

VisionLink

Selecting the Right Performance Measures for Your Incentive Plan

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Financial Visions



THE VISIONLINK
ADVISORY GROUP

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Today's presenter

Thomas E. Miller

President

949-265-5700

tmiller@vladvisors.com



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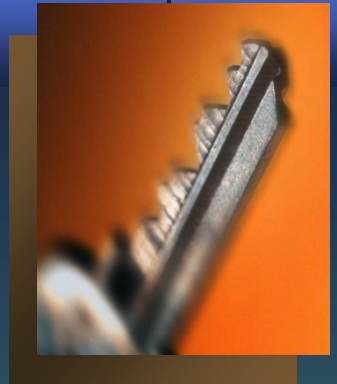
We're happy to provide a copy of today's slides. Information will be provided at the close of the presentation.

For questions during today's presentation:

*Use the question panel
to the right of your screen*

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Key Concepts



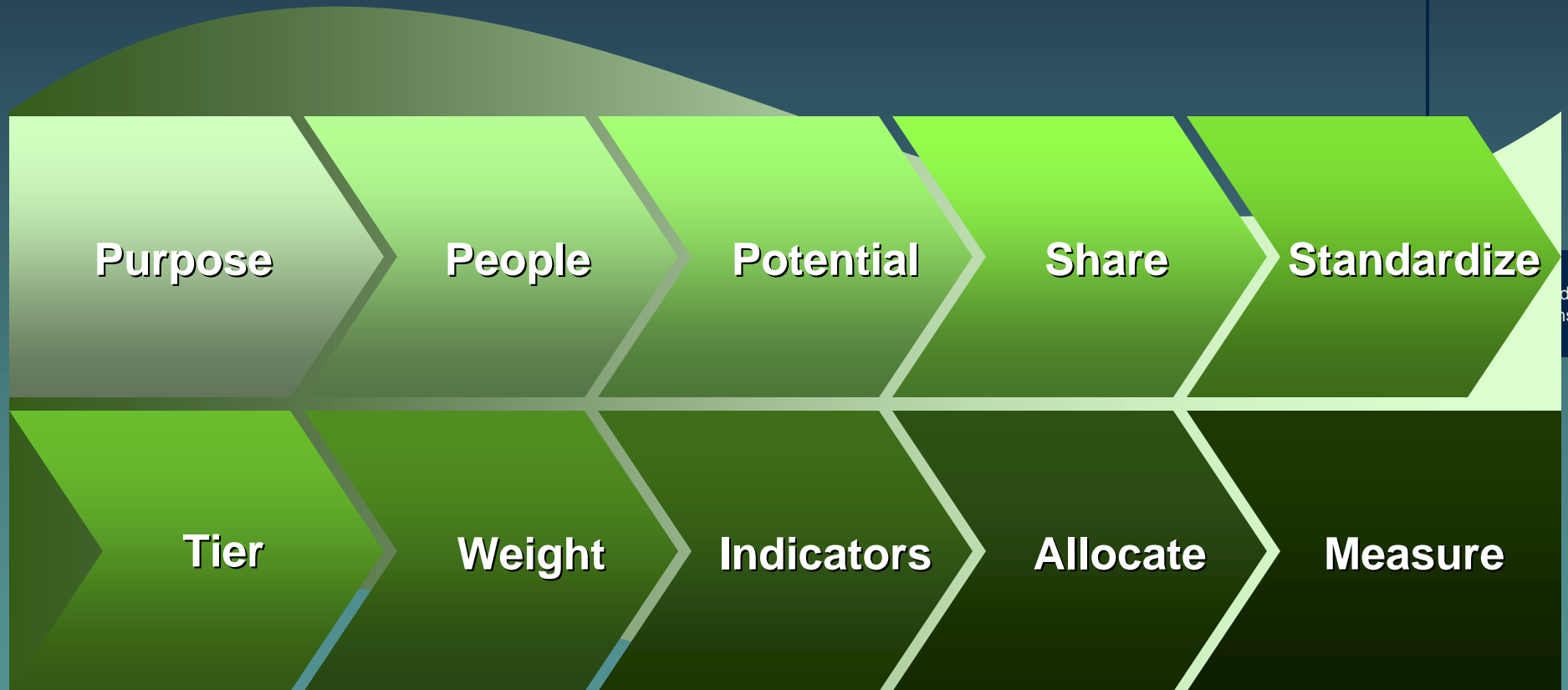
- The primary purpose of an incentive plan is to focus employees on a company's most important goals
- Selecting the right metrics can significantly alter behavior among key employees
- There are two core approaches to selecting metrics—each with pros and cons
- The effectiveness of your performance management system should be considered before selecting from the two approaches
- What is VisionLink's "Best Practice" approach?

Pay For Performance Objectives

- Recruit and retain highest quality employees
- Communicate and reinforce the values, goals, and objectives of the company
- Engage employees in the organization's success
- Reward contributors for successful achievements

Building an Incentive Plan

A Unique Process



Building an Incentive Plan

A Unique Process



Indicators:



- Measurable
- May or may not be in financial statements
- Track progress towards strategic objectives
- Reflect improvement in productivity

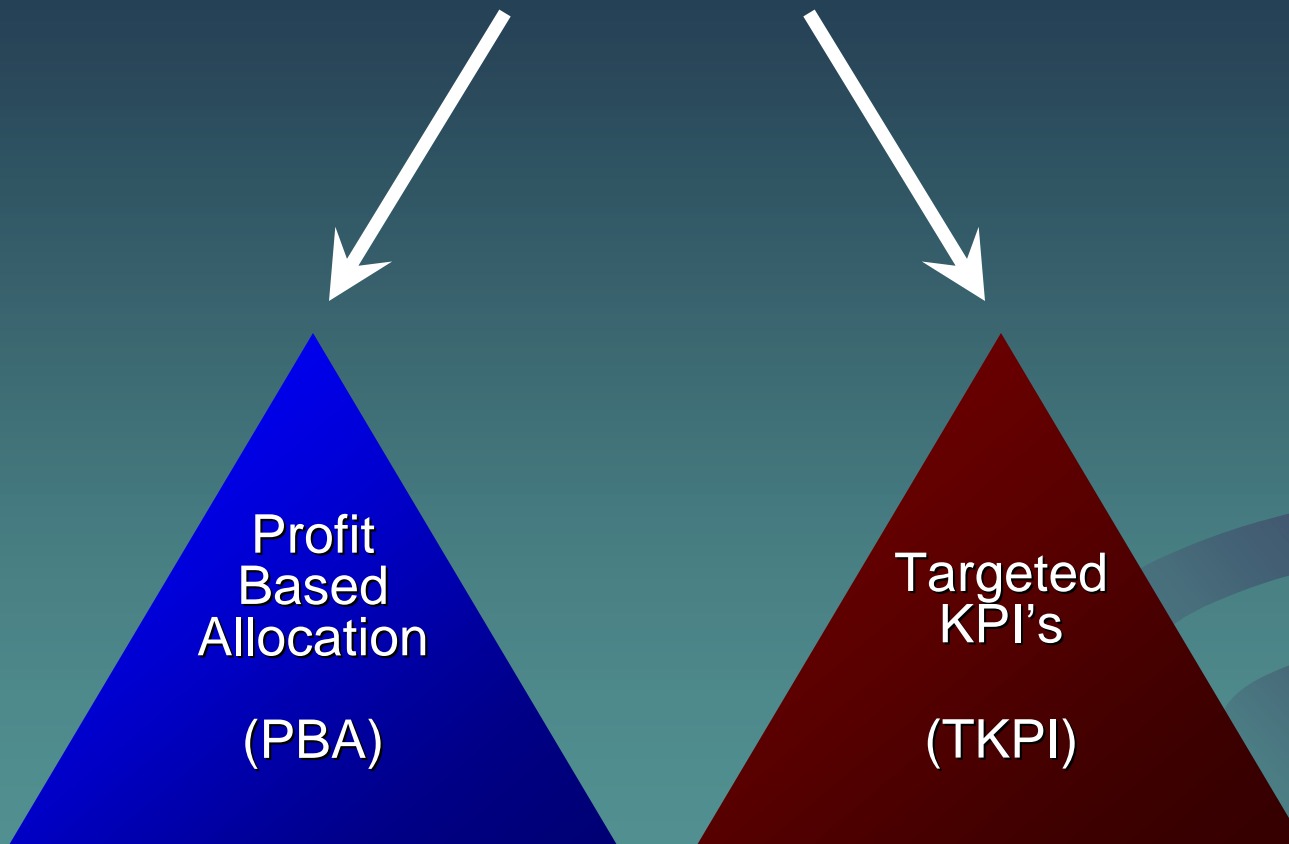
Indicators:

- Could be a number or a percentage
- Could be tied to budget (i.e., % of budgeted target achievement)
- Could be an improvement over prior period
- Could have a minimum threshold
- Could be tiered

In all cases:

- Seeking to improve performance
- Seeking to influence behavior
- Not trying to “motivate”
- Trying to “focus” through communication and reinforcement
- Trying to reinforce an ownership culture

Two Core Approaches



Profit Based Allocation
(PBA)

A percentage of annual profits awarded to employees

The award amount is divided among employees based on a pre-determined formula

Paid at year-end

Targeted KPI's
(TKPI)

Employees assigned a "targeted" incentive value – often based on a percentage of salary

Achievement of award is tied to multiple specific measurements or "metrics." Metrics can vary person to person.

Typically paid at year end, but may be quarterly.

Poll

QUICKPOLL

Which type of incentive is closest to the one used in your company?

Please select one:

- Profit-based Allocation
- Targeted KPIs
- Other
- Incentive plan, what incentive plan?!?

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QUICKPOLL

Which type of incentive is closest to the one used in your company?

Poll Results (single answer required):



Profit
Based
Allocation
(PBA)

Focus

Solely annual profits

Value

May be open-ended

Design

Relatively simple

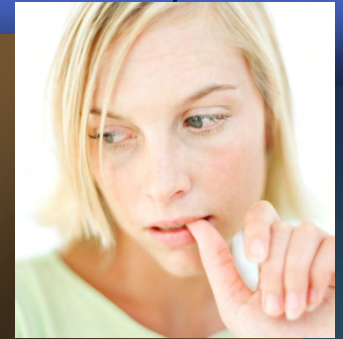
Essential

Strong Performance
Management System

PBA—Best Practices

- Define profits
- Select “benchmark” or “growth” approach
- Identify threshold
- Select percentage to share (fixed or tiered)
- Select allocation formula
- Determine whether employee awards will be influenced by personal performance

PBA—Dangers



- Failure to create line-of-sight
- Apathy
- Morale
- Lack of strong performance management system

Targeted
KPI's
(TKPI)

Focus

May include company, dept,
team & individual metrics

Value

Typically capped

Design

Can run from
basic to complex

Essential

Selecting the
right metrics

TKPI—Best Practices

- Select range of targets
- Select components
- Select drivers (metrics)
- Select performance tiers (eliminate all-or-nothing)
- Set up measurement systems

TKPI—Dangers

- Miscalculation
- Gaming
- Sandbagging
- Misalignment



Profit Based Allocation
(PBA)

Targeted KPI's
(TKPI)

Focus

Solely annual profits

May include company, dept, team & individual metrics

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Value

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Essential

Strong Performance Management System

Selecting the Right metrics

Indicators:

Selecting Indicators for a TKPI Plan

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Indicators:

Identify the indicators that will be used to measure performance in each area.

For example:

Company - Revenue growth and Net Income;

Department - Improvement in Customer Retention goal; Collections rate; Employee Productivity factor;

Individual - performance goal achievement

2008 Performance Matrix

Loans					
36,000	100%	115%	130%	140%	150%
33,000	80%	100%	115%	130%	140%
30,000	60%	80%	100%	115%	130%
27,000	45%	60%	80%	100%	115%
24,000	30%	45%	60%	80%	100%
	\$ 81,000	\$ 85,500	\$ 90,000	\$ 94,500	\$ 99,000
	Deposits				

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Company Indicators

Return on Equity
Return on Assets
EPS
Gross Sales
Net Income
Earnings Before Incentives
EBT, EBIT, EBITDA
Economic Profit (Productivity Profit)
Revenue per employee
Profit per employee
Customer satisfaction indicators

Department Indicators

New Loans
Deposits
Net Interest Spread
Gross Sales
Gross Margin
Overhead Percentage
Average Daily Room Rate
Average Daily Occupancy Rate
Contribution Margin
Expenses to Budget
Production Quotas
Employee Retention Percentage
Registrations
Client Referrals
Alpha
Number of MBOs met

Critical step:

Sensitivity Testing



Sensitivity Testing

- Tie incentive plan to annual budget projection
- Test highs and lows
- Test each matrix
- Show ROTRI™
 - Open up the incentives to be as high as possible



Is it possible for the shareholders
to get their highest return by paying
unlimited incentives?

ROTRI™ - Return on Total Rewards Investment

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How much is the Total Rewards Investment?

- Salaries
- Commissions
- Bonuses
- Deferred award accruals (LTIP)
- Core benefits
- Executive benefits
- Retirement contributions
- Payroll taxes



What return do you get on that investment?

_____ %

ROTRI™ Example:

Capital Account	\$ 2,000,000
Cost of Capital	12%
Capital Charge	\$ 240,000
NOPAT	\$ 1,000,000
Productivity Profit	\$ 760,000
Total Rewards Investment	\$ 4,500,000
ROTRI™	16.9%

(ROTRI = Productivity Profit/Total Rewards Investment)

PBA Allocation Schedule

Productivity Profit	Award %
First \$500,000	10%
Next \$500,000	15%
Amounts over \$1,000,000	20%

ROTRI™ Table

NOPAT	Productivity Profit	Award Amount	Owner's ROTRI (\$\$)	Owner's ROTRI (%)
\$1,000,000	\$ 760,000	\$ 89,000	\$ 671,000	14.9%
\$1,500,000	\$1,260,000	\$177,000	\$1,083,000	24.1%
\$2,000,000	\$1,760,000	\$277,000	\$1,483,000	33.0%
\$3,000,000	\$2,760,000	\$525,000	\$2,235,000	49.7%



Last thought:

Motivation

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Measuring Employee Passion

- Net Motivation Score (NMS)
- Examines three responses:
 - Clarity of the plan
 - Believability of the plan
 - Value of the plan



Net Motivation Score

- I clearly understand what personal and organizational results need to be achieved in order to receive my targeted incentive award
- I believe the company can, and likely will, achieve the results that will enable me to earn my targeted incentive award
- It is important that we achieve our results because my targeted incentive award value is very meaningful to me

Net Motivation Score

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Typical Score

Component	Motivated	Unsure	Not Motivated	Score
Clarity	4	3	3	1
Belief	3	5	2	1
Value	4	2	4	0
Composite				0.7

Positive Score

Component	Motivated	Unsure	Not Motivated	Score
Clarity	9	0	1	8
Belief	7	2	1	6
Value	8	2	0	8
Composite				7.3

How do we use the NMS?

- Learn
 - about the company's plans
 - the way they're communicated
 - where the employees are
- Strategize
 - how to improve the plans
 - how to better communicate them

Complimentary Offer

VisionLink invites you to participate in:

“Net Motivation Score” Assessment
(Confidential, and no obligation)

Indicate interest on survey form

Conclusions

- Select the right type of plan based on your organization's culture, business model and goals
- Select an approach (PBA or TKPI) and stay with it (polish and perfect over time)
- Measure the return on the plan's effectiveness through ROTRI™
- Measure and track your employees' engagement (NMS)

Next Online Seminar:



**“How Do I Structure Compensation
In Recessionary Times To Ensure
Ongoing Performance?”**

To be held on:

Tuesday, January 27th, 2009

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Questions?



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Thank you for attending

Please complete our brief survey immediately following our presentation.

We value your input.

*You may request a copy of our slides, our “Incentive Plan Guidelines” document, and the **“Net Motivation Score” Assessment.***

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Thank You!



Tom Miller

President

949-265-5700

tmiller@vladvisors.com

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