



Leadership Pulse

Pay for Performance

Research Report on big picture results produced by Sibson, which was our partner for this particular Leadership Pulse study.

On the next pages you will find a report done by Sibson, Inc. They partnered with the Leadership Pulse to conduct a study on pay for performance. They also did this same study with 2 other samples. This report combines all the data to provide you with an overall summary of the findings on this topic.

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STATE OF PERFORMANCE MANAGEMENT and Implications for Pay for Performance

Findings and Observations from Three Key Studies

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Focus of Our Webinar

This webinar will provide an overview of:

- Compelling data on perceptions from HR professional and line managers about performance management and pay for performance (P4P).

The data is from three sources:

<p>State of Performance Management 2010 <i>conducted with</i></p>  <p>WorldatWork The Total Rewards Association</p>	<p>Sibson's Real Pay for Performance Study</p>  <p>SIBSON CONSULTING A DIVISION OF SEGAL</p>	<p>Performance Management Pulse Survey <i>conducted with</i></p>  <p>leadership pulse</p>
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➤ We will also describe:

- Steps your organization can take to improve the effectiveness of its performance management processes
- Issues and best practices in performance management and implications for P4P

Information on the Studies

State of Performance Management Survey

- Conducted jointly by WorldatWork and Sibson Consulting in May/June 2010
- Surveys sent electronically to WorldatWork members, and 750 responses were received, primarily from senior-level HR professionals

Leadership Pulse Survey

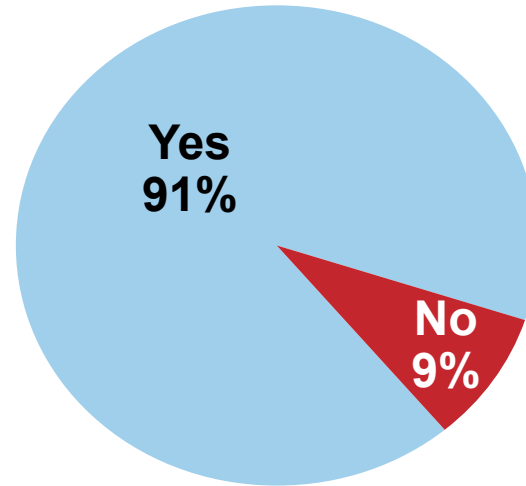
- An online survey among line managers to understand their view of performance management and relationship to pay in their companies
- Received 470 responses from senior leaders in diverse industries

Pay for Performance Study

- Conducted an online survey of 130 companies and detailed interviews with 30 participants to gain input on best practices in pay for performance linkage
- Study conducted between March 2010 and July 2010

Some Form of Performance Management Exists in Most Organizations

Does your organization have a formal performance management program?



Simply stated, the PERFORMANCE MANAGEMENT process includes:

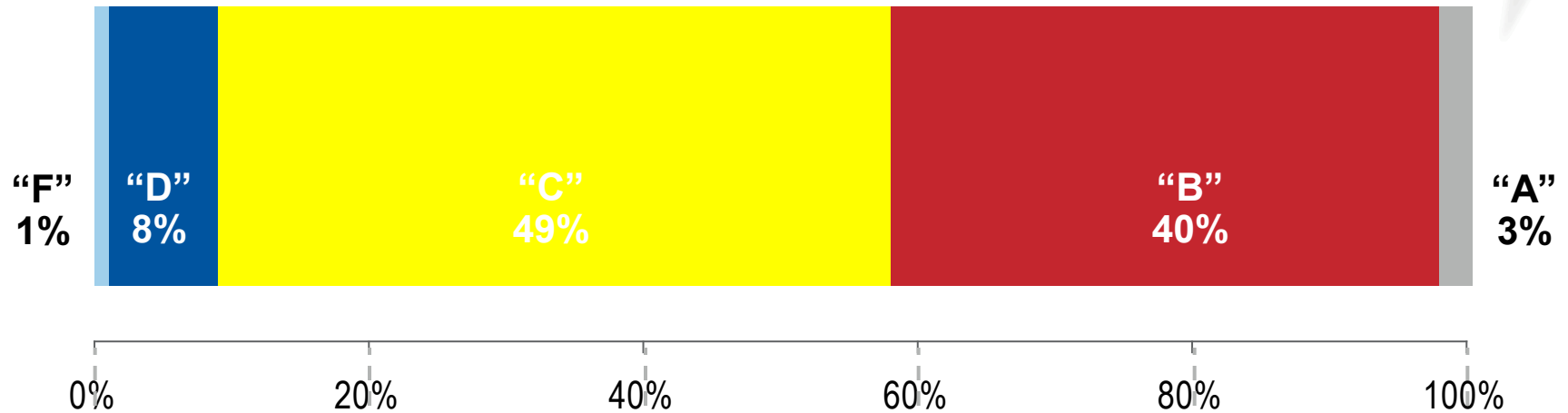
- setting expectations,
- evaluating results,
- providing feedback,
- conducting formal or informal discussions,
- communicating the evaluation and link to rewards

The Top 3 Desired Outcomes for Performance Management

Top 3 desired results of the performance management program	% Selecting
Differentiated distribution of rewards based on individual performance	66%
Greater individual accountability	54%
Talent development	46%

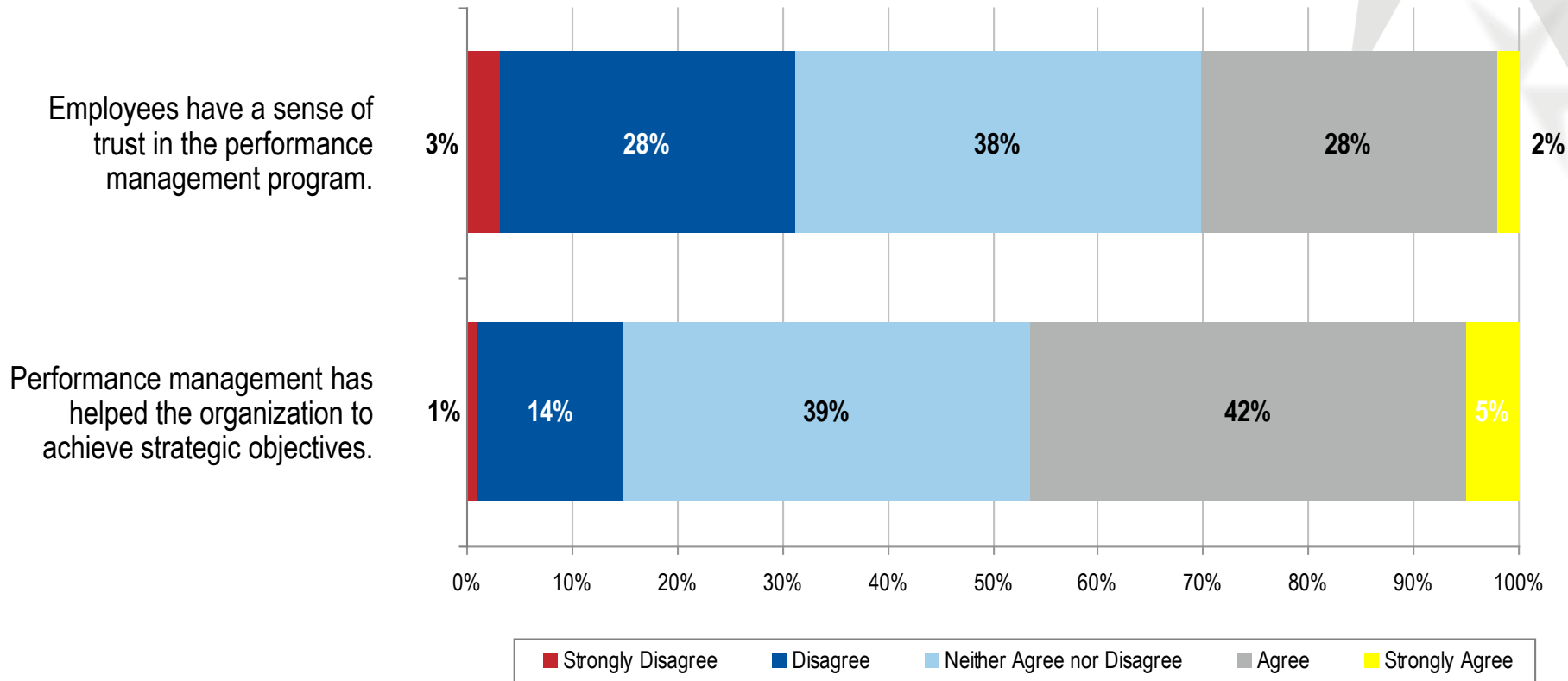
Assessments Indicate Programs May Not be Making the Grade on these Goals

Overall, what letter grade would you give your organization's performance management program's ability to achieve the desired results?



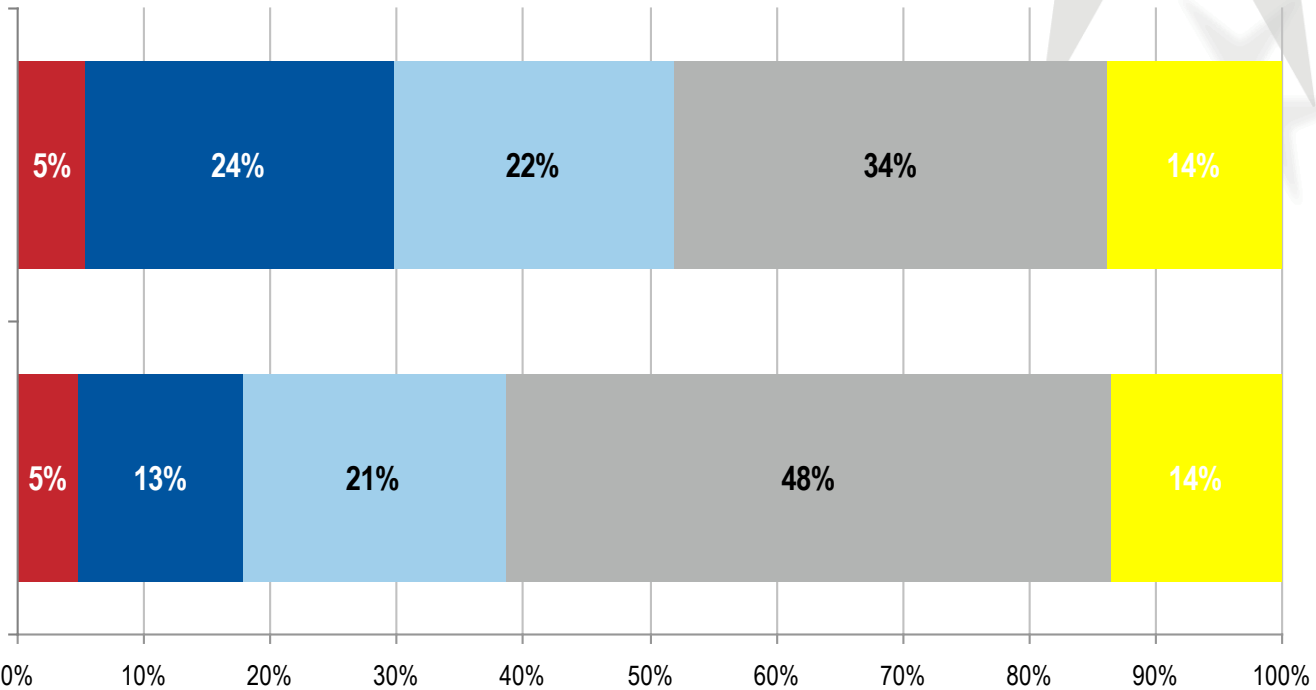
➤ Is a "C+" sufficient? What would be different if you had a B or better?

Sense of Trust and Effectiveness Mixed



And Business Leaders Agree with this Assessment

The way my company links pay with performance is fair and effective for all employees



Leaders Cite the Following Key Issues in Performance Management Processes

“Incentive goals that aren’t calibrated well for difficulty so some receive bonuses for doing their daily job while others have stretch goals.”

“Forced rankings and highly structured formulas which must be followed to the letter and allow little/no room for judgement.”

“Secret processes causing uninformed employees to feel disgruntled, often due to ignorance and assumptions, rather than actual injustice.”

“Failure to hold people responsible and accountable for their own performance.”

“Conflict-avoiding behaviours that lead to not giving feedback to people or dealing with poorer performers.”

“Poor quality, ambiguous goal-setting and the tendency to then manipulate goals to reduce or increase performance ratings”

“Rewards for just the ‘what’ at the expense of the ‘how.’”

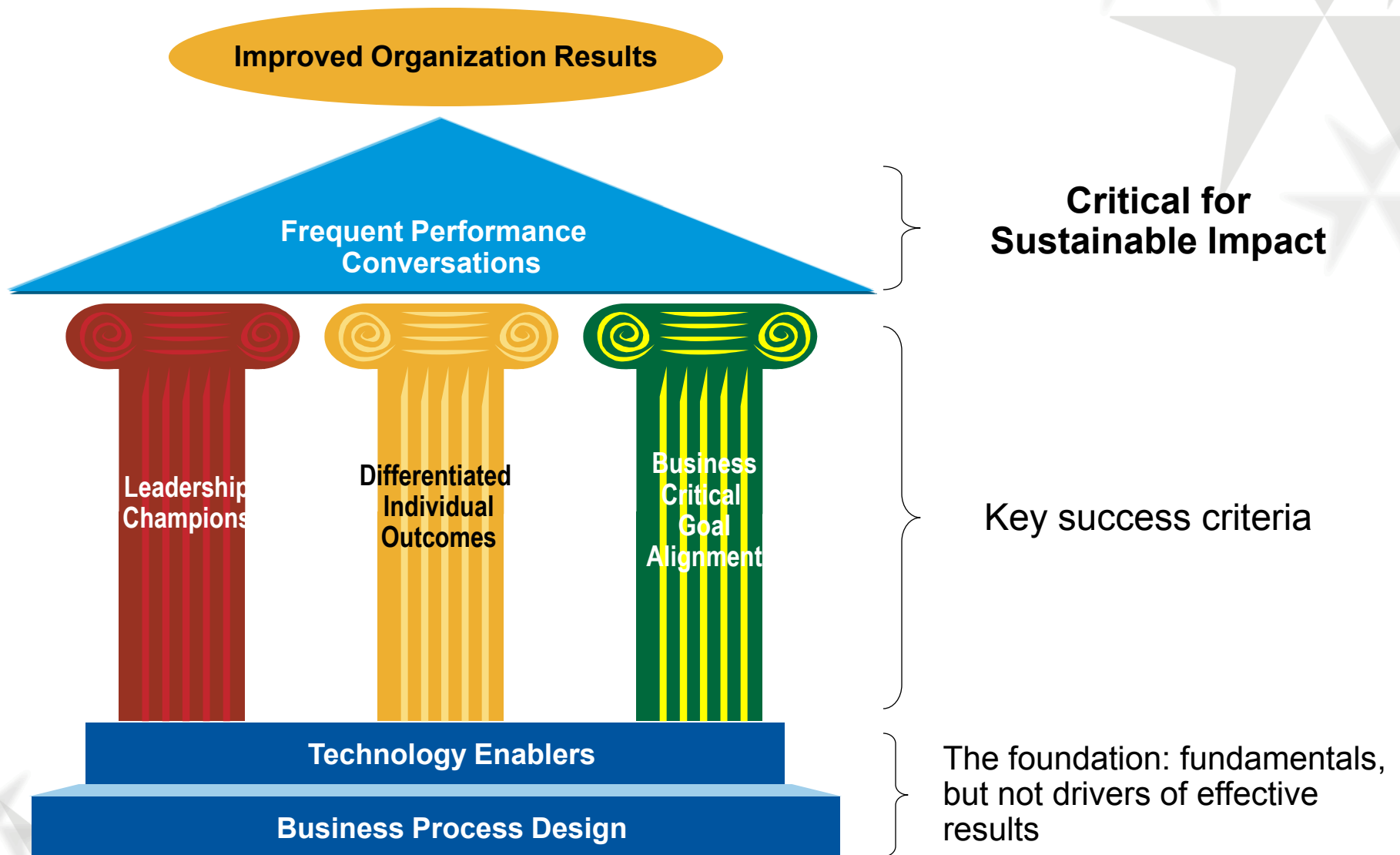
“When pay for performance becomes an expectation.”



Survey Results Confirm these Key Issues

Top 4 challenges of the performance management program	% Selecting
Managers lack the courage to have difficult performance discussions with employees	63%
Viewed as an “HR process” instead of business-critical	47%
Poor goal setting	36%
Rewards not linked to performance	25%

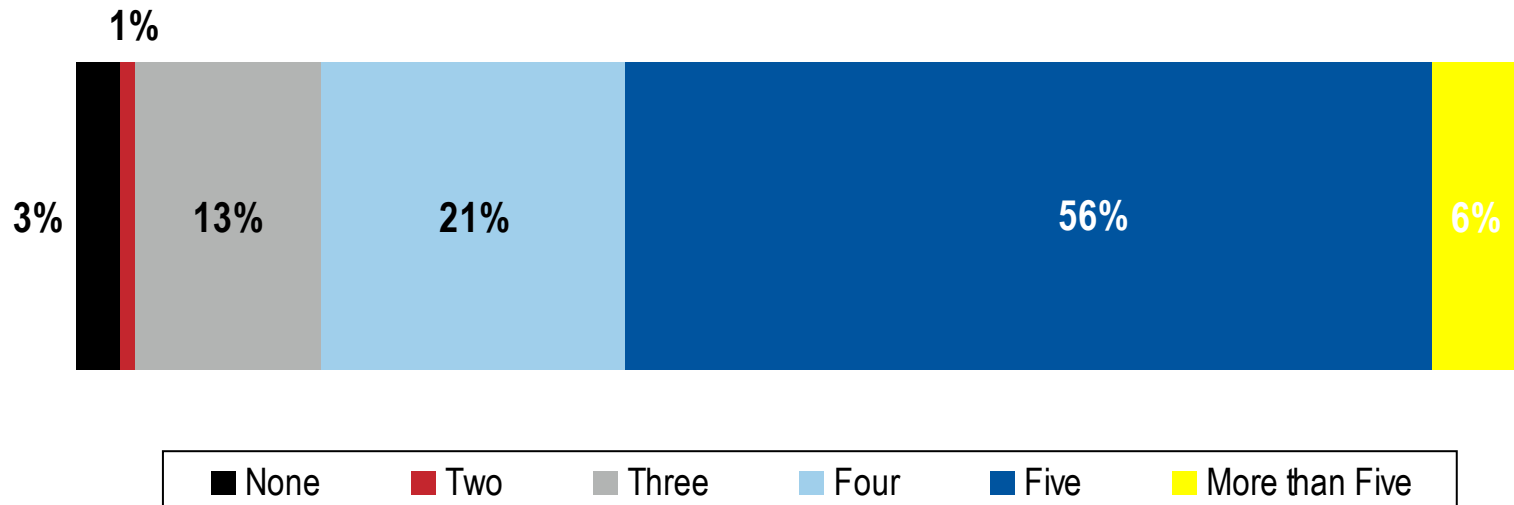
So How Do We Improve Performance Management?



It's Not About the Number of Ratings



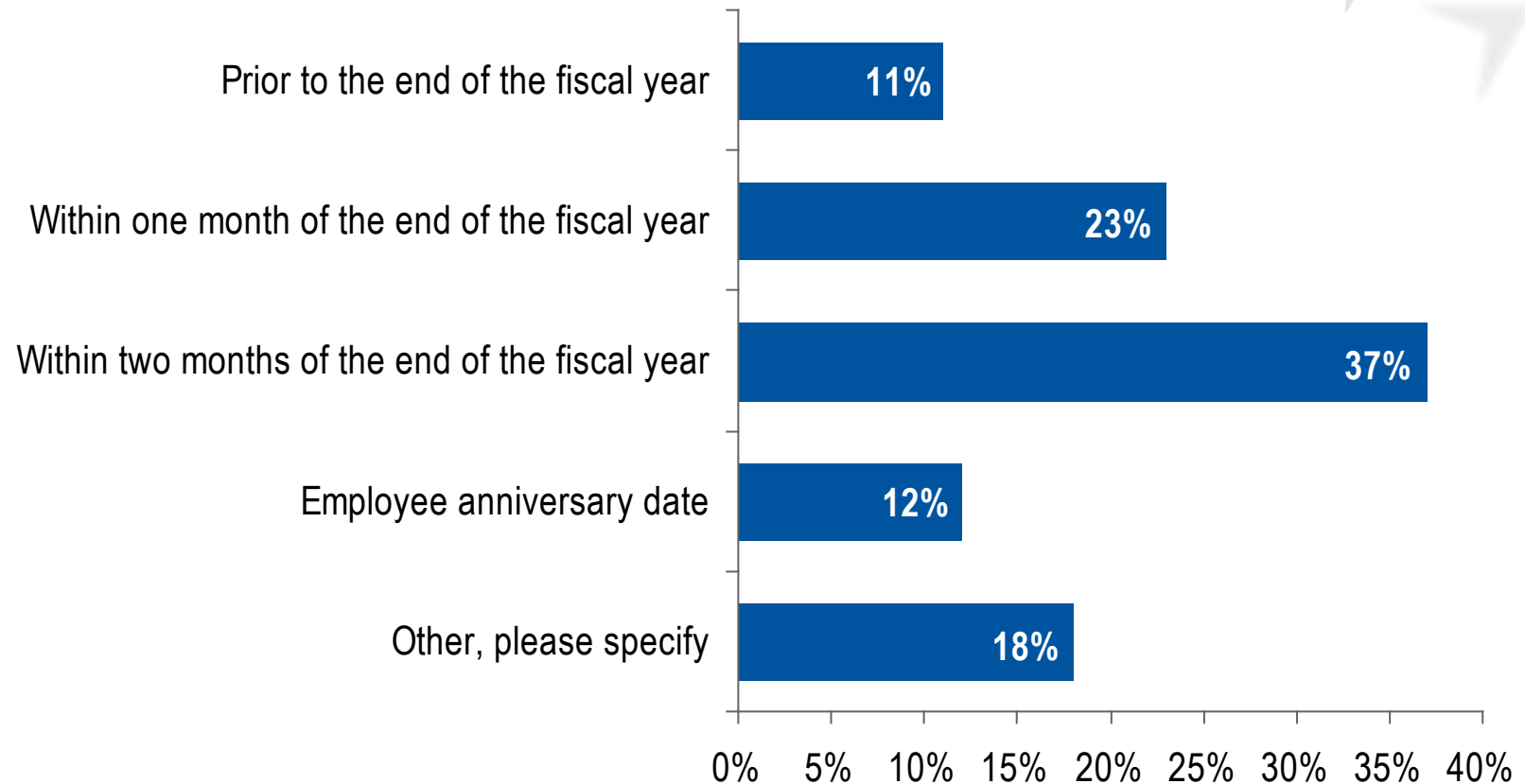
- 5 performance categories most prevalent, but other options can work
- Clear definitions and calibration on their meaning are a key to success



Or the Timing of the Performance Review



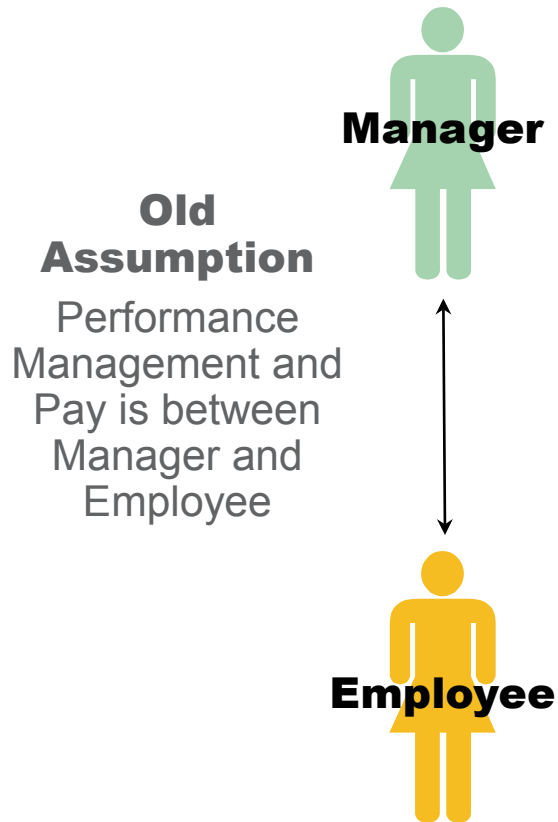
- Timing of performance review varies
- Ensure quick alignment with outcomes and calibration on ratings



It's About Ensuring Trust Among Employees and Managers

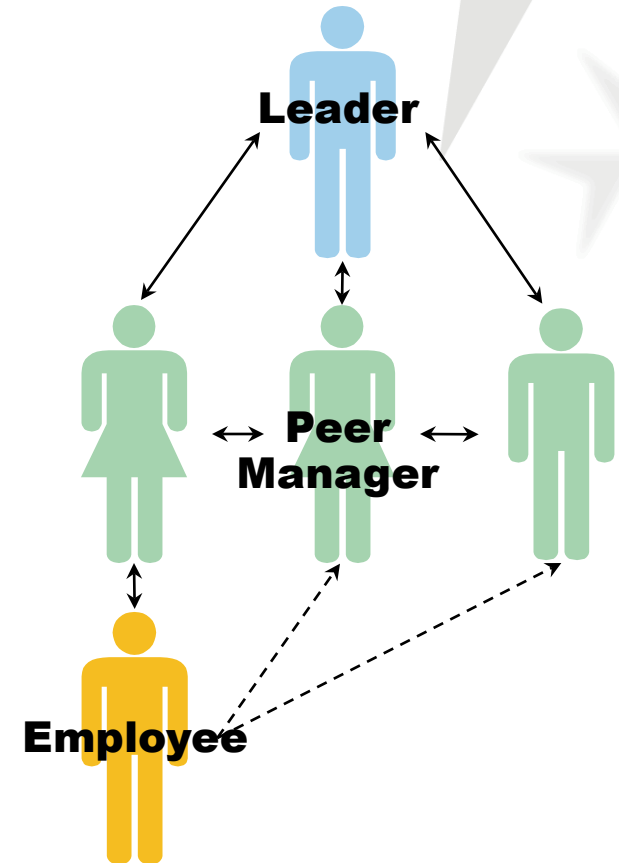


LOW VISIBILITY



New Assumption
These decisions are too important to be made individually without visibility

HIGH VISIBILITY CALIBRATION



Visibility of ratings and pay actions is driven through calibration among peer managers to improve transparency and reinforce expected standards.

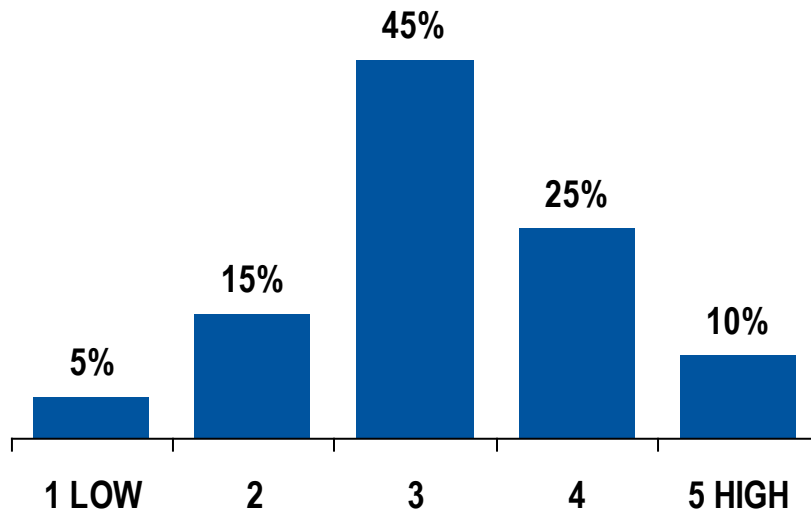
Acknowledge Performance Differences



- Trend is away from a “forced” distribution
- Trend is towards a target distribution linked to organizational performance
- More organizations using calibration or audits to make actual ratings visible

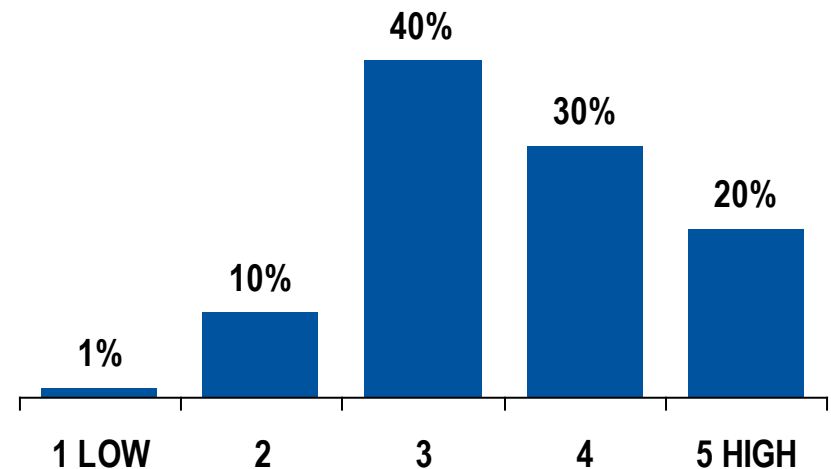
EXAMPLE

TARGET RATINGS DISTRIBUTION



Have a Target Distribution

ACTUAL RATINGS DISTRIBUTION



Make the Actual Distributions Visible to Leaders

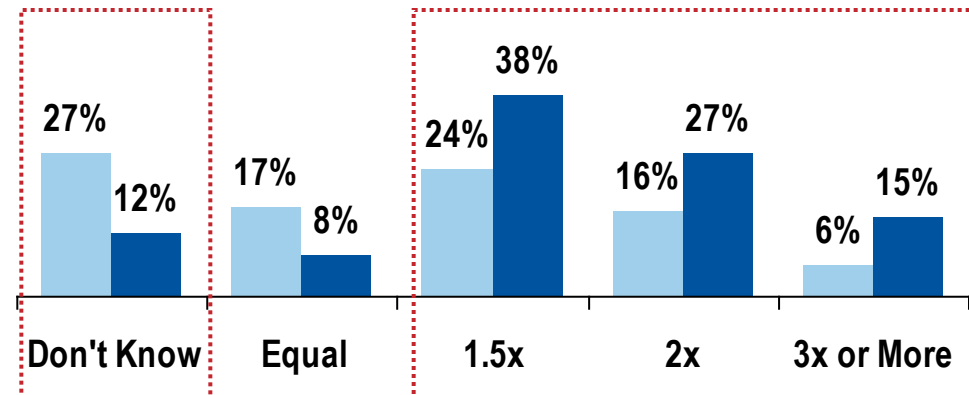
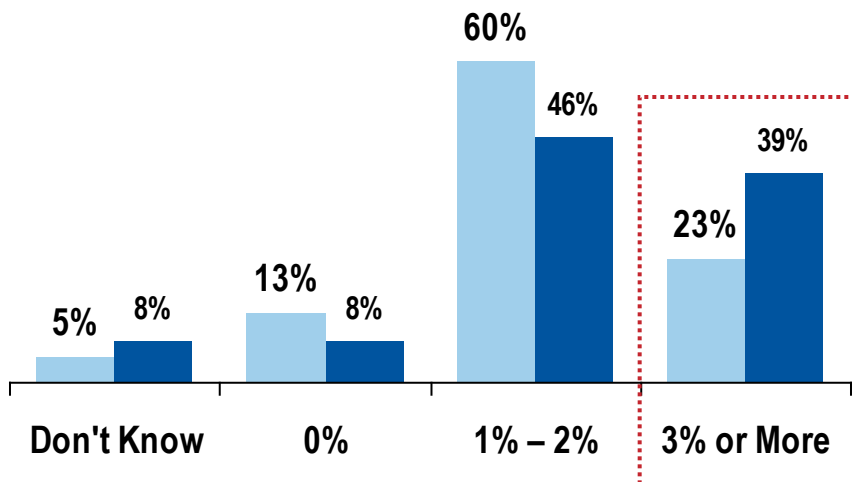
Track and Communicate Metrics on the Outputs



“Best Results” organizations are able to realize more differentiation and have a better understanding of how much pay differentiation is achieved for high performers, particularly with annual incentive plans

**Greater Merit Award
(Last Performance Cycle)
High Performers vs. Average Performers**

**Greater Annual Incentive Payout
(Last Performance Cycle)
High Performers vs. Average Performers**

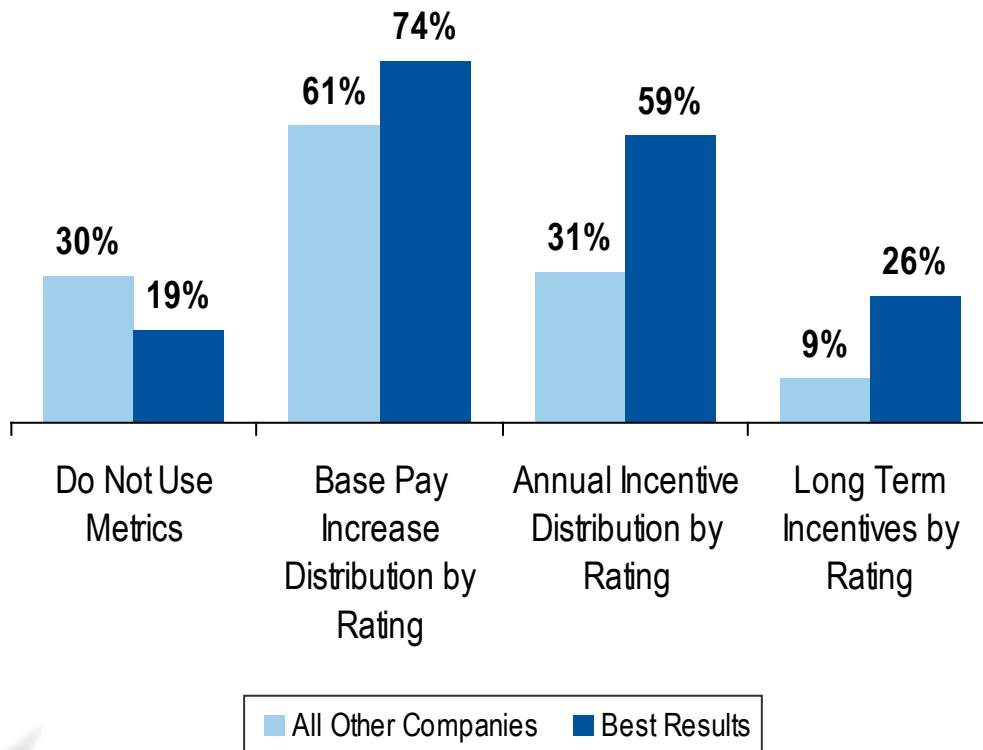


■ All Other Companies ■ Best Results

Provide Metrics to Track Pay for Performance



METRICS USED TO TRACK PAY FOR PERFORMANCE EFFECTIVENESS



Participant Quotes

“We use metrics that are made public to leaders to help track our effectiveness on pay for performance execution.”

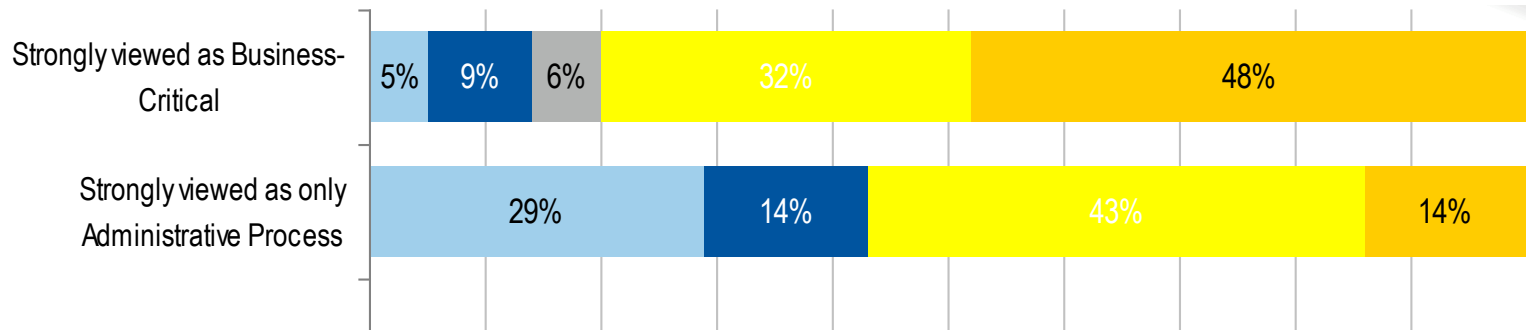
“We used to not track much of anything, now we track it and make it visible. It holds leaders accountable to make the right decisions.”

Viewing PM as Business Critical Also Drives Better Outcomes

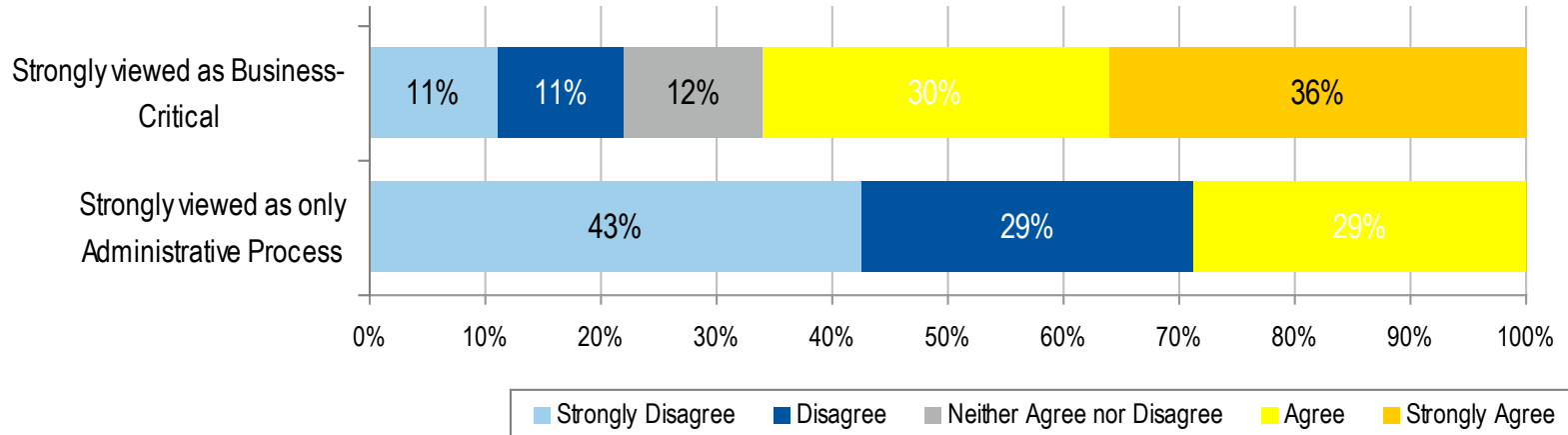


Please rate the extent to which you agree/disagree with the following statements.

Managers focus on having effective performance conversations and not just on completing the forms.



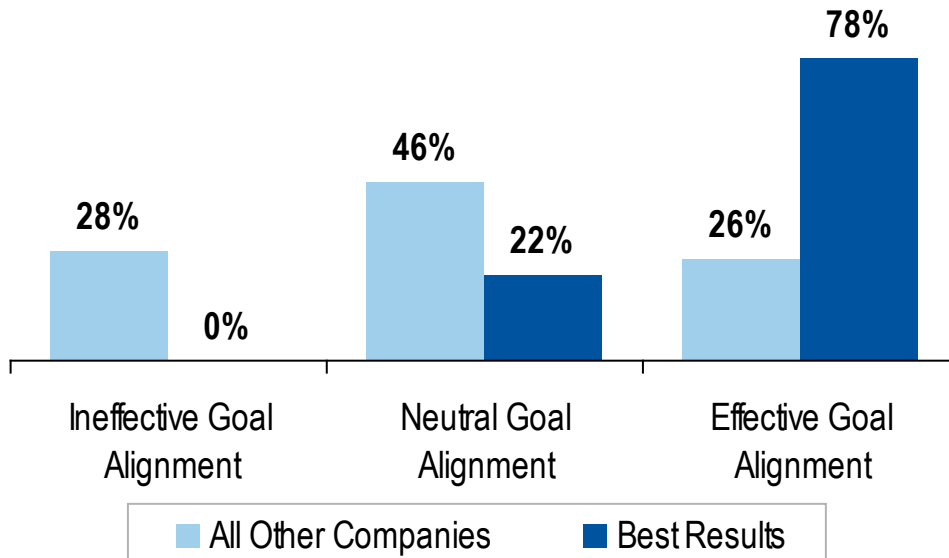
High performers receive significantly differentiated pay increases from average performers.



As Do Aligned Goals and Acknowledgement of Performance Differences



EFFECTIVENESS LEVEL OF GOAL ALIGNMENT



Participant Quotes

“Company and division goals are published on our intranet so that all employees have a guide when setting their individual goals.”

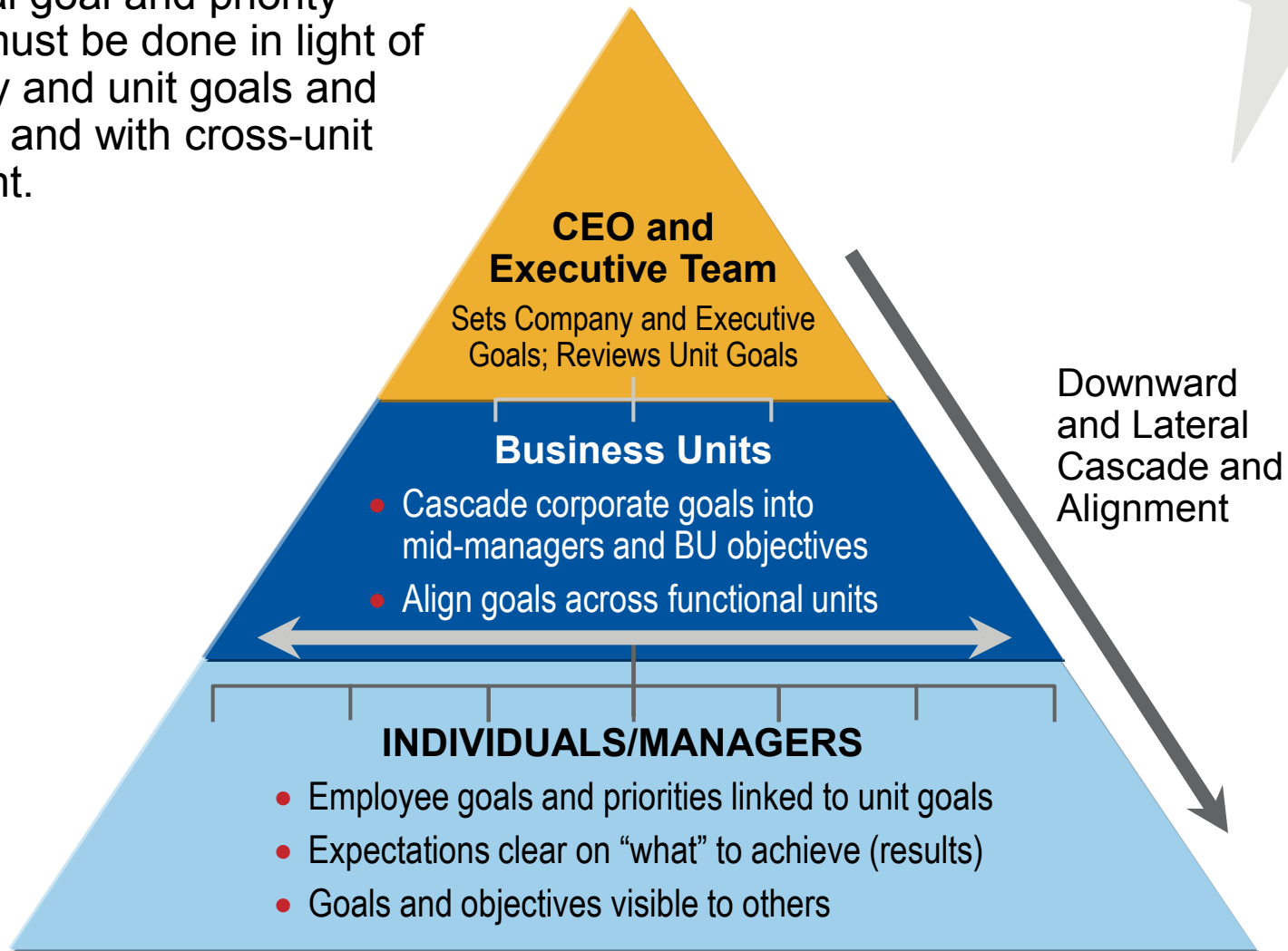
“Our management team develops their goals first and shares them with each of their direct reports. That continues with all supervisors expecting to share their goals with their direct reports.”

What you can do:

- Improve visibility of goal setting, have goals documented and transparent.

Align Goals Across the Organization

Individual goal and priority setting must be done in light of company and unit goals and priorities and with cross-unit alignment.



Define the Link to Pay to Performance— *Differs by Organization, Must Reinforce Desired Culture*



What are some of the ways it works?

1. Low base, high variable driven by individual success against goals
2. Mostly base, but base pay varies a good deal by performance, modest bonus driven by company, division, or unit results
3. Base ties to market, variable is main reward for individual performance, everyone gets options
4. Base varies with individual performance, group gain-sharing bonus
5. Large advance-from-within organization promotions are the main reward for performance

Participant Quotes

“We usually only have about 5% of our population identified as high performers so there is no debate with paying them more.”

“Our merit has been small but top performers get 2 or 3 times the average performers.”

“We use merit as ‘market’ and differentiate mainly with bonus.”

What you can do:

- Make the desired approach clear and transparent
- Reward achievement of critical success factors (both what and how)
- Measure and report on pay for performance alignment

Make Promotions Prominent



- Promotions should not be an entitlement, i.e., for years in a position or level
- Promotion is often seen as the biggest reward for performance
- Promotions are not only a huge reward, they send a message about who and what is valued

Participant Quotes

“Everyone understands that the biggest reward is a promotion, so we manage them like we do other rewards by having criteria and approval processes.”

What can you do:

- Budget and report on promotions like other aspects of pay
- Make part of talent reviews or calibration
- Require multiple levels of approval

Differentiate Based on Performance, While Managing To A Merit Budget



Stay Within Budget By Flexing Payouts According to Ratings Distributions

- Managers will tend to rate high if they think they can get their people more money—adjusting the merit increase targets based on performance distributions avoids this gaming
- A modest change in merit increases relative to the performance distribution maintains the desired budget

ACTUAL AND EXPECTED PERFORMANCE RATING DISTRIBUTION BY SALARY INCREASE

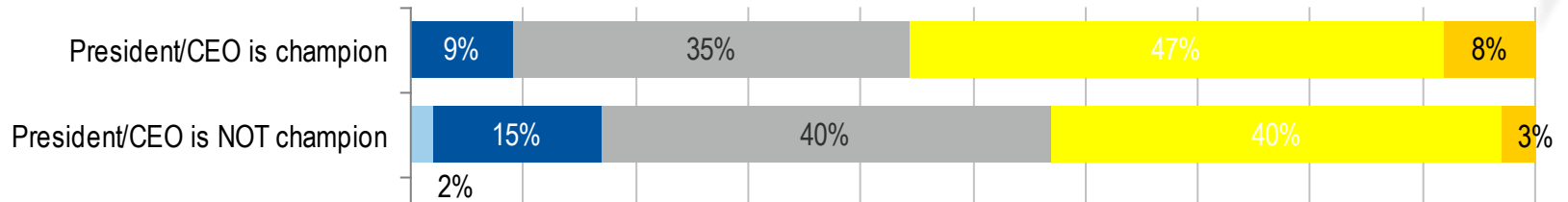
Rating	1	2	3	4	5
Expected Performance Distribution	5%	15%	50%	20%	10%
Budget Merit Increase	0%	2%	3%	4%	8%
Actual Performance Distribution	2%	10%	40%	32%	15%
Adjusted Salary Increase	0%	1%	2%	4%	6%

Ensure that Leaders Champion Performance Management, and Value of the Program Will Increase

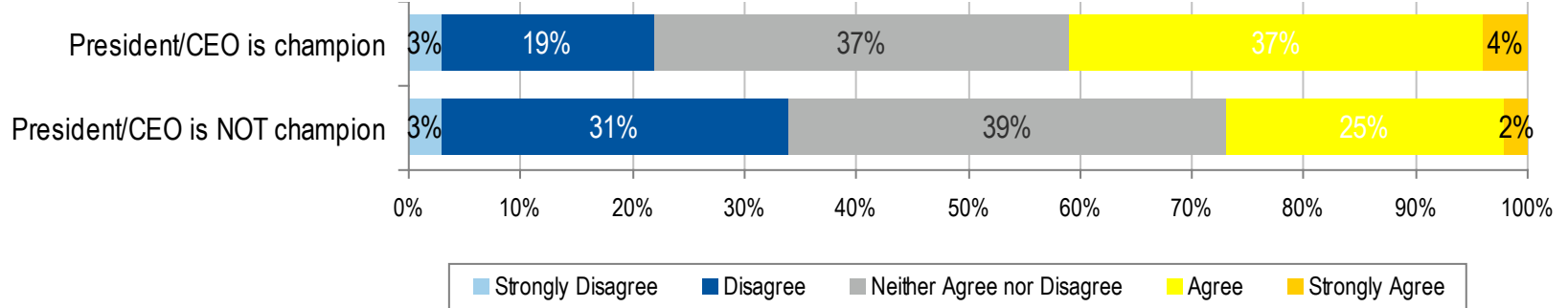


Please rate the extent to which you agree/disagree with the following statements.

Performance management has helped the organization to achieve strategic objectives.



Employees have a sense of trust in the performance management program.



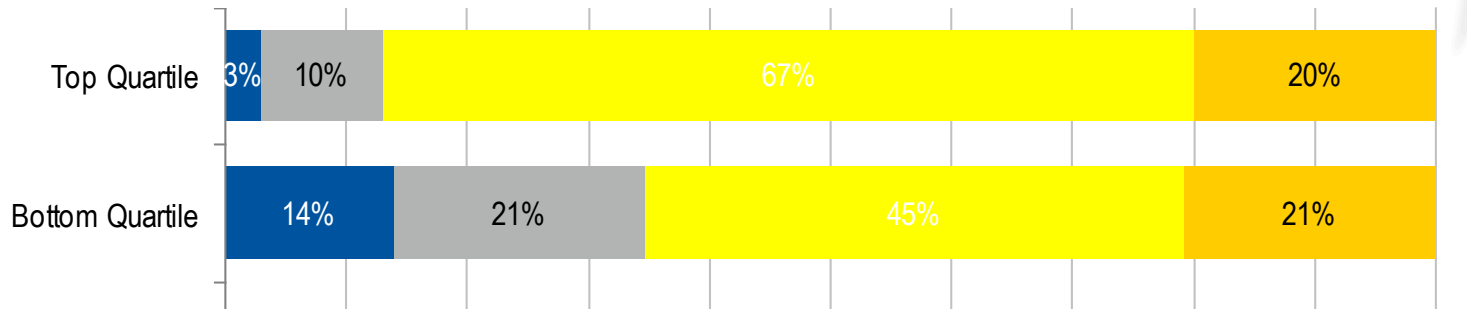
Top Performing Companies are More Likely to Have Support of Senior Management in the PM Process



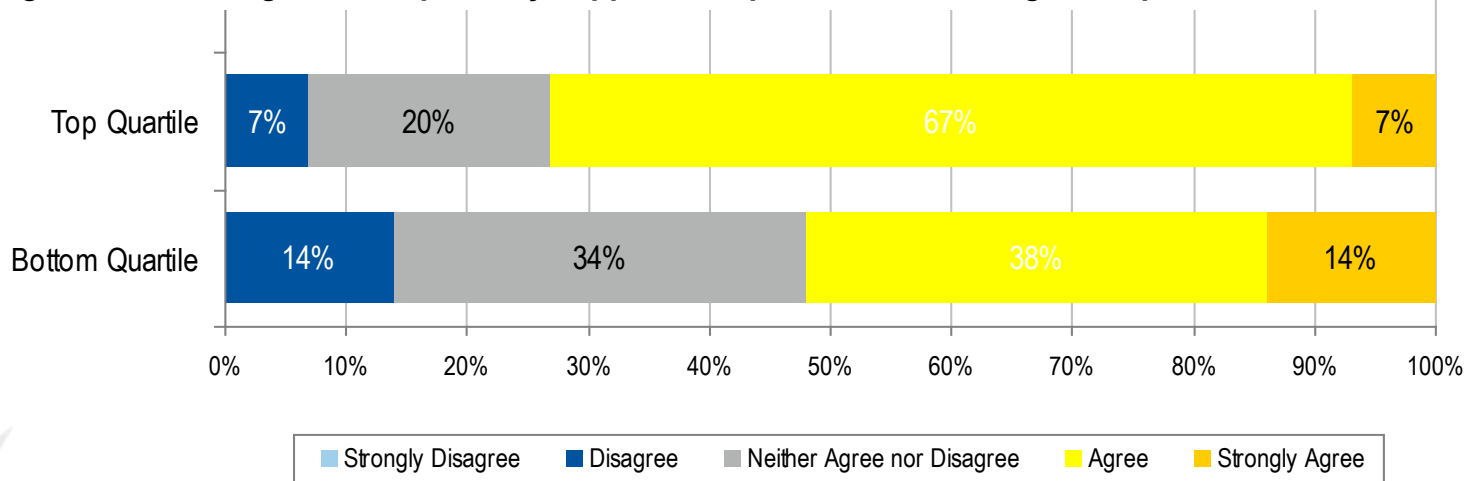
Please rate the extent to which you agree/disagree with the following statements.

TOP BOTTOM QUARTILE OF 3 YEAR TOTAL RETURN TO SHAREHOLDERS

Senior management in the organization publicly supports the performance management process.



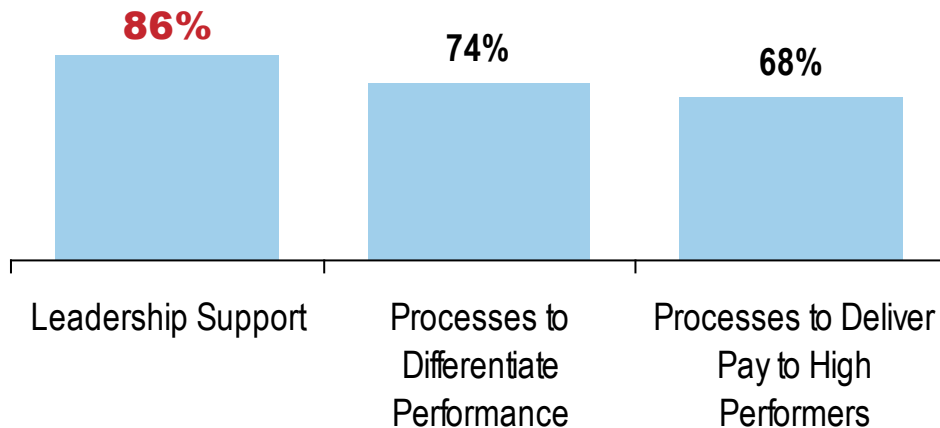
Senior management in the organization privately supports the performance management process



Leadership Support is the Catalyst for Real Pay for Performance



Leadership Support is the #1 factor that enables an effective pay for performance culture



Participant Quotes

“Our CEO has personal interest in performance evaluations. He does not hesitate to push back on pay arrangements if they do not reflect performance levels. This drives our senior managers to be directly involved with pay differentiation.”

“Our President does not encourage pay for performance, therefore, it doesn't happen.”

What you can do:

- Help leaders get it right for their own group: goal setting, evaluation, and differentiating rewards
- It does not start well in the middle, but does cascade down

Focus on Conversations

Improve Managerial Courage



Remember the greatest challenge

➤ **63% cited managerial courage**

Yet—

- Managers know who their best and worst performers are, and
- Many managers naturally want to give direction and feedback
- So, what gets in the way?
 - The difficulty of **bad** news
 - The difficulty of **good** news

What you can do:

- Design Performance Management to support management process
- Train managers to use regular conversations to build trust
- Balance company and individual needs

Build Trust Through Manager-Employee Interactions

Sibson's Five Conversations Used in PM training



CONVERSATION #1

- Recognize priorities, goals, styles
- Agree on relationship norms



CONVERSATION #2

- Understand Company's goals/objectives and requirements of the role
- Translate to actionable expectations given needs of the business and employee
- Discuss respective roles in delivering on expectations



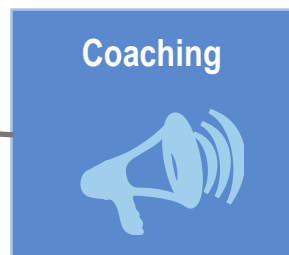
CONVERSATION #3

- Exchange performance information
- Plan for success



CONVERSATION #4

- Identify performance and development challenges
- Agree on potential actions

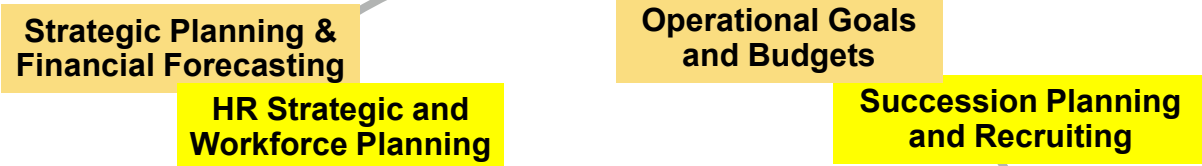


CONVERSATION #5

- Clarify personal development and growth goals
- Align goals with personal business realities



In Summary—Integrate and Align Processes



Illustrative Performance Management Process



Synchronizing the performance management calendar with other key processes ensures appropriate information (inputs and outputs) is available when making decisions / investments.

In Summary—Keep in Mind Seven Success Criteria

Effective Performance Management Requires

1. Leadership to not only sponsor but model appropriate behaviors
2. Goals and other performance criteria clearly defined and aligned across the organization
3. Regular and constructive communications to occur between supervisor and employees
4. Calibration to occur across the organization to reinforce fairness and equity
5. Answer to the question—“What’s in it for me?”
6. A process that is viewed as business-critical
7. Rewards and other talent management processes to be consistently linked

Seek TRANSPARENCY throughout the process.

Thank you!



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