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Reward Programs: What Works and What Needs to be Improved

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Reward Programs:
What Works and What Needs
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What works when it comes to rewards? A simple question one might think, but its answer is quite elusive. Clearly, finding an answer is essential, particularly for those who are accountable for developing and administering reward programs. Thousands of research studies, journal articles and opinions exist on this complicated subject. Organizations have spent millions of dollars searching for answers, in the hopes that the latest promising reward programs, or their internal talent or external consultants, will help show them the way. Determining what makes reward programs effective is critical, in part due to the sheer size of the investment organizations make in their people, but also due to the expectations that organizations place on people to contribute to organization success.

The authors confirmed that effective reward programs contribute to overall organization effectiveness in a previous research study (Scott, Sperling, McMullen and Wallace 2003). The opposite is true as well. Ineffective reward programs can severely damage organization effectiveness. Beyond squandering financial resources, poorly designed and executed reward programs can compel talented employees to leave the organization and misdirect the effort of those who remain. The authors also found from another recent research study with WorldatWork that most organizations do not even formally evaluate either the effectiveness of their reward programs or the return on investment (ROI) of their reward programs (Scott, McMullen and Sperling 2006).

So, what *does* work when it comes to reward-program design and execution? And what are the key areas that need to be improved?

The study sought to discover what compensation professionals really think makes their reward programs successful. After all, these professionals are not only intimately involved in the design and administration of compensation programs, but also are a big part of the programs' success.

In pursuit of answers to these two questions, the authors didn't think a traditional, structured survey would afford fellow professionals in the field the opportunity to offer the type of information being sought. Most structured surveys ask multiple-choice questions, making it easy for participants to complete and provide researchers with data that can be easily quantified and tabulated. Unfortunately, structured questionnaires also tend to restrict the respondents' ability to express themselves by focusing the questions on what the researchers think is important.

The study gave compensation professionals an unrestricted voice and the freedom to relate what they think makes their organizations' reward programs effective as well as what needs to be improved. Instead of asking a series of multiple-choice questions, just two simple, open-ended questions were asked. And the questionnaire gave respondents plenty of space to respond at length. The research questions were:

1 | The most important characteristic or attribute that makes my organization's rewards effective is _____.

2 | The one or two key things my organization must do to improve our rewards systems are _____.

This attempt to obtain an unfiltered look at how compensation professionals evaluated their pay programs posed some risk for the researchers, including:

▪ What if open-ended responses required too much effort to answer or seemed to have little value; would busy compensation professionals bother to respond?

▪ Even if they responded, what would researchers do if their responses were so idiosyncratic or unique to their own companies that the research offered little insight into reward programs?

The authors' definition of rewards is a broad one, which includes monetary and nonmonetary rewards, as depicted in the widely accepted WorldatWork model (See Figure 1 on page 8).

RESEARCH PROCESS

While the survey's concept is simple, the following rigorous qualitative research protocol was followed:

1 | A conceptual definition of what constituted organizational rewards (as shown in Figure 1 on page 8) was adopted and included in survey instructions.

2 | The two qualitative research questions were formulated.

3 | A pilot test of compensation professionals was conducted with the Chicago Compensation Association (n = 26) and compensation professionals in the restaurant industry (n = 11).

FIGURE 1 WorldatWork Total Rewards Model

Figure 1 WorldatWork Total Rewards Model
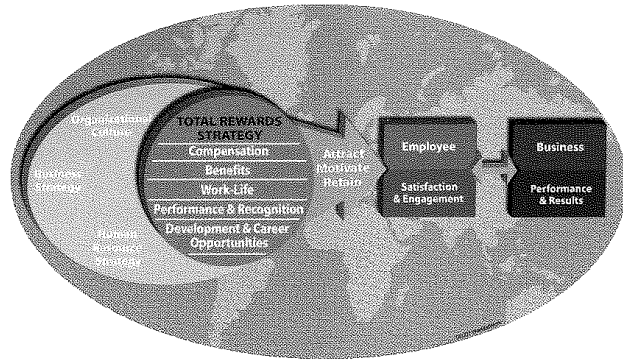
4 | An e-mail link was sent to a random sample of WorldatWork members who were invited to participate in the survey via the WorldatWork Web site. Useable responses totaled 461 from compensation and HR professionals.

5 | The five-member research team examined the narrative response data and, based on this review, identified thematic categories into which to group (or code) the responses.

6 | Two teams of two researchers independently coded the narrative responses. The few coding differences between the two teams were reconciled by the entire research team.

7 | The coded data were analyzed using basic frequency statistics and averages.

It is important to note that although qualitative data were collected from two open-ended questions, these data were examined systematically by five compensation professionals who have more than 100 years of combined experience in the field. Specifically, the categories for coding the data were derived from responses to the questionnaire, and the data were coded independently by two, two-person teams. The data were coded in categories which were grouped, where appropriate into larger data categories (defined as compensation themes). The number of responses for each theme and category are shown in Figure 2. Since responses were open-ended, it was not uncommon for single responses to be placed or coded into two or three categories. For example, a response from one participant about the key attributes that make the organization's rewards effective reads:

I would have to say the perception of "fairness and transparency" encompasses our rewards system. We have been on a three-year initiative to design the processes and systems that support how our rewards are distributed. During this time, we have run employee focus groups after each perform-

ance cycle and solicited ideas for improvement. We have also done surveys on the effects of different rewards on employee performance. Our senior-management team has taken the time to support these initiatives and make improvements based on feedback.

FIGURE 2 Frequency for Code Responses

Question 1: The most important characteristic or attribute that makes my organization's reward program effective is ___?

Question 2: The one or two things my organization must do to improve our reward systems are ___?

Note: Each count represents a codeable response by each of the 461 organizations participating in the research.

Response Codes	Question 1: Effectiveness	Question 2: Improvement
Alignment		
▪ Across the organization (internal consistency)	1	25
▪ Goals, strategy, results and objectives	56	28
▪ Values, culture, vision and mission	15	8
▪ Employee line of sight	19	28
Total Alignment Score	91	89
Benefits	6	4
▪ Above the market	12	0
▪ Health care	3	0
▪ Pension or retirement	2	2
▪ Perks and time-off	0	3
▪ Comprehensive	0	6
Total Benefits Score	23	15
Communication	2	7
▪ About the business—competitive environment	2	5
▪ Reward programs	45	99
▪ Transparency or employee understanding	10	15
Total Business Score	59	126
Control and Accountability by Management	0	4
▪ Fiscal accountability	0	0
▪ Process or policy accountability	3	0
Total Control and Accountability Score	3	4
Development and Career Opportunities	15	23
Evaluating ROI / Effectiveness	0	6
Job Content	1	0
Leadership Support		
▪ Executive or senior management	15	7
▪ Middle managers and supervisors	1	16
Total Leadership Support Score	16	23
Pay-Program Attributes	2	0
▪ Broad-based eligibility	12	14
▪ Stability over time	4	4
▪ Differentiation	14	29

FIGURE 2 Frequency for Code Responses *(continued)*

Response Codes	Question 1: Effectiveness	Question 2: Improvement
Flexibility	19	11
Timeliness	12	11
Measures, standards and goals	2	31
Funding	0	14
Rewards valued by employees	9	17
Connection between pay and performance	35	35
Total Pay-Program Attributes Score	109	166
Type of incentive Program	0	2
Individual-based	8	2
Team-based	5	0
Organization-based	1	0
Multiple level-based	4	3
Total Type of Incentive-Program Score	18	7
Pay Comparisons—External	25	28
Above market	17	2
At market	4	0
Below market	0	3
Total Pay Comparison—External Score	46	33
Pay Comparison—Internal	3	1
Job level or job evaluation	1	6
Internal fairness	17	14
Total Pay Comparison—Internal Score	21	21
Type of Pay Program		
Base pay, salary or wage	0	0
Short-term incentive or annual cash award	13	5
Long-term incentive or equity award	6	3
Recognition or spot award	23	23
Total Type of Pay-Program Score	42	31
Performance Assessment or Appraisal	5	30
Rewards Mix (i.e., base, incentive and benefits)	19	6
Work Environment	6	1
Culture, values and employee engagement	15	1
Flexible work schedules	6	2
Job satisfaction	1	0
Work-life balance	13	14
Holding employees accountable	0	6
Total Work Environment Score	41	24
Simplify or Streamline Programs and Processes	0	10
Tools and Training for Managers	2	17
Responses not Scored		
Response left blank	26	14
Not related to company	43	23
Total Response not Scored	69	37

The response was coded as reflecting all of the following categories:

- "Communication—transparency"
- "Pay comparison internal—fairness and consistency"
- "Leadership support—executive."
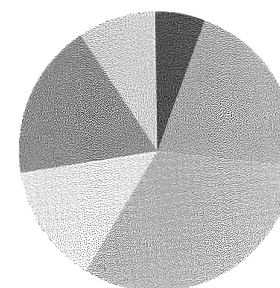
Demographics

The rewards survey received 461 responses from compensation professionals representing 435 different organizations. In 18 cases, multiple (typically two) compensation professionals from the same company responded. However, given the demographic information by these individuals, it was likely they were from different business units, possibly with different compensation policies and practices. After reviewing their responses, these respondents were left in the data set.

Participating organizations were diverse in size, type and industry as shown in Figure 3, Figure 4 and Figure 5. Although most respondents held mid- to senior-level compensation positions (88 percent), some emerging practitioners responded to the survey (See Figure 6 on page 12).

RESEARCH FINDINGS

The coding categories, themes and frequency data for the two questions are shown in Figure 2. In Figure 7 on page 13, the percentages for the major themes are shown in descending order of the number of combined total responses for the "contributes to effectiveness" question and "needs improvement" question. Effectiveness— and needs—improvement responses

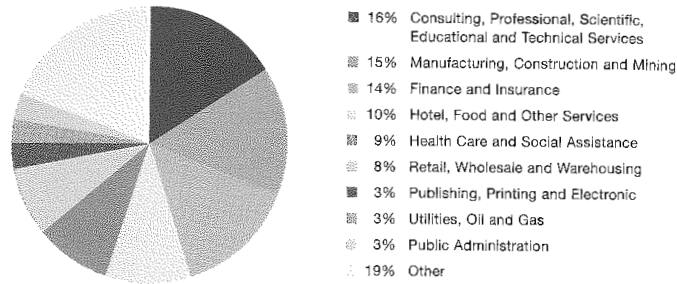FIGURE 3 Participant Demographics: Number of Employees

- 6% <100
- 21% 100 – 999
- 32% 1,000 – 4,999
- 14% 5,000 – 9,999
- 18% 10,000 – 49,999
- 9% 50,000+

FIGURE 4 Participant Demographics: Type of Organization
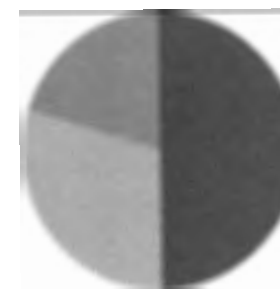
- 50% Public
- 30% Private
- 20% Not-For-Profit, Education, Government

FIGURE 5 Participant Demographics: Industry Sector

- 16% Consulting, Professional, Scientific, Educational and Technical Services
- 15% Manufacturing, Construction and Mining
- 14% Finance and Insurance
- 10% Hotel, Food and Other Services
- 9% Health Care and Social Assistance
- 8% Retail, Wholesale and Warehousing
- 3% Publishing, Printing and Electronic
- 3% Utilities, Oil and Gas
- 3% Public Administration
- 19% Other

are combined into single bars in Figure 7 and all subsequent figures report findings because the authors believe the two questions ask respondents to identify important characteristics of their reward programs, and the combination of positive and negative responses indicates the true importance of the characteristic in the respondents' views.

Major Themes

Figure 7 shows specific pay-program attributes were most often identified as key factors in reward-program effectiveness and as a key improvement need. The pay-program attributes included issues of program eligibility, consistency over time, differentia-

FIGURE 6 Participant Demographics: Level of Responsibility

- 43% Mid-Level
- 32% Senior-Level
- 13% Executive Officer
- 8% Emerging-Level
- 4% Consultant

tion, flexibility, timeliness, measures, standards and goals, funding, rewards valued by employees and the connection between pay and performance, which will be discussed more specifically in this paper. Thirty-five percent of respondents perceived one of these elements or attributes of their reward programs as key improvement needs, and 26 percent of respondents saw one of these attributes as a key strength of their reward programs.

Communication was the next most-mentioned theme, with 29 percent of respondents indicating that reward communications needed improvement and 15 percent seeing it as a strength of their reward programs. It is interesting, though perhaps unsurprising,

FIGURE 7 Major Themes—Strengths and Improvement Needs
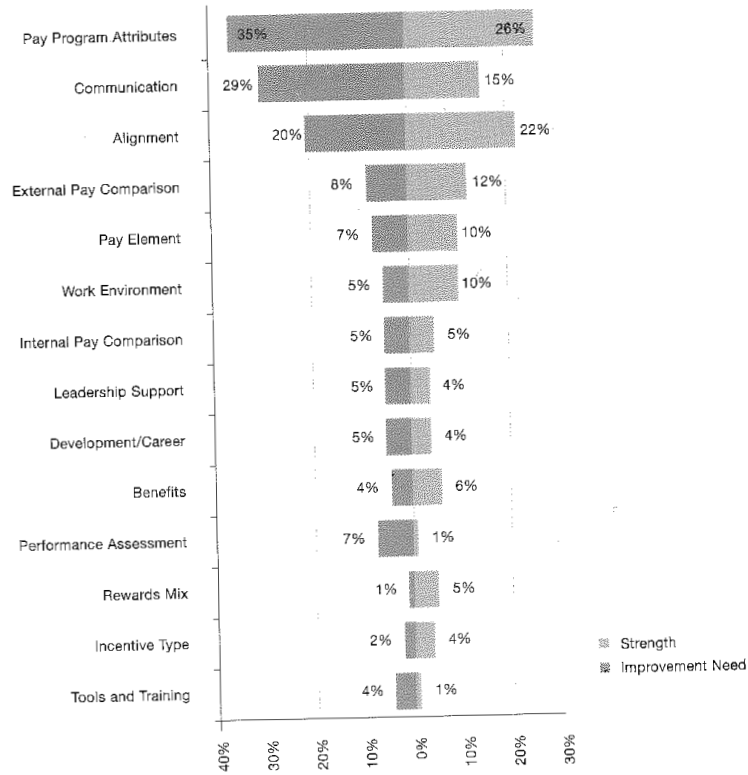
that communication was frequently identified both as a strength and as needing improvement, and almost twice as likely to be identified as needing improvement versus being a strength.

Alignment of rewards with the organization's business is slightly more likely to be reported as a strength than as a need for improvement (22 percent and 20 percent, respectively).

External pay comparisons, pay elements and the work environment are the next most-frequently mentioned themes in total responses. These three themes were more likely to be identified as strengths then as areas needing improvement. Other broad themes identified in the survey responses are:

- Internal pay comparisons
- Leadership support

- Development and career opportunity
- Benefits
- Performance assessment
- Rewards mix (base salary, incentives or benefits)
- Incentive type (individual, team, organization or mixed)
- Tools and training for administering pay programs.

As previously noted, three themes emerged in this survey as the most-frequent responses, in terms of strengths and improvement needs: (1) pay-program attributes, (2) communications and (3) alignment. A closer examination of these three themes follows.

Pay-Program Attributes

Pay-program attributes or characteristics of the pay program clearly matter to a substantial number of respondents. Figure 8 shows that pay for performance; differentiation; flexibility; and measures, standards and goals are most-frequently mentioned within the overall category as either key contributors to the effectiveness of the rewards or key improvement needs. The following was a typical type of response coded in the pay-for-performance attribute category.

One of our most effective pay-program characteristics is that all rewards are tied into individual performance and accomplishment of objectives. Making sure financial objectives are continually reinforced is a critical gatekeeper for any reward being made.
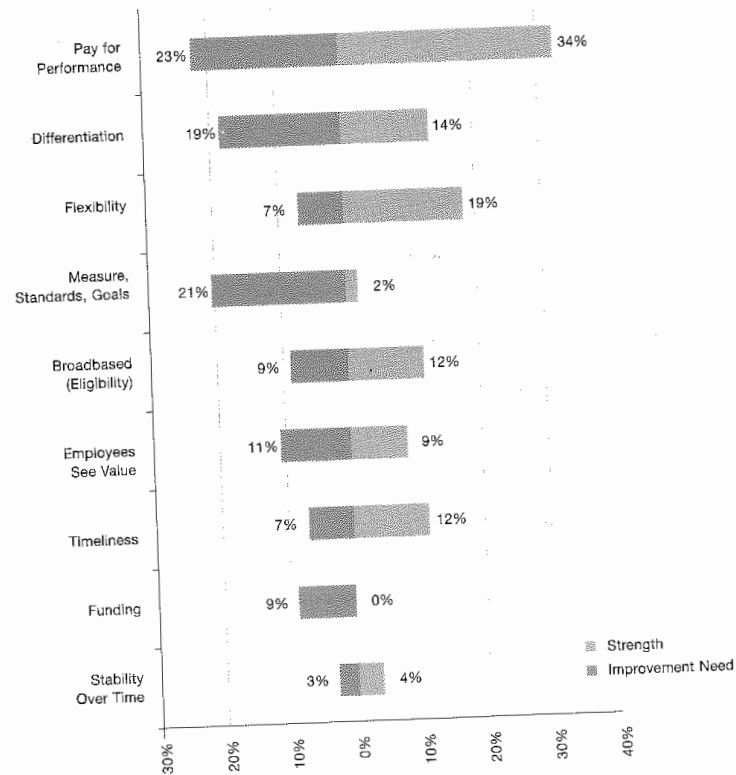
It is worth noting that three of the four most-frequently identified attributes are clearly related to linking pay to performance. Related to the pay-for-performance issue was the finding that most organizations did not see their performance-appraisal process as a strength, but as a program element that needed to be improved (See Figure 2).

Communications

Several types of communications were identified by respondents. Of these, providing employees information about reward programs was far more frequently mentioned as both a strength (78 percent of positive comments about the impact of communications related to reward communications) and as an improvement need (80 percent of negative comments about communications focused on reward communications). A common response attributing reward communications as an integral component of rewards effectiveness is exemplified by the following response:

Surprisingly it's not the value of pay. It's the communication. We've spent years spending hundreds of millions on providing benefits that employees didn't value, understand or even know existed. Regularly communicating the "total value" ... significantly improved the effectiveness of our rewards programs.

FIGURE 8 **Pay-Program Attributes**

| Attribute	Strength	Improvement Need
Pay for Performance	23%	34%
Differentiation	19%	14%
Flexibility	7%	19%
Measure, Standards, Goals	21%	2%
Broadbased (Eligibility)	9%	12%
Employees See Value	11%	9%
Timeliness	7%	12%
Funding	9%	0%
Stability Over Time	3%	4%

Percentages Indicate % of Organizations Responding in Category

General communications, business and organization-performance communications, and achieving transparency were mentioned, but far less frequently than reward communications. This may reflect a bias of the compensation professionals who responded to the survey, but it also may reflect the value of getting the basics of communications correct.

Alignment

The study's third most-mentioned theme is alignment. Figure 9 on page 16 shows the subcategories identified within this theme. By far, the most-prevalent mention of alignment deals was alignment between rewards and the organization's goals,

FIGURE 9 Alignment of Reward Programs
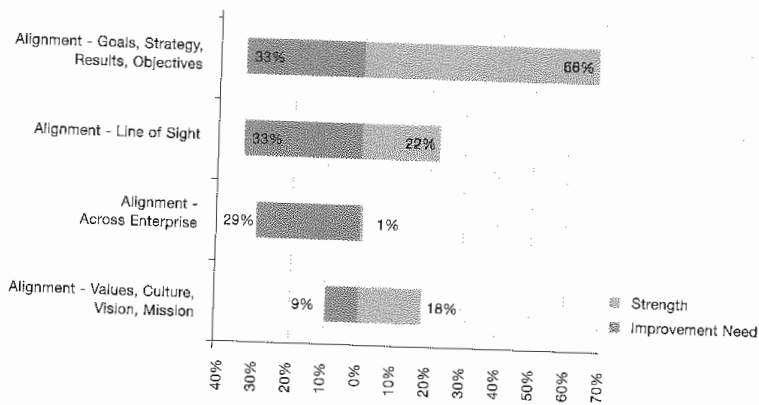
Percentages Indicate % of Organizations Responding in Category

strategy, results and objectives. This is reinforced by the following response identifying alignment with business goals as an area for improvement:

We need to establish a total rewards strategy and implement a methodology for setting goals and objectives at the organization—and individual—levels that links rewards to results.

Alignment between rewards and the organization's values, or culture of the enterprise, was also a key theme. Line of sight was also a theme in this category, as it relates to the connection between the individual's actions and business results. The final aspect of alignment—alignment or internal consistency *across* the enterprise—was mentioned by respondents as well. Alignment specifically with goals, strategy, results and objectives was twice as likely to be mentioned as a strength than lack of alignment as a weakness. However, employee line of sight and alignment/consistency of pay programs across the enterprise were most likely to be identified as areas that need improvement.

Responses Examined by Demographic Characteristics

Some interesting findings were uncovered when the data were examined based upon the demographic characteristics of respondents including:

- Senior-level compensation and HR executives see communications as a much more important issue than lower-level compensation practitioners.
- Lower-level compensation practitioners are more concerned about internal-equity issues as they relate to pay than senior compensation or HR executives.

- Not-for-profit and government organizations find that issues related to performance management, external competitiveness and pay communications are more challenging than do privately owned or public organizations.
- Many mentions of work environment as a key factor in making rewards effective noted that the positive aspects of the work environment offset negatives associated with the organizations' relatively low cash compensation and inability to be more aggressive in cash.
- Smaller organizations reported that internal equity and the work environment were more likely to be advantages than at larger organizations.
- Organizations that were rated as "Most Admired Companies" by *Fortune* magazine were more likely than respondents from other organizations to identify alignment as important, both as a strength and as an area needing improvement.
- Most Admired Companies were also more concerned than other organizations about external market competitiveness as an area needing improvement.
- Most Admired Companies were more likely to indicate that leadership support was a strength of their program than an area that needed improvement.

RECOMMENDATIONS AND CONCLUSIONS

Compensation professionals participating in this study suggested myriad ways to improve the effectiveness of reward programs. Three in particular rose to the top: (1) paying for performance; (2) clearly communicating reward programs to employees and (3) ensuring the alignment of rewards with organizational goals, strategy and results. Indeed, these are much easier said than done. And each is worthy of its own journal paper. Based on data from this study and the authors' collective experience consulting in the field, organizations can take a variety of practical steps in these three areas to improve the effectiveness of their rewards.

Pay for Performance

The authors' experience in working with *Fortune* magazine's Most Admired Companies is that the companies are quite serious about their performance-management processes and tend to take a more-integrated approach to establishing a shared understanding of what must be achieved and how. Most Admired Companies reinforce the connection between the organization's suite of rewards and performance. Some practical steps organizations can take include the following:

1. Remember the "management" in performance management. This means that organizations need to do much more than develop the ideal performance appraisal form or devise the perfect merit-increase guide. Effective performance-management requires a comprehensive performance-planning process with employees, ongoing coaching, and providing employees with regular updates on the progress they have made toward performance objectives.

2. Define performance, and then set specific performance measures, goals (targets) and standards.

3 | Establish linkages between performance and rewards that are clear and understandable to employees.

4 | Differentiate rewards—not just performance ratings—between high and average performers, and between average and below-average performers. This undoubtedly will mean that some employees will not receive performance-based salary increases or incentive pay.

5 | Ensure that managers and employees understand and appreciate all of the rewards available in the organization. This goes beyond base-salary increases and variable pay programs and includes promotions, recognition and learning and development opportunities.

Communication

Unlocking the "black box" of reward programs can have a remarkable effect on the workforce. It helps employees understand what the organization values. It educates employees on the economic realities that influence the setting of pay levels. It explains to employees how reward programs are intended to work. And it clarifies the linkage between pay and performance. Effective rewards communications typically include the following:

1 | Simple and focused messages that offer brief explanations of rewards elements.

2 | The use of multiple methods of communication, including newsletters, manager presentations, Web sites and video segments. Get the communications and marketing departments involved to help frame and communicate pay-program information.

FIGURE 10 **Communications**
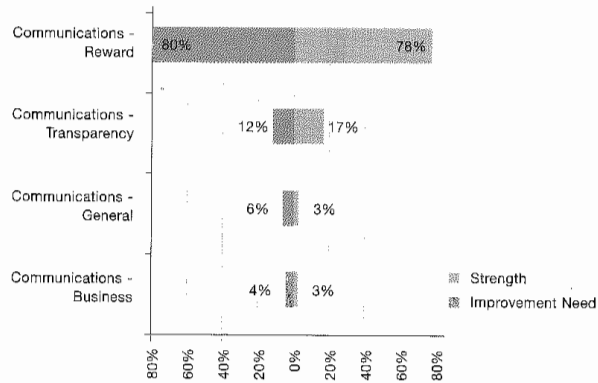
Percentages Indicate % of Organizations Responding in Category

3 | The practice of "strategic redundancy" of important objectives and features of reward programs or "keep repeating the message."

4 | Pilot tests of communications messages and mediums with managers and employees before broader rollout.

5 | The education of managers and supervisors regarding the reward programs before communicating to the broader workforce. Get the training department involved in designing and conducting these programs.

Alignment

Aligning reward programs with organizational goals, strategies and work culture can provide substantial benefits to the organization. Establishing this connection may require time and foresight, but having individual and collective efforts focused on common goals is well worth the investment. Key steps to creating this alignment include the following:

1 | Clearly define and articulate the business and reward strategies.

2 | Determine the reward elements best reinforcing the achievement of desired goals and strategies.

3 | Design reward contingencies (if-then's) that reinforce the achievement of results.

4 | Secure the support of leaders so that they lead the charge in communicating and sustaining employee commitment.

5 | Create connections between employee accountabilities and business outcomes.

It is worth noting that many respondents defined rewards more broadly than traditional direct-pay and employee-benefits elements. Career and development opportunities and the work environment were deemed important contributors to reward effectiveness and areas that organizations needed to improve. These findings indicate that compensation professionals have taken a more holistic approach to how they view rewards.

Research methods seldom allow compensation professionals to draw conclusions about what was *not* mentioned in the study. However, in the spirit of fictional detective Sherlock Homes, who in the *Hounds of the Baskerville* placed great importance on the fact that "the dog did not bark," the authors found it interesting that job standards, management control and pay-program evaluation were seldom mentioned as features contributing to the effectiveness of a reward program.

FIGURE 11 Work Environment
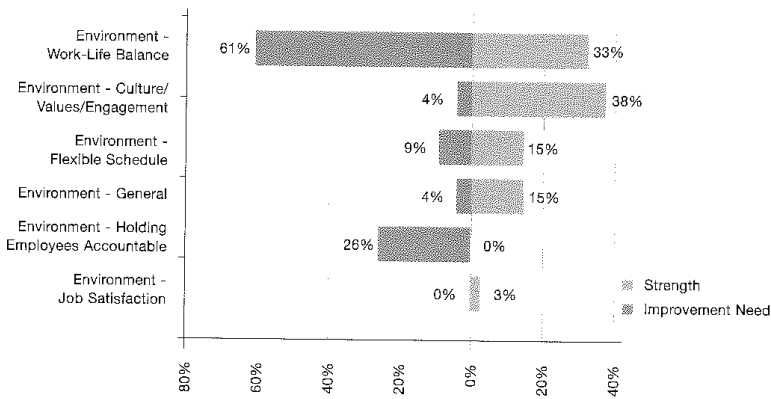
Percentages Indicate % of Organizations Responding in Category

Limitations

The open-ended nature of this study has strengths and weaknesses. The differences in terminology, ambiguity and complexity of the responses created some coding challenges for the research team, even with the team members' extensive experience. Furthermore, the response rate to this open-ended survey was lower than some of the more-structured surveys the authors have conducted. However, the open-ended nature of these research questions provided very detailed information, which enabled the team to gain a keener insight into reward-programs' effectiveness than what could have been gained through a traditional survey.

This study's sample was composed primarily of compensation professionals. Although this group has the best understanding of their pay system and has the technical background to assess its strength and weaknesses correctly, it must be recognized that line managers may view the pay programs differently.

Lessons Learned

This study provides several lessons for compensation professionals:

▓ It reinforced the importance of reward communications, and is a strong reminder that the absence of communications can erode the effectiveness of even the best-designed reward programs.

▓ The alignment of business goals, strategies, results and objectives with reward programs is acknowledged as very important by compensation professionals. However, improving employee line of sight between organization goals and reward programs requires substantial work, as indicated by a significant number of respondents.

▓ Although it is important to recognize that senior-management support contributes to the effectiveness of reward programs, support by middle and lower management also is important, and weak support at lower levels diminishes program effectiveness.

▓ Compensation professionals need to consider and manage the specific attributes of pay programs, including employee eligibility, pay differentiation between high and average performers, flexibility of pay programs and rewards for performance.

▓ Nonfinancial rewards such as career and development opportunities, work-life balance and organization culture were identified as important aspects of reward programs, and improvement in work-life balance was identified as a means to enhance reward program effectiveness.

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