

Pay, Performance, and Productivity: How to Use Compensation to Motivate and Make a Difference

SAP SuccessFactors 



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How important is effective compensation management in terms of motivating your workforce? Plenty.

Compensation has consistently remained one of the top five job-satisfaction factors considered most important to employees. At a time when budgets are tight, many companies are facing a serious dilemma: How can you reward employees in ways that encourage high performance and ensure retention, yet still hold steady on operational and payroll costs?

A well-designed compensation strategy that connects rewards and performance can benefit both employers and employees. Ideally, this strategy should create an environment that is a true meritocracy — a place where employees who get results are rewarded for their work. Sounds like something everyone would want, right? Yes, but a few myths can sometimes get in the way of bringing accountability into the process. Don't let the objections of a few stop you. The benefits are worth the effort.

To design a compensation strategy that connects rewards and performance, you should:

- **Focus on total rewards:** Individual compensation elements are structured as part of a broader strategy of total compensation. These rewards are uniquely designed to support both the organization and its employees.
- **Align company and individual goals:** Rewards are based on degrees of performance against defined business objectives of the company.
- **Rank talent accurately:** Front-line managers evaluate individual performance based on assessment criteria that's calibrated throughout the organization.
- **Get rid of Excel:** The benefits of a compensation management solution far outweigh the limitations of Excel.
- **Gain employee buy-in:** Frequent and informative messaging underscores a communication strategy to create awareness, understanding, and acceptance from employees.

Compensation can be the single biggest cost to an employer, representing up to 70 percent of annual operating costs. In 2011, 54 percent of employees indicated that compensation was very important to their job satisfaction.

Source: SHRM Research Report. 2011 Employee Job Satisfaction and Engagement: Gratification and Commitment at Work in a Sluggish Economy.



The Five Myths of Compensation Management — Exposed

Even within the most well-run companies, pockets of resistance or misunderstanding can pop up among managers who are ultimately accountable for bringing pay strategies to life. You may have heard some of these myths:

- **“All of my people are good performers or they wouldn’t be here.”** While this statement may be true, numerous industry reports confirm that companies improve performance — in terms of both revenue and profitability — when their compensation and rewards programs are clearly differentiated based on individual performance.
- **“The company met its year-end targets, so everyone should share the same rewards.”** There are times when spreading compensation rewards evenly across the organization is perfectly appropriate — for example, the sharing of team or profit-based bonuses. However, this type of “peanut butter” approach doesn’t work for rewarding your top performers. Actually, it can create retention problems for these high-value employees.
- **“I can’t afford to discourage or disengage anyone on my team with no pay increase. I’m short-staffed as it is.”** Diverting well-earned rewards from top performers is the disengagement risk you should worry about most. Holding a frank conversation with an underperforming employee who’s receiving a minimal pay increase may be challenging. However, these conversations are an essential part of a compensation strategy that rewards results.
- **“I know some people talk about confidential pay issues, and I don’t want the word to spread.”** When employees clearly understand how their performance will be evaluated and rewarded in a transparent way, they’re less likely to have misgivings about a compensation program.
- **“I don’t have enough insight to differentiate performance.”** Managers need factual and relevant feedback, observations, insight, and data to make fair decisions about pay. Getting quality information like this can be difficult and time-consuming, especially when working with paper or spreadsheets. An automated compensation solution makes it easier for managers to make sound pay decisions based on a complete picture of employees’ performance.

Attracting, motivating, and maintaining a productive workforce requires more than equitable salaries and wages. Don’t let these myths prevent you from moving toward performance-based rewards. Effective compensation management, as part of an integrated performance management process, can engage employees, ignite better performance, improve execution, and ensure retention of the true top talent. You can dispel these myths easily with a few simple steps: a focus on total rewards, the alignment of goals, appropriate calibration and differentiation, the right technology, and good employee communication.



Focus on Total Rewards

An effective compensation strategy must be about more than base pay. To best support the strategic goals of the organization, a total rewards framework should include monetary compensation alongside non-cash elements such as career and professional development. After the right mix of cash and non-cash rewards has been determined, a budget must be allocated to encourage the right behaviors, deliver high-perceived value to employees, and improve return on investment.¹

The idea is to motivate the workforce to deliver superior results with a mix of:

- Base-pay increases
- Short-term incentives, such as individual or team bonuses
- Discretionary awards, such as spot bonuses
- Equity awards
- Long-term incentives, such as long-term cash plans
- Profit sharing

This winning strategy works because it offers top-performing employees what they are looking for, while delivering productivity, engagement, and high performance to the organization.²



You must show employees “what’s in it for me.” This means tying together the benefit of the job, the culture, their colleagues, and the company’s mission and its values, as well as total rewards. But total rewards are the most immediate and visible element to employees.

Source: Bremen, John and Sejen, Laura. Advancing Total Rewards & the Employee Value Proposition. WorldatWork. 2012.

1. Towers Watson. The Talent Management and Rewards Imperative for 2012 — Leading Through Uncertain Times. The 2011/2012 Talent Management and Rewards Study, North America.

2. Bremen, John and Sejen, Laura. Advancing Total Rewards & The Employee Value Proposition. WorldatWork. 2012



Align Company and Individual Goals

Linking performance and compensation connects two important concepts:

- How employees and departments are performing
- How the company rewards accomplishments and results

Most employees get it. There should be a connection between how a company performs and how employees are compensated. The connection between these two points is goal alignment. As top-level strategic goals are established, managers should share (or “cascade”) those targets down to the individual employee level. Cascading ensures that the day-to-day work of employees is aligned with overall company goals.

Establishing individual goals gives managers and employees a chance to discuss how performance will be evaluated. This tactic provides a significant opportunity to set clear performance expectations. What’s the difference between meeting and exceeding expectations? This is the chance to have that conversation and to set the bar.

By the way, compensation managers also benefit from this process. Aligning goals and bringing line managers into the conversation reduces the burden on HR, as well as providing better visibility to avoid mistakes, improving results, aligning budget compliance, and reducing overall cycle times.³

Research shows that companies with higher standard deviations in compensation have 15 to 20 percent greater performance when measured by revenue and profit growth.

Source: Harris, Stacey and Jones, Katherine. Total Rewards as a Strategic Talent Management Tool. Bersin & Associates. May 2011.



3. Bersin, Josh. Enterprise Compensation Solutions: The Next Wave in Integrated Talent Management. Bersin & Associates. January 2009.



Rank Talent Accurately

Doing less with more is simply business as usual today. Most annual merit-increase budgets remain in historically low ranges, and everyone is trying to use these limited resources to reward top performers. Ranking talent accurately balances these conflicting needs. Identifying and segmenting top, average, and low performers takes work and requires clear-cut, objective data. However, the results are worth it (see the callout).

How can you be sure that one manager's top rating is the same as another manager's? That's where calibration comes into play.

Employees' individual results are comprehensively calibrated against their peer group and evaluated on defined criteria, including:

- Performance relative to objectives
- Job-scope delivery

- Demonstration of leadership competencies
- Living the company's values
- Personal development⁴

Using best-practice calibration techniques ensures that only the top performers are rated at the highest levels. Comments included in performance appraisals are more precise about performance instead of being general (e.g., "She's a good worker").⁵ Although differentiation and calibration may put front-line managers in the middle of delicate conversations with their direct reports regarding pay issues, the right training and data can prepare them to play their role.

COMPENSATION SHOULD BE SIMPLE, RIGHT?

There are many variables that go into evaluating employee compensation — too many for an Excel spreadsheet to handle well. Ideally, compensation in your organization should consider several types of data, including:

- External compensation market data
- Supply and demand of different talent segments
- Allowances for location and geographic variance
- Economic market conditions
- Corporate or organizational culture and conditions

Source: Harris, Stacey and Jones, Katherine. Getting Compensation Right: The Value of Compensation Analysis and Planning Tools. Bersin & Associates. April 2011.

4. Garr, Stacia. The Performance Management Framework: Evolving Performance Management to Fit the Modern Workforce. Bersin & Associates. May 2011.

5. Ibid.



Get Rid of Excel

Compensation planning is one of the most complex tasks facing the HR professional, but many companies still rely on Excel spreadsheets for compensation administration.

Handling complex and sensitive pay data this way poses limits and risks, such as:

- Data changes and errors hidden in formulas that could affect individual pay or the company budget
- Lack of security or version control
- Failure to comply with reporting as required by EEOC, OFCCP, or Sarbanes-Oxley

A better approach is a Web-based compensation management solution. The advantages of automation can bridge the gap between strategy and results.

Automating compensation makes it easy to:

- Tie rewards to performance: With increased visibility from compensation that's aligned with the performance management system, managers are more informed to make better, smarter pay decisions.
- Optimize your compensation budget: Build compensation budgets based on company performance metrics or KPIs, and ensure that managers stay within their assigned allocations by using flexible "what if" scenarios.
- Save time and cost while eliminating errors: When you eliminate your manual processes, you significantly reduce the possibility of errors. You also reduce cycle times significantly and make it easier to audit and meet compliance guidelines.



Offering transparency to total compensation, benefits, and rewards will serve companies well by giving a clearer picture of the employee to their manager and providing the employee with an understanding of the scope of true benefits accrued from the organization.

Source: Harris, Stacey and Jones, Katherine. Total Rewards as a Strategic Talent Management Tool. Bersin & Associates. May 2011.

Gain Employee Buy-in

Your company's compensation program may initially run like a well-oiled machine, but even the most structurally sound programs need continual reinforcement. For starters, managers and employees both benefit from frequent communication regarding compensation. Let's face it — every employee thinks they are an expert at evaluating how their base pay compares with the external market. Compensation management is a complex business practice — part art, part science — and your compensation strategy may fall short if it's not communicated accurately, honestly, and often.

Most employees take a keen interest in finding out how the various elements of a compensation program come together to reward their performance. Research shows that employees have a more favorable view of programs they understand. Improving your communications efforts can have a greater effect on program utilization and satisfaction than making programs richer — and at a much lower cost.⁶

Your employees should be able to have the same view of their compensation, corporate benefits, bonus history, training, and other monetary and non-monetary rewards, that their managers have.⁷ An automated solution can provide both managers and employees with the visibility needed to communicate about compensation effectively.

6. Towers Watson. The Talent Management and Rewards Imperative for 2012 — Leading Through Uncertain Times. The 2011/2012 Talent Management and Rewards Study, North America.

7. Harris, Stacey and Jones, Katherine. Total Rewards as a Strategic Talent Management Tool. Bersin & Associates. May 2011.



Conclusion

Successful leaders understand that to succeed in today's economy but to win the war for talent, organizations must not only reach but also maintain the highest levels of employee motivation, engagement, and contribution.

Information is power. Leaders rely on accurate compensation data and analytics to help them effectively — and fairly — evaluate, reward, and recognize their employees. Yet, even with today's technology tools, it can be difficult to provide a true picture of the entire total rewards package provided by an organization. Managers need to be able to see the entire compensation and reward history of the employee in one consolidated place.⁸

It's up to HR to answer the compensation call. Start by developing a total rewards strategy to move the business forward, devise compensation management practices that are fair, square, and equitable, and power your entire talent management strategy — including compensation — with SAP SuccessFactors HCM Suite.

8. Ibid.



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