afford to deliver significant pay increases to all employees each year



Homogeneity – employees are generally subject to the same merit increase guidelines, regardless of talent segment



Differentiation – merit increase differentiation is challenging given small budgets



Entitlement mentality – employees expect an annual increase each year, regardless of their job marketability



Focus on the future – when making base pay decisions, managers give more weight to the present and future, rather than past, which is typically not prescribed within the program design

*Suggesting a need to challenge
conventional thinking...*



Pay for performance

Where have we been and why change now?

In the current world....

Performance is typically rewarded with base pay increases and cash bonuses:

- Largely one size fits all
- Tried and tested
- Easy to administer
- Low risk
- Easy to design

Challenges organizations are facing today:

- Optimizing ROI and maximizing engagement
- Segmenting reward for different generations
- Treating employees as consumers



Organization have responded by moving to increased flexibility

- Flexible benefits
- Healthcare exchange
- Flexible working arrangements

....so why continue to be so limited with performance-based rewards?

Introducing flexibility in the way performance-based rewards are delivered **assists at recruiting, motivating and retaining top, critical talent**

Rethinking merit increases: how to modernize your approach

PURPOSE

1

Less emphasis on last year's performance

- Broader future oriented and skills view and career progression
- Objectives for aligning to "market"
- Integrated

DIFFERENTIATION

2

Meets an age of transparency

- The degree of individual pay variance may differ by talent segment
- Salary increases may also be differentiated by talent segment
- Clear communication of differentiation criteria is essential

QUANTUM

3

Meaningful amounts

- Performance-based or promotion increases should be perceived as meaningful or "zero" increases are provided
- "Meaningful" may vary by job level and salary

TIMING

4

Rethink the annual cycle

- "Annual" may not be right cadence for all talent segments

BUDGET

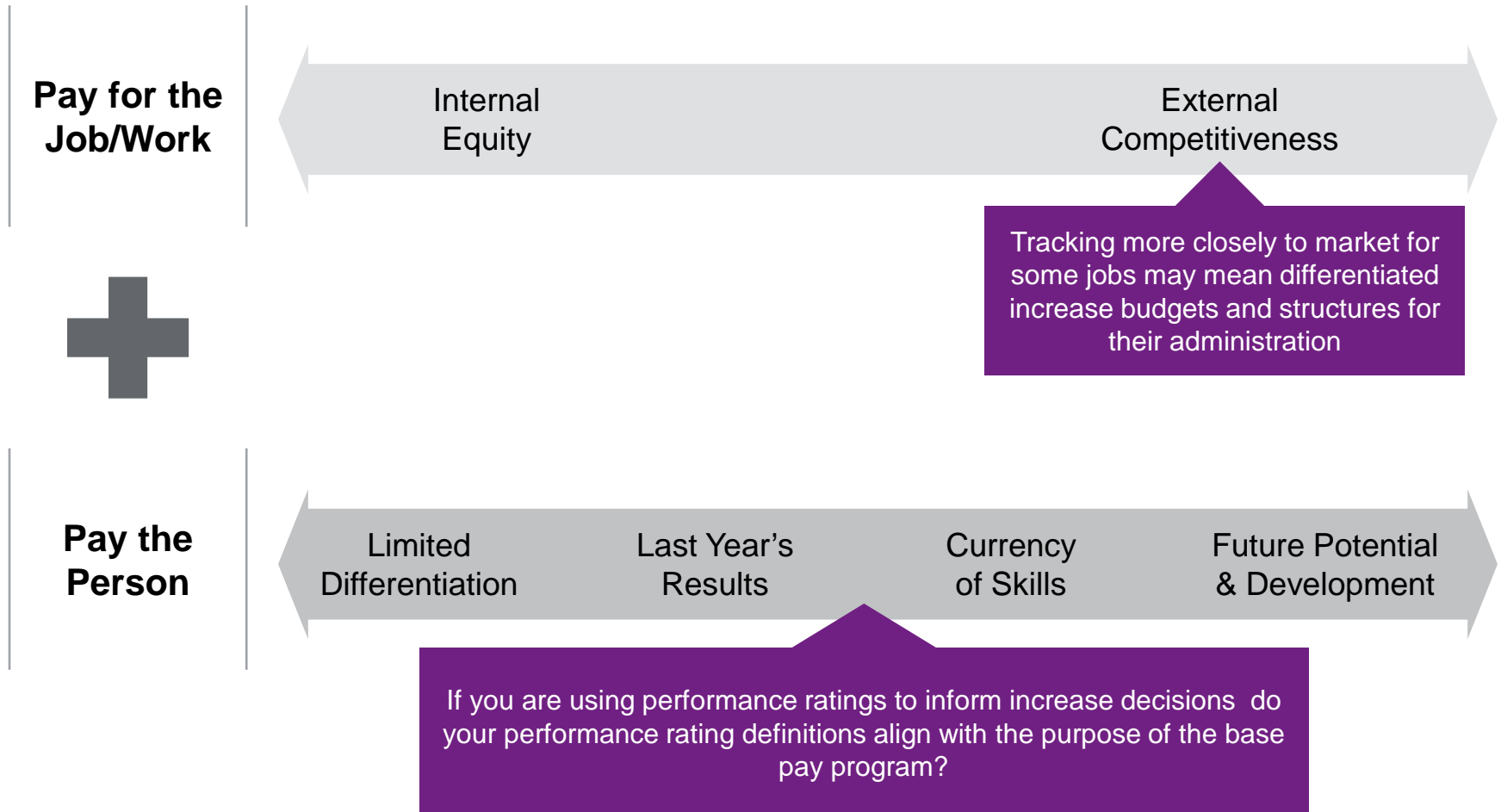
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Revisit and prioritize your budgets

- Ensure budgets meet business and talent objectives

What's your salary for?

Where you plot answers on this continuum will shape program design



De-stigmatizing ratings

Am I average?

Communicate that the "middle" rating is not equivalent to a C in school, but rather like shooting par in golf. Par doesn't mean perfect. Par also doesn't mean average or mediocre or middle of the road. What par represents is the number of golf strokes considered necessary to complete a hole or course in expert play. A pro golfer can often do better but par is what is expected of an expert.

Use labels for the middle performance category such as **"Solid Performer," "Meaningful Contributor" or "Fully Effective."** People take greater pride in these designations than labels like "Competent" or "Satisfactory" which denote mediocrity.

De-stigmatizing ratings

5 Level Rating Scale

Exemplary/
Outstanding

Commendable

Meaningful Contributor

Approaching Competent/
Developing

Unsatisfactory

3 Level Rating Scale



Rethinking the annual cycle

TIMING

Rethink the annual cycle

- “Annual” may not be right cadence for all talent segments

Frequency

There may be some exceptions to an annual cycle

- More frequent for targeted critical skill groups or fast-moving markets
- Slow moving markets may mean that there are some years where “broad-based increases” - are not required – requires significant change management and must be considered in relation to all programs

Timing

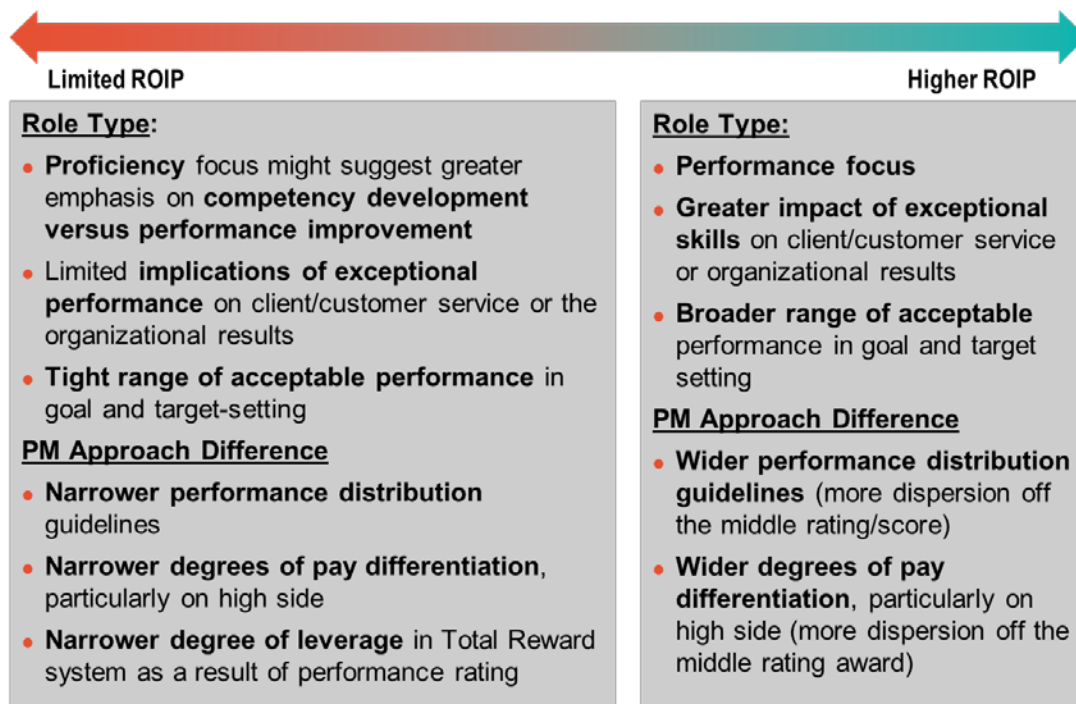
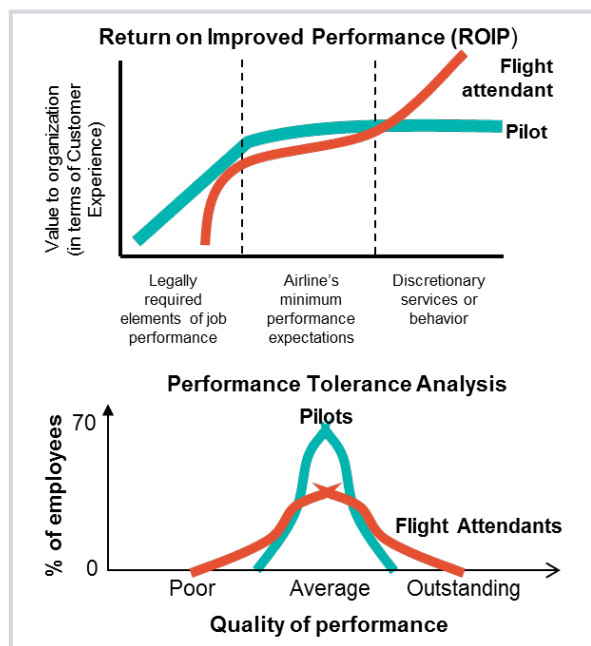
- Consider decoupling either the communication or timing (balanced with administrative burden) of market adjustments vs. individual performance/skills based increases
- Pros and cons exist in a variety of approaches and will vary by organization culture and program emphasis

Pay for performance

The importance of segmentation

Best practice: Segmentation

- Different roles impact/contribute to the business differently; improved performance of some roles add more value to the business than others
- Identify categories of roles that will be treated differently because of pivotalness to the organization or the nature of their contribution/performance

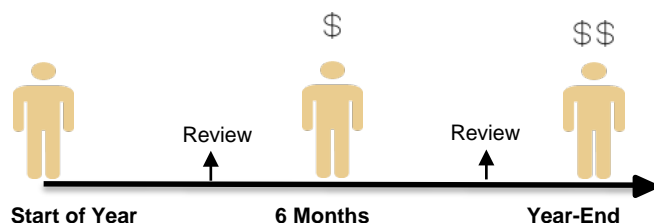


Goal of purpose and differentiation

May lead to segmented approaches

Illustrative

Specialized program to retain high potential
“early career” professionals



- More frequent increases (bi-annual))
- Based on skill assessment
- Lower tolerance for below market positioning – simulate the external market practice of “big increases” for demonstrated experience of emerging skills

Presenting Issue

Market pay progression for early career customer analytics roles was found to be high – lots of opportunity for pay growth by changing employers

- Tracking to external market pay considered a high priority for the first two levels of the career track
- Roles were moved to bi-annual increase cycle **for review**
- Increase amounts tied to market reference points within the career level and an assessment of skill currency and potential (increase not automatic)
- Need to re-assess program annually

Pay for performance – linking with other programs

Differentiating across total rewards

Best practice: Differentiating across various reward elements

Organizations significantly advance alignment across systems by specifying how various reward elements vary by performance, where relevant

Reward Elements	Does Not Meet Minimum Expectations	Approaching Competent	Meaningful Contributor	Exceeds Expectations	Exemplary Performance
Merit Increase	0 x average merit (e.g., 0%)	$\frac{1}{4}$ – $\frac{1}{2}$ X average merit (e.g., 1% – 1.5%)	Average merit (e.g., 3%)	$1\frac{1}{2}$ - 2 x average merit (e.g., 4.5% – 6%)	>2.5x average merit (e.g., 8%)
Short-term Incentive Award (or GIP)	No incentive	No incentive to $\frac{1}{2}$ target incentive	Target incentive	$1\frac{1}{2}$ x target incentive	2x target incentive
Training Opportunities	Minimal training; focus on performance	Remedial training	Normal training	High-performer training opportunities	High-performer training opportunities
Development Opportunities	Immediate performance improvement plan	Close monitoring and coaching	Eligible for development assignments	Targeted for developmental assignments	Identified as high-potentials and targeted for special assignments
Promotions	Not eligible for promotion	Not eligible for promotion; but may be eligible for lateral move	Eligible for promotional consideration	Targeted for promotional consideration	Targeted for promotional consideration
Percent of Population	5% – 10%	10% – 15%	60%	10% – 15%	5% – 10%

Pay for performance – linking with other rewards

Segmentation

Program	Talent Segments				
	Executives	Managers	Sales	Critical Talent	HiPos
Merit	✓	✓	✓	✓	✓
STI	✓	✓		✓	✓
Sales Incentives	✓		✓		
LTI	✓	✓	✓		✓
Corp/Local Recognition	✓	✓	✓	✓	✓
Stock Options	✓	✓			✓
Development Programs	✓	✓	✓	✓	✓
Spot Bonuses	✓	✓	✓	✓	✓
Other Total Rewards (i.e. Additional PTO)			✓	✓	✓

Pay for performance

Hello Mark, welcome to your Performance-based flexible rewards!

Your **Basic Package** is:

Reward Element

Basic pay

Fixed cash allowances

Children's education benefits

Annual leave days

Other leave days

Retirement

Life and disability insurance

Unemployment insurance

Basic medical insurance

Health assessment

Mobile phone

Workplace flexibility

Note: point calibration is illustrative

Mark, you have been recognised as a high performer, thank you for your hard work!

Your Performance Points Balance is: 23,000 points. Select from your **Performance Rewards Shop...**

Reward Element	Cost (Points)	Select
Cash bonus	10 points per dollar	<input checked="" type="radio"/>
Additional annual leave	1,000 points per day	<input checked="" type="radio"/>
Sabbatical	20,000 points per month	<input type="radio"/>
Retirement contribution	6 points per dollar	<input type="radio"/>
Child care vouchers	6 points per dollar	<input type="radio"/>
Emergency eldercare	6 points per dollar	<input type="radio"/>
Gym membership	1,000 points per month	<input type="radio"/>
Additional medical insurance	8 points per dollar	<input type="radio"/>
Children's education account contribution	8 points per dollar	<input type="radio"/>
Company car	50 points per day	<input type="radio"/>
Training course	20 points per dollar	<input checked="" type="radio"/>
Career management programs	100-200 points	<input type="radio"/>
Enhanced maternity/paternity	500 points per day	<input type="radio"/>
Tuition reimbursements	8 points per dollar	<input type="radio"/>

Points based on previous performance period and increase in line with higher performance

Revisit and prioritize budgets

..... to meet business and talent objectives

Actual dollars invested in salary increases often exceed those reported in published survey data. Why? Increases resulting from “promotions to vacancies” and “internal transfers” are often lost as part of budgeted headcount expenses. Unveiling the total spend takes courage, but the result is a more transparent, thoughtful view of the base pay management story and measured correctly

Budget Categories Should be Clarified – Even if they Are Administered Together

Market Adjustments

- Uplift of entire job roles due to market movement (generally performance “agnostic” excluding documented low performers)

Performance or Skills Based

- Increases based on defined criteria (i.e. the definition of performance to be rewarded through base salary)

Event/Milestone Driven

- Promotion or progression to a vacant role
- “In line” promotion within a career track tied to defined milestones
- May reflect a “simulation” of market progression

Prioritizing budgets

..... to meet business and talent objectives

Market Adjustments

Prioritize When....

- Close alignment to market is the primary purpose
- When traditional “merit” has yielded inconsequential differentiation
- When distinguishing job based market adjustments from “individual” rewards increase transparency

Cadence

- At pace with market – in today’s environment, excluding “hot skills” may be less frequent than annual

Performance or Skills Based

- When the purpose of base pay is to distinguish for a defined, measurable definition of performance

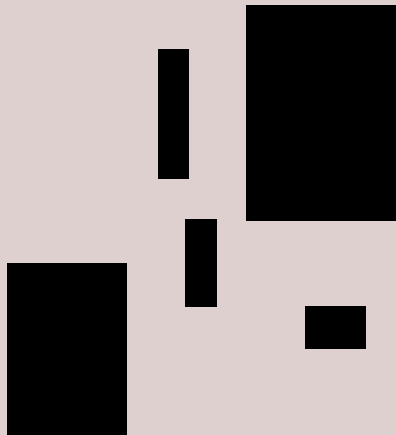
- May be annual with caveats – amounts should reflect minimum tolerance standards

Event/Milestone Driven

- Reward for internal development and skills progression is a primary purpose of base salary (over other definitions of performance)

- Tied to milestone achievement

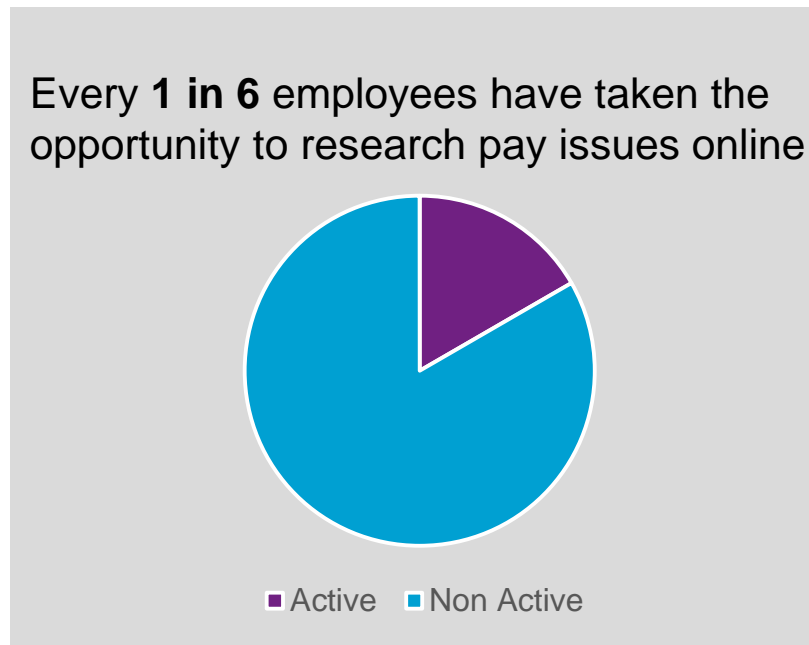
Pay Transparency





Transparency is a given...

In the ever changing workplace, transparency and openness is becoming a critical issue



Source: 2016 WTW TM&R and Global Workforce Studies



Companies are increasingly required to be...



Transparent

Open communication is becoming the norm to establish a positive culture and meet compliance requirements



Leading

Organizations want to be best-in-class to create an engaging, fair and honest dialogue with employees to promote the understanding of total rewards across all employee segments



Proactive

Mounting requests and a growing need to be on top of the issues makes it inevitable to pre-plan and respond to the changes in advance



Why initiate the transparency dialogue...

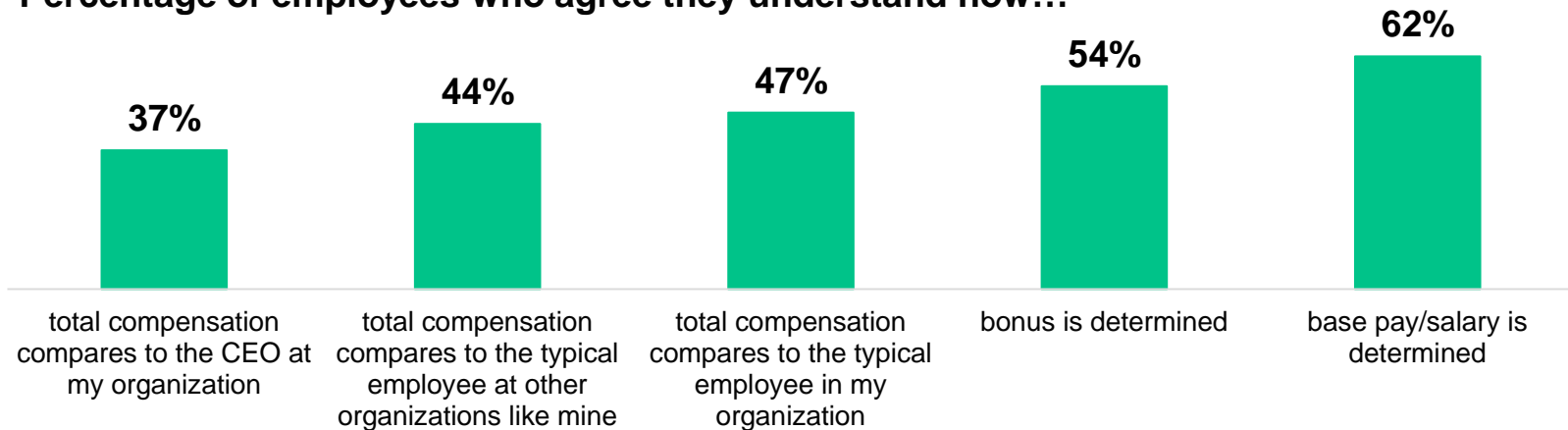
Changing Employee Expectations

- Low levels of employee understanding
- Retention is at risk
- Diversity trends and perceptions
- What will the future of work look like: changing working patterns

Changing Legislation

- CEO Pay Ratio
 - Gender Pay Equity
 - Gender Pay Gap Reporting
- And there is likely to be more coming down the line

Percentage of employees who agree they understand how...



Legislation is driving us towards greater transparency

Equal pay, gender pay, CEO pay, pay ratio

What is it?

Legislation varies around the world but pay equity and transparency is becoming an increasingly important dialog for companies to be compliant

Who does it affect?

In many jurisdictions, legislation is far reaching and impacts the majority of companies

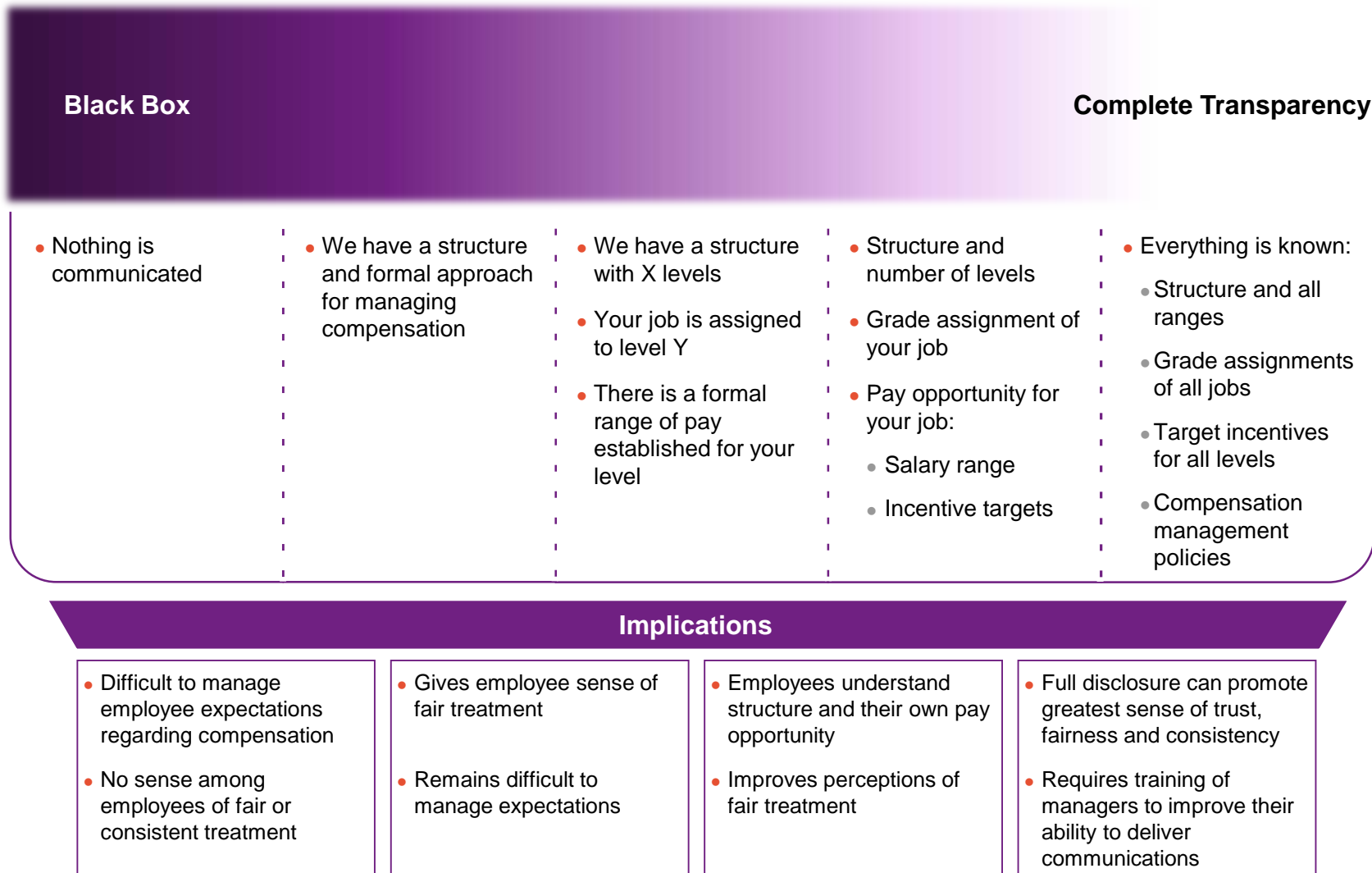
Why is it important?

It is a foundational element of compensation administration and compliance in the mature markets; talent landscape is changing globally. Talent is diverse and spread across geographies becoming increasingly accessible

Why else is it important?

There has been an upward trend in lawsuits; violations may lead to civil and criminal penalties, extensive investigation by the authorities in the Labour Department, and heavy settlement costs. Employer brand is tarnished

What does it mean to be transparent?



In closing

Keys to creating a competitive, effective compensation program

1. **Determine how compensation aligns with your strategy and culture.**
2. **Identify your key employee groups, their reward preferences and segmentation strategy.**
3. **Prioritize pay design.**
 - To ensure external pay equity, carry out comprehensive benchmarking but focus on critical roles.
 - To ensure internal pay equity, establish a global job-leveling system and salary structure.
4. **Revisit criteria for merit pay and pay for performance.**
 - Adopt a more holistic view of performance.
 - Evaluate a broader set of performance dimensions
 - Go beyond individual performance considering the past and include factors such as team goals and potential.
5. **Ensure manager education and advocacy**
 - Equip them with training, tools and technology to make effective compensation decisions and have effective compensation discussions.





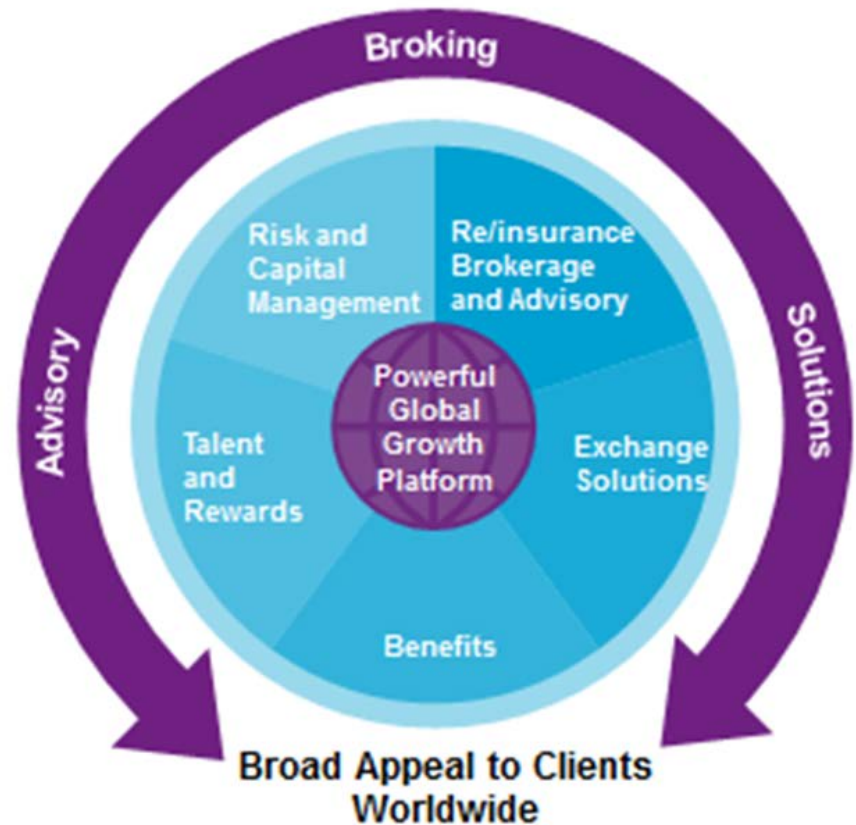
In a constant struggle for top talent

...

a credible, competitive
compensation program can mean
the difference between attracting
and retaining top talent or
settling for leftovers.

Willis Towers Watson: A Comprehensive Offering

Thank You!!!



Willis Towers Watson 

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