

## Breaking all the Rules: NEW DIRECTIONS IN COMPENSATION STRATEGY

These are challenging times for employers as they grapple with critical - yet sometimes divergent - total rewards priorities.

This year, McDowall Associates conducted its second annual Total Rewards Pulse Survey with the aim of highlighting not only the pressures that today's employers face, but also the opportunities that are arising to take their reward strategies and programs in a new direction.

And for many organizations, a new direction may be critically important, as many of our survey respondents indicate the old ways of doing things may not be enough to address emerging challenges.

As with last year's survey results, we have divided the findings into those from private sector respondents and those from public sector / not-for-profit respondents. There are some notable differences in the priorities and concerns across these two groups of employers.

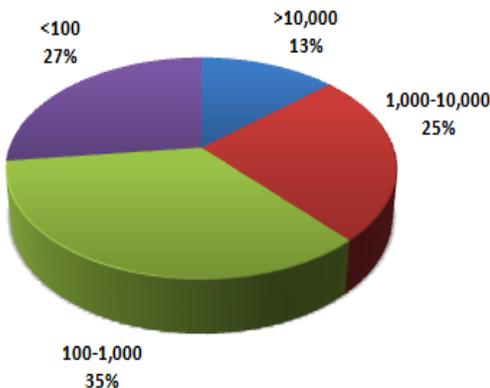
One common theme, however, that transcended sectors was the concern about talent. The private sector respondents reported more concerns about retaining talent while the public sector/not-for-profit group indicated emerging concerns about their ability to attract talent.

But all the participants seemed to recognize that a strategic approach to compensation and total rewards is the cornerstone of an effective talent management approach. A notable percentage reported plans to implement a total rewards strategy within the next three years.

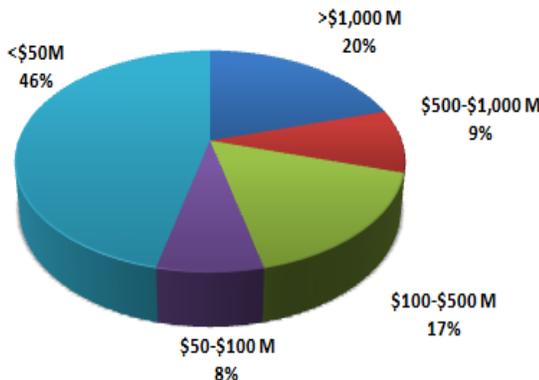
### Participant Profile

Close to 60 organizations fully answered the 2012 Total Rewards Pulse survey. Respondents represented a diverse range of organizational sizes and included organizations from both the private sector and public sector/not for profit. Some 39% of respondents were from the private sector, with 61% representing the public sector/not-for-profit sector.

**Organization Size by  
Number of Employees**



**Organization Size by  
Total Revenue/Operating Budget**



### HIGHLIGHTS OF SURVEY FINDINGS

#### Establishing a Total Rewards Strategy a Key Priority

31% of public sector/not-for-profit respondents and 21% of private sector respondents reported plans to implement a total rewards strategy in the next three years

#### Retaining Talent a Key Private Sector Imperative

Private sector respondents identify retaining key talent as their top total rewards issue, both currently and over the next three years

#### Public sector/not-for-profit Grappling with Cost Containment Challenges

Public sector/not-for-profit respondents identified compensation and benefit program costs as their top current total rewards challenge, although attracting key talent emerges as the top concern for the coming three years

#### Total Rewards Segmenta- tion an Emerging Priority

Almost a third of the private sector respondents reported having total rewards programs that specifically target critically skilled employees, versus 8% of the public sector/not-for-profit group

## Prevalence of Total Compensation and Total Rewards Strategies

Survey participants were asked to identify whether they had in place or were planning to implement a total compensation and/or total rewards strategy.

Most strikingly, the responses highlight the growing use of total compensation strategies across public sector/not-for-profit organizations over the 2011 results. Total compensation strategies define an organization's approach to designing and managing all elements related to pay, including base pay as well as short-term and long-term incentives and perquisites.

Half of the public sector/not-for-profit respondents in the 2012 survey reported having a total compensation strategy, up from 35% in 2011. Further, an additional 16% of respondents plan to introduce a strategy in the next three years.

The prevalence of such strategies has remained steady in the private sector sample, with 84% of respondents reporting having a total compensation strategy, down just slightly from 85% in 2011. An additional 11% reported plans to implement a strategy in the next three years.

Not surprisingly, total rewards strategies are not as prevalent as total compensation strategies, although they represent a logical next step. Total rewards strategies address all the major components of the employment deal, including pay, benefits, performance recognition programs, work/life balance programs and career development opportunities.

The prevalence of such strategies remains largely unchanged from 2011, with 63% of private sector respondents and 16% of public sector/not-for-profit respondents reporting having a total rewards strategy in place.

Nevertheless, survey respondents did recognize the value of such strategies, as 21% of private sector organizations and 31% of public sector/not-for-profit organizations reported plans to implement a total rewards strategy within the next three years.

Prevalence of a Total Compensation Strategy		
Organization Response	Sector	
	Private	Public/NFP
Yes	84%	50%
No, no plans to implement in near future	5%	34%
No, but planning to implement in next 3 years	11%	16%

Prevalence of a Total Rewards Strategy		
Organization Response	Sector	
	Private	Public/NFP
Yes	63%	16%
No, no plans to implement in near future	16%	53%
No, but planning to implement in next 3 years	21%	31%

## Top Five Total Rewards Issues

Survey respondents were asked to identify the top five reward issues they felt had the most significant impact on their organization's business success, both currently and anticipated over the next three years.

Although different priorities emerged among the private sector respondents relative to those of the public sector / not-for-profit respondents, some clear themes related to the strategic importance of talent were evident for both groups.

### Private Sector

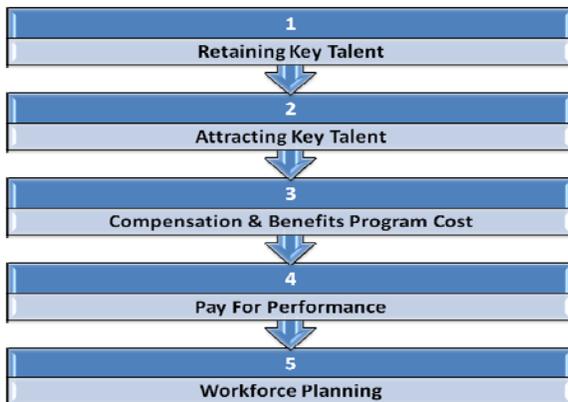
Retaining key talent was the top current issue, up from the number two spot in 2011, and attracting key talent was number two on the list, down from the top spot in 2011.

Meanwhile, workforce planning made the top five list of current issues for the first time in 2012, further highlighting how focused these organizations are on maintaining a strong talent pool as they look to the future.

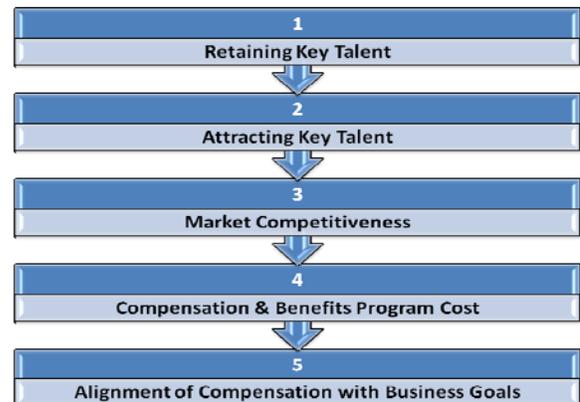
When asked to identify their top five total rewards issues looking out to 2015, the private sector respondents maintained their focus on talent, with retaining and attracting key talent remaining one and two on the list. Reinforcing the retention theme, market competitiveness emerged third as a future concern, even though it didn't rank among the top five current concerns.

Looking ahead, cost containment remained a top five concern, although it slipped to the number four spot. The findings suggest respondents may be anticipating the need for more investments in total rewards in the coming three years as a way of supporting efforts to retain and attract talent.

Current Total Rewards Issues



Future (2013-2015) Total Rewards Issues



## Top Five Total Rewards Issues continued ...

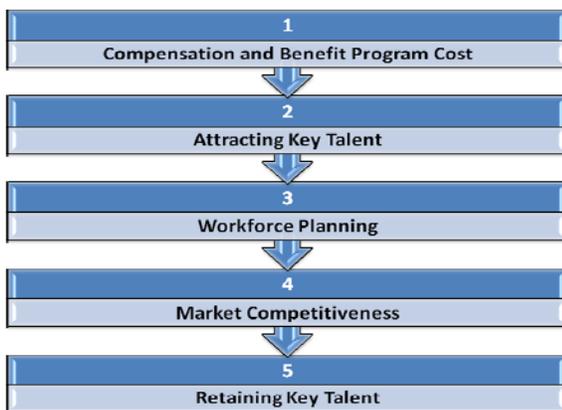
### Public Sector/ Not-for-Profit

While attracting and retaining talent both made the top five list of current concerns for the public / not-for-profit sector respondents, these concerns did not rank as high as for the private sector group.

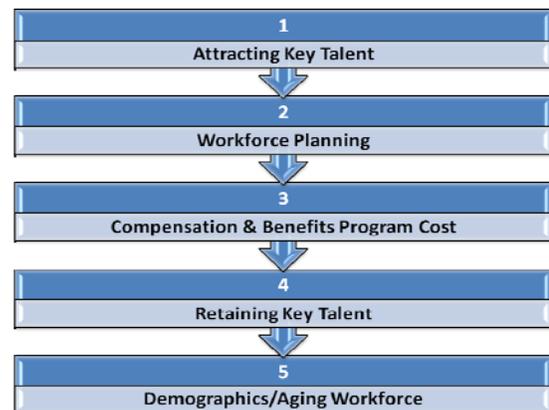
Topping the list was concern about compensation and benefit program costs. At the same time, the results suggested the public sector/not-for-profit employers are concerned about securing a strong workforce for the future, given attracting key talent and workforce planning ranked second and third on the list of current issues.

The theme of ensuring a sustainable talent pool was even more strongly reflected in the findings related to future total rewards challenges. When asked to look out to 2015, the public / not-for-profit sector respondents identified attracting key talent and workforce planning as their top two concerns, although interest in managing costs remained front and centre, ranking third on the list.

Current Total Reward Issues



Future (2013-2015) Total Rewards Issues



## Market Pricing and Market Positioning

While maintaining market competitiveness is an important issue for many of the survey respondents, there were few surprises with how organizations approached market pricing.

Most of the private sector organizations reported that they benchmark internal pay levels with consideration to total compensation. In contrast, less than half of the public / not-for-profit sector respondents reported considering total compensation in their benchmarking efforts, but the reality is that variable pay is less prevalent in this sector.

Meanwhile, only a small percentage of survey respondents reported that they are considering making changes to their desired market positioning for base pay in consideration of total rewards. This could indicate that few organizations were planning significant enough changes to their total rewards to warrant revisiting the positioning of base pay. Alternatively, it is possible only some organizations were prepared to take a more aggressive position on base pay, even if trimming expenditures in other total rewards areas.

Market Pricing Approach		
Organization Response	Sector	
	Private	Public/NFP
Base Salary Only	11%	53%
Total Compensation	89%	47%

Total Reward Impact on Base Salary		
Organization Response	Sector	
	Private	Public/NFP
Yes	11%	17%
No	89%	83%

## Workforce Segmentation

Survey participants were asked to identify if any of their total rewards programs were designed to address the needs or preferences of specific generational groups (e.g., baby boomers, generation X, millennials).

The survey findings show the prevalence of such programs is quite low, with only a small number of public sector/ not-for-profit organizations indicating they utilize such an approach to workforce segmentation today.

Nevertheless, some organizations in both the private (17%) and public sector/not-for-profit (5%) groups report the intent to explore such workforce segmentation in the next three years. This emerging trend aligns with the other themes in the research findings related to employer concerns about access to talent.

When asked to identify programs that specifically target or address cross-generational needs, survey participants cited the following:

- Employee assistance program;
- Employee surveys;
- Scholarship program; and
- Flexible work arrangements.

While segmentation based on generational demographics was not a major area of focus for the survey participants, the results show a stronger orientation to developing total rewards programs specially aimed at employees with critical skills. Just under a third of the private sector respondents and 8% of the public sector/not-for-profit respondents reported having such programs.

Examples of programs used by survey respondents that are specifically targeted at critically skilled employees include:

- Retention bonuses;
- Succession planning; and
- Increased training and professional development opportunities.

Total Rewards programs specifically targeted at INTER-GENERATIONAL groups		
Organization Response	Sector	
	Private	Public/ NFP
Yes	0%	8%
No, no plans to implement in near future	83%	87%
No, but planning to implement in next 3 years	17%	5%

Total Rewards programs specifically targeted at CRITICALLY SKILLED employees		
Organization Response	Sector	
	Private	Public/ NFP
Yes	28%	8%
No	72%	92%

## Pay for Performance

Pay for performance is a topical compensation subject, and sometimes the focus of much debate. Survey respondents were asked to report on how they deliver compensation through both variable pay and base pay programs.

Survey respondents were asked to report on their variable pay budgets, both for the current year and for the next three years.

Variable Pay Budget		
Organization Response	Sector	
	Private	Public/ NFP
Increased compared to last year	5%	31%
Remained the same as last year	89%	69%
Decreased compared to last year	6%	0%

Base Salary increases differ based upon individual employee performance		
Organization Response	Sector	
	Private	Public/ NFP
Yes, Entirely based upon individual performance	39%	18%
Yes, Partly based upon individual performance	50%	30%
No, Not based upon individual performance	11%	52%

Variable Pay Budget vs. Merit Pay Budget: CURRENT		
Organization Response	Sector	
	Private	Public/ NFP
Variable Pay Budget is HIGHER than Merit Pay Budget	71%	17%
Variable Pay Budget is THE SAME as Merit Pay Budget	23%	39%
Variable Pay Budget is LOWER than Merit Pay Budget	6%	44%

Variable Pay Budget vs. Merit Pay Budget: NEXT 3 YEARS		
Organization Response	Sector	
	Private	Public/ NFP
Variable Pay Budget is HIGHER than Merit Pay Budget	76%	12%
Variable Pay Budget is THE SAME as Merit Pay Budget	24%	41%
Variable Pay Budget is LOWER than Merit Pay Budget	0%	47%

Determination of Salary Increases		
Organization Response	Sector	
	Private	Public/NFP
Merit Matrix	67%	22%
Service Only	0%	5%
Cost of Living and/or General Increase	11%	31%
Combined COLA/Gen. Increase & Performance	22%	42%

## Other Total Rewards Practices

Although compensation programs represent a significant component of any total rewards offering, other elements are also important to support employee attraction, retention and engagement.

The 2012 Total Rewards Pulse Survey explored two additional facets of total rewards - employee recognition and employee wellness and work/life balance.

### Employee Recognition

Many organizations utilize a variety of programs, in addition to compensation, to recognize employees for their contributions and results.

Survey respondents were asked to describe the formal or informal employee recognition initiatives that have had the most significant impact.

Responses included:

- Monthly town hall recognition in front of peers;
- Top performers recognized at annual gala or BBQ event;
- Company-paid social events;
- Spot awards;
- Service awards;
- Individual- and team-based award, including a letter from the president; and
- Customer, peer and manager recognition awards.

### Employee Wellness and Work / Life Balance

Programs related to employee wellness and work / life balance also represent an important total rewards component.

When asked to define their top employee wellness and/or work / life balance programs that were having the most significant impact, the private sector respondents identified flexible scheduling as their top program, both currently and over the next three years, whereas public sector respondents identified time off in lieu as the top program both currently and over the next three years.

It is interesting to note that the ranking of health / fitness / wellness programs made a major jump in the rankings when the private sector respondents looked out three years, up from the number four spot to being ranked second. Many companies are grappling with rising benefit costs and concerns about employee health and productivity, which may explain the anticipated stronger focus on health and wellness that survey respondents expected to emerge.

## Looking Ahead

### So how do organizations find the right balance between managing costs and making investments

For many organizations, delivering an effective total rewards offering is a balancing act between the need to contain costs and the need to make investments to better attract and retain talent.

The McDowall Associates 2012 Total Rewards Pulse Survey suggests many organizations are still grappling with how to find the right balance.

Managing compensation and benefit program costs was consistently ranked among the top five total rewards issues, both at present and over the next three years. So cost containment remains a key issue, especially in the face of continuing economic uncertainty on a global scale.

Yet at the same time, respondents consistently identified talent - be it the attraction or retention of key talent, as a key concern as well.

So how do organizations find the right balance between managing costs and making investments?

For the moment it appears many organizations are sticking with the status quo. Some 53% the public sector / not-for-profit respondents and 16% of private sector respondents report no plans to implement a total rewards strategy in the near future.

And perhaps partly in response to lean budgets for salary increases, 52% of public sector/ not-for-profit respondents and 11% of private sector respondents indicate that individual performance is not a consideration in the allocation of salary increases.

Yet experience has taught us that to effectively attract and retain talent, organizations need to take a holistic view of what they offer from a total rewards perspective - both to optimize expenditures and to better address employee needs and preferences. Further, often such strategies directly address how best to recognize and reward key talent - including top performers.

The survey results suggest that the need to attract and retain talent may fuel a rethinking of total rewards in the coming years. Already, efforts are being made to design total rewards programs to better support the attraction and retention of critically skilled employees. And a modest number of respondents indicate they will begin to explore how to evolve total rewards programs to increase their appeal to different generational groups.

The survey results indicate that new thinking is starting to emerge to address organizational needs for talent. And these original ideas will no doubt set the stage for new directions in compensation strategy.



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