

Employee Compensation that Encourages Performance

By Kate Greene, SPHR

The strategy my neighborhood kids use to get customers for their lemonade stand is not unlike what many employers use to get employees. The kids scream “35 cents a glass” over and over, louder and louder. Would they have more success if they used signs, knocked on doors, yelled in a more even tone of voice, sold from a rolling wagon, etc.? Similarly, employers that advertise \$8.00 an hour, over and over, may not get applicants or results they require. Better results come from compensation strategies that align company and employee performance goals. Establishing wages that will both attract employees and provide contain labor costs starts with careful evaluation of internal and external factors to establish fair pay ranges that reward performance.

Recently a client asked how to best compensate his employees. The response, it depends. Compensation is a complex issue requiring careful consideration and research regarding many factors. The design of your company compensation structure can send a very strong message regarding what you expect from employees.

Many authors have written on this subject and a lot of research and compensation theories/plans have been completed. When working with a small to mid-size employer to create a compensation plan, I recommend following a few central principles. These are:

1. Keep it Simple

Pay structures needs to be easy to communicate and understand. Complicated formulas that weigh a large number of variables and have many inputs do not send a clear message – business goals get lost in the measurement and calculation.

2. Create a System for the Entire Organization

Of course not everyone should be paid the same or have the same benefits, however a process needs to be established for all levels of the organizations. Too often compensation plans stop at executive levels of management or bend easily. Without a system for determining raises and bonuses at every level, it is too easy to make decisions which break internal consistency. This opens a company to pay compression problems and possible lawsuits.

3. Align Pay With Company Goals

At an individual or company level, compensation sends a very strong message regarding what results are important to the organization. If customer loyalty and profit margin are the key determinates to profitability, then these should be included in the bonus or commission structure.

4. Compensation Encourages Employees to Look at the Big Picture

Individual incentives to perform communicate the importance of specific results. Rewarding for team or company wide goals widens the scope of what employee consider important. When meaningful, incentives tied to group results or profitability margins encourage loyalty, cooperation and get employees to look beyond just their function or department.

5. Stay Abreast of the Local Wage Market

Understanding the compensation marketplace and creating fair total compensation packages is worthwhile to all employers. Doing so ensures minimized turnover and saves time and money when filling openings when they do occur. Additionally, keeping tabs on the market allows you to be proactive, adjusting to trends before facing competitive pay problems. Web

resources like www.salary.com or www.michlmi.org are available and provide one point of data. In considering survey data it is very important to consider the position descriptions, sample size, geographic area and methodology of calculating the wage levels.

6. Consider Total Compensation

A common pitfall is the wide spread tendency to separate the elements of total compensation. This thinking leads may lead to employees coming forward with external data from salary.com and telling you “The survey says I should be paid more - I need a raise.” Beyond geographic differences, it is important to make certain that the salary data is comparing the same components that make up total compensation, which may include:

- Base pay – hourly, weekly, or monthly wage.
- Short term incentives – Often not cash, these are offered to individuals or teams, typically rewarding the accomplishment of a defined task or performance level.
- Long term incentives - offered to individuals or teams, typically rewarding overall company performance.
- Other cash compensation - such as allowances
- Benefits – health insurance, work breaks, training, vacation/personal days, and company provided uniforms among others.
- Perquisites – “perks” often left out of total compensation, these include a wide variety of company discounts, memberships or assistance programs. An example of a perk is the Guinness Brewery’s policy that provides employees a monthly beer allowance, or a company which provides membership to a health or country club.

Employers and owners need to create organizations where excellent performance leads to competitive compensation for people throughout the organization. Without rewards, a company is planting seeds for high turnover, low productivity and long-term failure. However, to reward employees that are not performing saddles an organization with higher payroll costs and encourages poor performers to stay while discouraging the employees that go above and beyond expectations.

In the past, more traditional organizations had more narrowly defined jobs and career paths. The system, rather than the individual, made the largest impact on the success of the company. Today employers demand that many employees problem solve, interact with customers in innovative ways and utilize technology updates virtually weekly. This is especially true in small and mid-sized companies, where it is individuals and teams that create success or failure. An organization risks losing the people that make a difference if they fail to provide total compensation that recognizes the value of employee’s contributions.

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