

# REWARDING ORGANIZATION AND INDIVIDUAL PERFORMANCE WITH VARIABLE PAY

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**M**ost compensation systems are boring. Most compensation systems do not pay for performance. Few systems encourage commitment to the organization. And while they can send powerful messages to employees about the kind of organization they work for and the skills and behaviors it values, most of those messages -- and systems -- are uninspiring. In fact, they often inhibit organizations and employees from achieving their highest levels of performance.

Again and again, surveys point out employees are not motivated by current pay and reward systems -- in fact, they don't even believe their performance has any influence on pay!

## CHANGING BUSINESS ENVIRONMENT

Traditional compensation systems with grades, matrices, and annual reviews do provide a sense of control, order, and stability. The problem is we operate in a business environment where the only constant is change, where flexibility is mandatory, and where controlling must evolve to influencing.

This presents a distinct incongruity. Rather than having compensation programs in place that:

- Motivate individuals to improve performance and increase their skills
- Help control costs and improve productivity so the organization can compete effectively
- Attract and retain high-caliber employees from a shrinking labor pool . . .

We have systems that often do the opposite by not providing timely, meaningful rewards for achieving success.

## PAY FOR PERFORMANCE

But there are ways to use this changing environment to your advantage, to assure your programs are in tune with and support the needs of your organization and employees. Start by having programs that truly pay for performance and link your organization's success with individual success. That means part of all employees' pay must be variable -- contingent on performance and success.

This, of course, brings us to variable compensation. And let's start by defining what we mean by variable pay -- pay that varies with performance. Performance may be overall organization, unit/team, or individual.

For example, variable pay programs include:

- Profit Sharing
- Gain Sharing
- Group Incentive
- Recognition Award
- Individual Incentive
- Equity/Stock Award
- Lump Sum Bonus
- Key Contributor Award
- Project/Team Incentive
- Participative Peer Award

And, of course, there are numerous types of recognition plans such as paid sabbaticals, travel awards, merchandise, tickets to events.

While the definition of variable pay may be simple, its implementation is difficult. It's not just a question of designing some bonus or incentive plan; that's the easy part. It's getting to that point -- changing to a variable pay philosophy -- that's tough.

How do we make that change? How do we make a variable pay program effective and exciting?

## **MAKING VARIABLE PAY WORK FOR YOU**

Briefly, here are factors to consider:

- Make sure your program is integrated with your business strategy -- this is crucial to acceptance and support by top management. If you don't have the business plan, ask for it! Analyze it, understand it, and use it to develop your pay strategy.
- Design it to focus employee efforts on areas critical to organization survival and success by rewarding results employees can influence.
- Be sure the plan and the process reflect your culture and values. For example, don't use a gain-sharing plan if you're not willing to share information with employees or if trust is low.
- Make sure the program is cost-effective. If your company is squeezing out profit margins to survive, participate in that effort by maintaining or reducing fixed compensation costs. Consider paying salaries only to the range midpoint or market rate and provide bonuses to reward outstanding performance.
- Don't expect perceptions to change overnight. Traditional systems have been around a long time. Changing to a variable pay philosophy is not a short-term project.
- Be prepared to spend time and effort to train and educate managers and employees, alleviate their fears, and gain understanding, acceptance, and credibility for any new approaches.

- Do this through clear, ongoing communications. These messages must reinforce the link between the company's ability to achieve business goals and succeed in the marketplace and its ability to support an effective compensation plan.
- Don't be stingy. If you want outstanding results, pay outstanding rewards.
- Pay out as frequently as you can administratively. The closer the reward is to the performance event, the better it will reinforce performance. Good performance doesn't happen just once a year.
- Make the program important. Publicize it, promote it, market it. Make sure everyone knows and understands its importance to them and to the organization.
- Don't build unreasonable expectations. Be realistic and follow through with promises. Don't tell employees you'll pay for results and then give discretionary awards to select people who don't meet their objectives.
- Above all, inspire. Do whatever you need to do to get people excited and focused on improving individual and organization performance.

As the business climate continues to change, we need to find new ways to manage our human resources more effectively.

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