

January 26, 2010

# “Do Incentive Plans Really Work?”



THE VISIONLINK  
ADVISORY GROUP

Today's Presenter:

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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

# Key Concepts



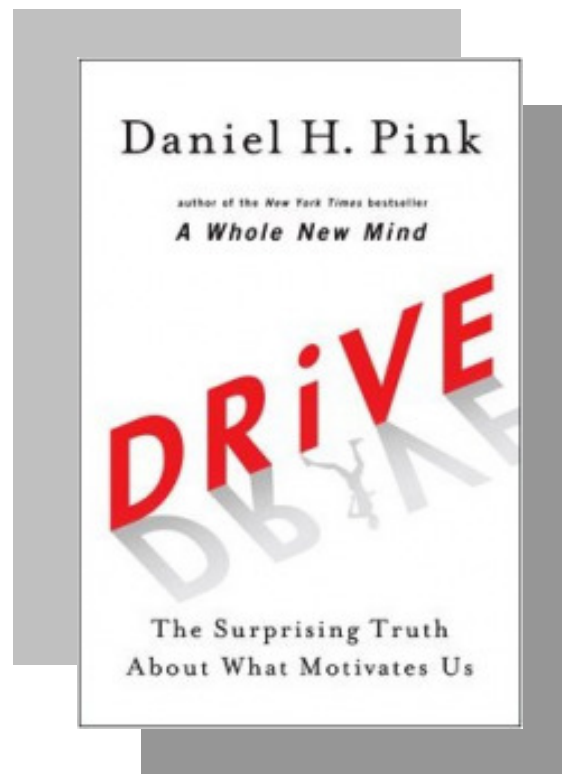
- It's true that incentive plans can backfire!
- But well-designed plans reinforce (rather than force) correct behavior
- Ideally, incentive plans reward for results, not simply behavior
- Ultimately results must help solve a problem on the CEO Worry List
- Most incentive plans look alike. World class plans are trend breakers.

# Chapter One

## An interesting debate

# Do incentives work?

Catch the buzz about Dan Pink's book—Drive



# Drive—studies show...

- Rewards narrow our focus, concentrate the mind, and restrict our possibilities
- When a task requires creative thinking, offering a reward extends the time it takes to solve the problem
- Extrinsic rewards should not be applied to tasks that require creativity

# This isn't new...and it's “not wrong”

- Studies have reached this conclusion for 30 years
- Rewards can distract from results by focusing people on “how to get the bonus”
- Rewards can buy temporary compliance but do not change intrinsic motivation
- Rewards can discourage innovation



# Drive—“instead...”

Use intrinsic rewards

- Autonomy—directing our own lives
- Mastery—getting better at something that matters
- Purpose—doing what we do in the service of something larger than ourselves

# Drive

No real argument here, but...

“Pay people adequately and fairly,  
get the issue of money off the table,  
then give them lots of autonomy.”


# Drive

- Not so easy in real life:
  - Do you set salaries at the same level that formerly reflected total pay?
  - How do you handle pay management for people of clearly different skill levels?
  - How do you budget for total compensation without anticipating self-financing elements?
  - How do you tell people, “don’t worry about pay; enjoy the intrinsic awards”?



# The Obvious Question

Can we develop a culture that  
supports intrinsic motivation and  
offers extrinsic rewards?





Compelling Future

Positive Work  
Environment

Opportunities for Personal  
and Professional Growth

Financial Rewards

Compelling Future  
Purpose

Positive Work  
Environment

Opportunities  
Autonomy and Mastery

Financial Rewards

# Poll

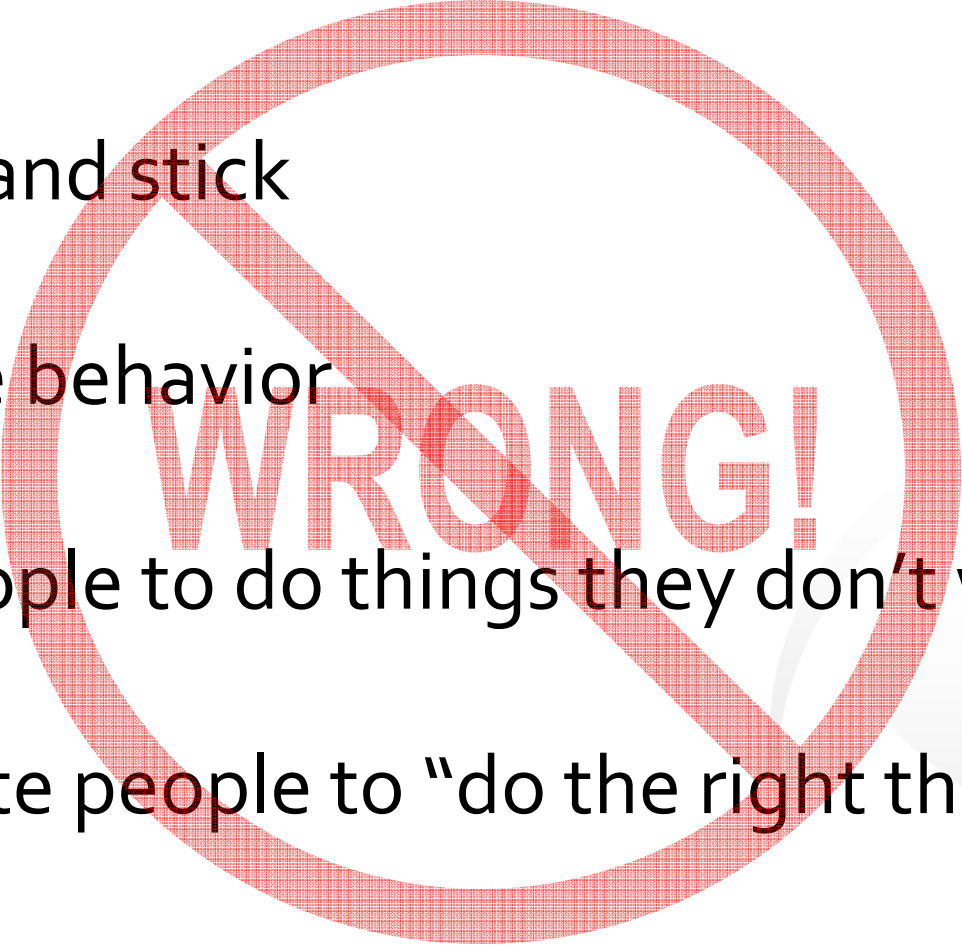


# Chapter Two

## Reinforce, don't force



# Purposes of the incentive plan

- 
- Carrot and stick
  - Change behavior
  - Get people to do things they don't want to do
  - Motivate people to “do the right thing”

# Purposes of a good incentive plan

- Demonstrate a financial partnership with employees
- Communicate the outcomes and results most valued by the organization
- Create flexible means of rewarding high performers and recognizing special circumstances and achievements

# Force

# Reinforce

This is the behavior that's expected and rewarded.

These are the results that are valued and rewarded.

Do these things whether you like them or not (they're a necessary part of the job).

As you can see the outcomes we're striving for, determine the best ways to get them done. Here are our standards, patterns, expectations.

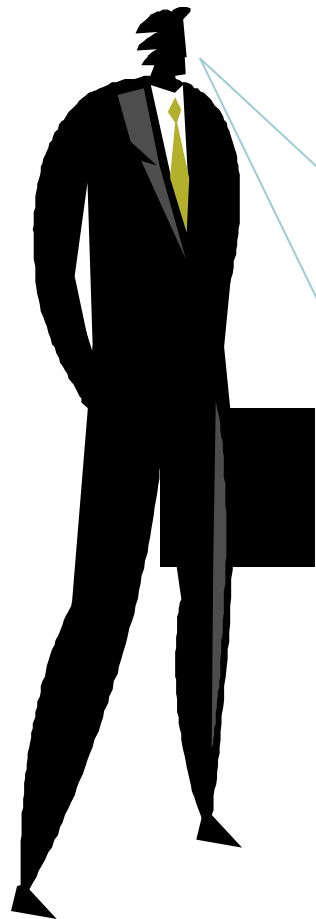
Our bonuses are reflective of our "market pay" analysis for your job classification

Our bonuses reflect the way we share value that you help create.

**Bad profits**

**Good profits**

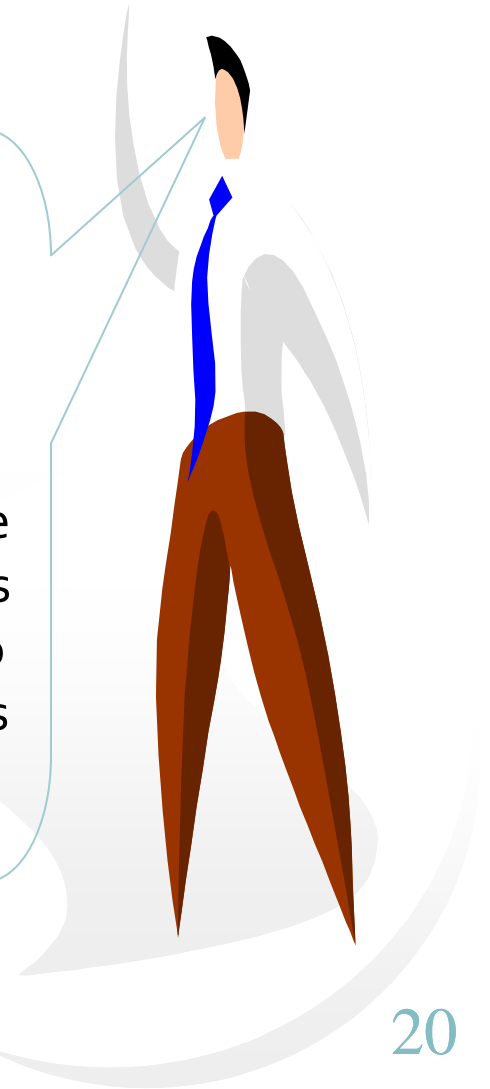
# Owner



Help us create financial value (good profits). We have a specific, proven and valuable way to share it with you.

# Employee

I see what business results create value. I understand how you share that value. It's meaningful to me. I see ways I can contribute.



This is fundamentally about fulfilling a commitment to reward people fairly (generously) for helping to fulfill the mission of the organization. When quality people understand and believe in this commitment you reinforce their intrinsic desire to deliver on your business plan.

# **Chapter Three**

## **Alignment**

# CEO Worry List



Sales

Productivity

Competitive Advantage

Execution

Talent

Not hitting  
sales targets

Sales not  
growing

# Sales

Sales cost  
too high





Gross  
profit/employee  
too low

Gross profit  
not improving

## Productivity

Headcount  
too high



Market share  
not improving

Return on  
equity not  
satisfactory

## Competitive Advantage

Market value  
not growing



Employees  
lack sense of  
urgency

Innovation  
cycle too long

Execution

Falling short  
of critical  
KPIs



Not employer  
of choice

Turnover  
too high

Talent

Talent level  
below desired  
standard



# Worry List

- No award should be generated unless improvements are made in one or more of these 5 strategic areas
- Must have ways to measure each
  - Sales growth—easy
  - Employee productivity—multiple metrics (see next poll)
  - Competitive Advantage—market share, ROE
  - Execution—critical KPIs, employee engagement
  - Talent—turnover, attraction strength

# Poll



# Addressing the Worry List

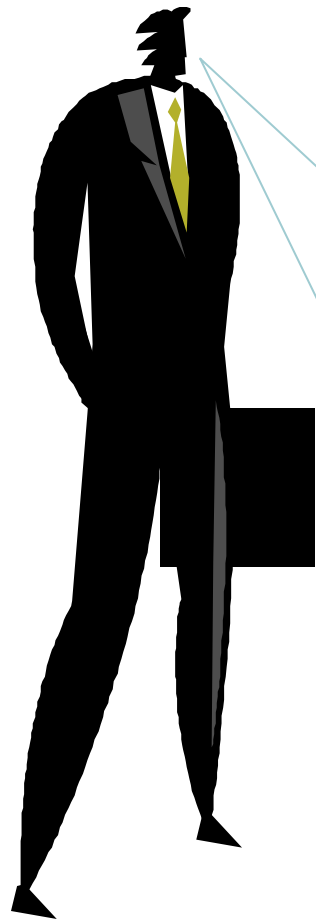
- New value is created (sustainable profits)
- Competitive advantage is enhanced
- Employer of choice
- The culture is all about execution

# Chapter Four

## Connect the Dots



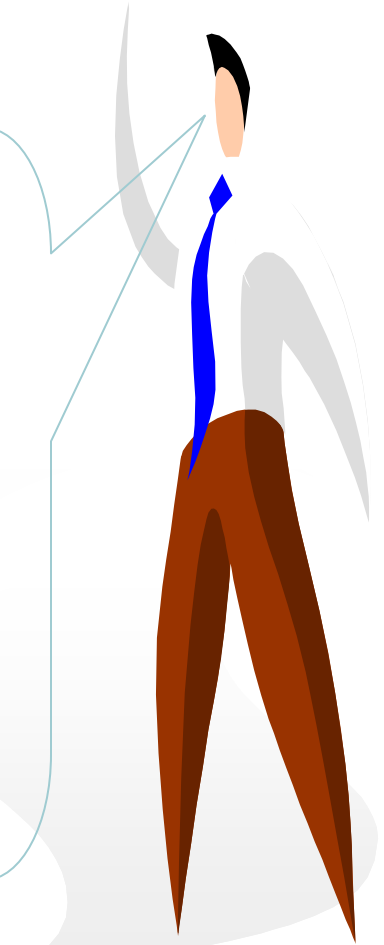
# Owner



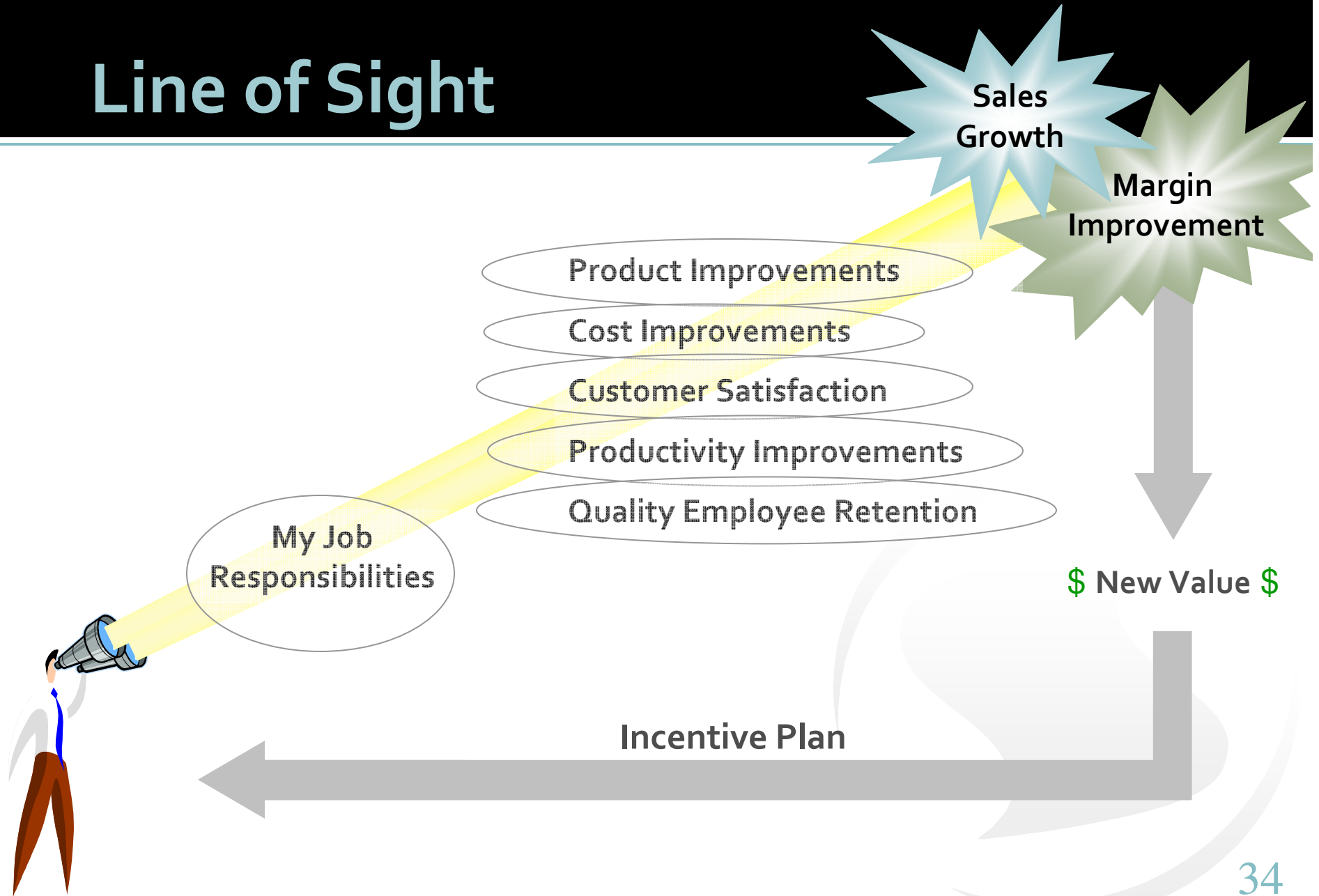
These are the things that are most important to our business success.

# Employee

I get it! I see how my job relates (and I see a future here). By the way, thanks for letting me share in the value.



# Line of Sight



# Rewards Pyramid



# Rewards to Results



# Chapter Five

## Don't Follow the Trend

# The Trend

- Short-term incentive plan
  - Profit-based
  - Target-based
- Some day—long-term incentive plan for senior executives

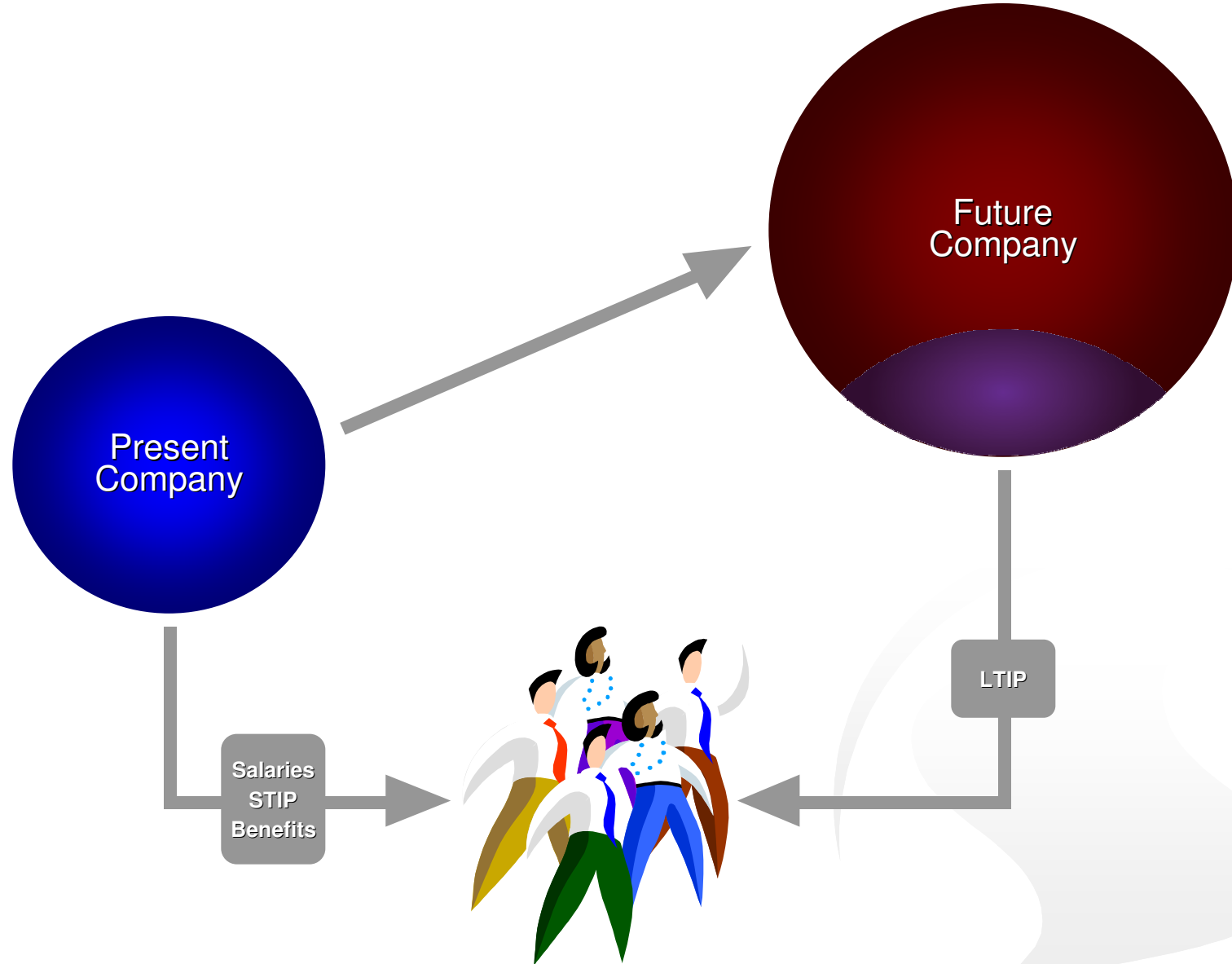
# Trend Breaker—Part 1

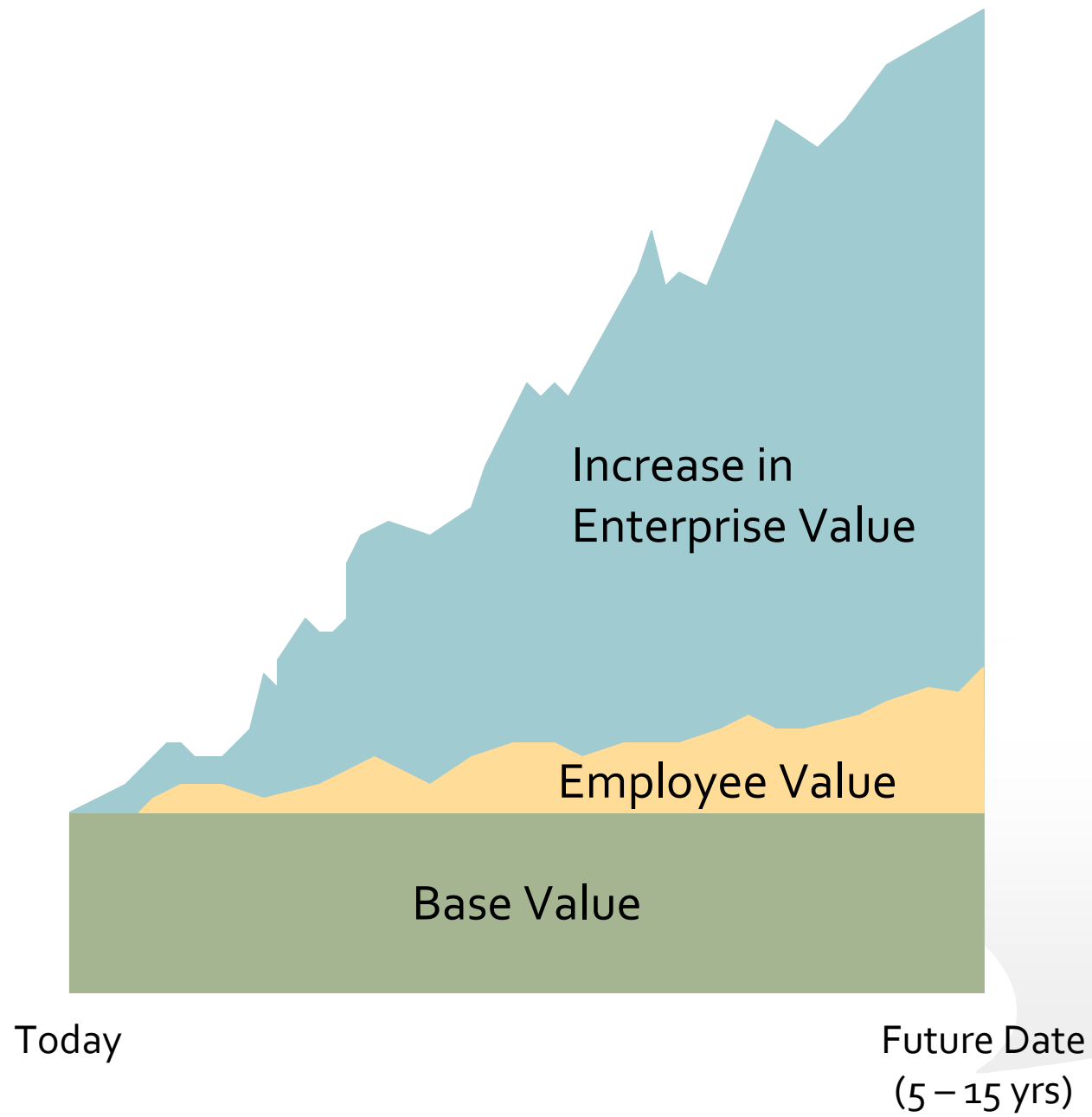
- Short-term Productivity Incentive
  - Recognizes both human and financial capital
  - Creates rewards pool for producing profits in excess of Return on Capital threshold
  - Pool allocated to employees based on evaluation process that recognizes contributions to “good profits”
  - (Stay tuned for a future presentation)

# Trend Breaker—Part 2

- Long-term incentive plan tied to growth and value creation goals
  - Estimate potential “new future value”
  - Determine portion to be shared
  - Determine best way to assign, measure, distribute, etc.
  - (See VisionLink’s Long-term Incentive Plan Decision Tree at [www.VLadvisors.com](http://www.VLadvisors.com))







# Why?

- Treats employees like true partners
- Allows for values to grow and mature
- Creates ownership mentality
- Strengthens both recruitment and retention
- Self-financing



# Fundamental Philosophy



Fair salaries, strong benefits, great upside for short- and long-term growth and profitability. We share the economic value our employees help create.

# Employee Value Statement for John Sample

	2010	2011	2012	2013	2014
<i>Total Rewards</i>					
Cash Received (Annual)	238,000	245,140	252,494	260,069	267,871
Value of Benefits Received (Annual)	15,200	16,440	17,795	19,276	20,896
Wealth Accumulation Earned (Annual)	62,926	92,509	126,302	164,831	208,685
Total Rewards Value (Annual)	316,126	354,089	396,591	444,176	497,452
<i>Cumulative Rewards Value</i>	\$ 316,126	\$ 670,215	\$ 1,066,806	\$ 1,510,982	\$ 2,008,434

# Do incentives work?

- No, if “work” means you can positively improve results by tying incentives to targeted KPIs
- Yes, if “work” means you can forge a stronger relationship with employees and engage them in a unified vision for growing the business

# Conclusions

- Don't expect a traditional incentive plan to improve productivity (if anything, it might make it worse)
- Employee perception of the plan is more important than the plan itself ("is this a game or is this for real?")



# Conclusions

- However, the lack of an incentive plan can make it difficult to:
  - Provide competitive pay structures without straining the budget
  - Fulfill the commitment to support long-term wealth opportunities for top performers

# Conclusions

- Utilize a short-term incentive plan that shares profits above a productivity threshold
- Utilize a long-term plan that shares an appropriate part of created wealth
- Build on a philosophy that treats employees like your most valuable asset

# First Step

- Where are we now?
- VisionLink's Tool:
  - Alignment Appraisal™
    - A focused look at your current practices with a comparative eye on “World Class Compensation” standards. “Is your total rewards program enhancing or slowing growth?”
    - Process—(1) employee survey, (2) current practices summary, and (3) completion of a profile questionnaire

# Quantitative and Qualitative Assessment

Function

Does the company develop and carry out an effective pay philosophy and associated strategies?

Passion

Is there a superior level of commitment and engagement on the part of employees that manifests itself in consistent execution?

Productivity

Is there a measurable return to shareholders that can be attributed to the contributions of employees, especially key talent?

Competitiveness

Is the company able to attract and retain superior talent and compete in the marketplace for the best people?

# Special Offer

This Appraisal is typically \$1,800.

For today's webinar attendees only:

*No cost if survey scheduled by  
February 10, 2010*

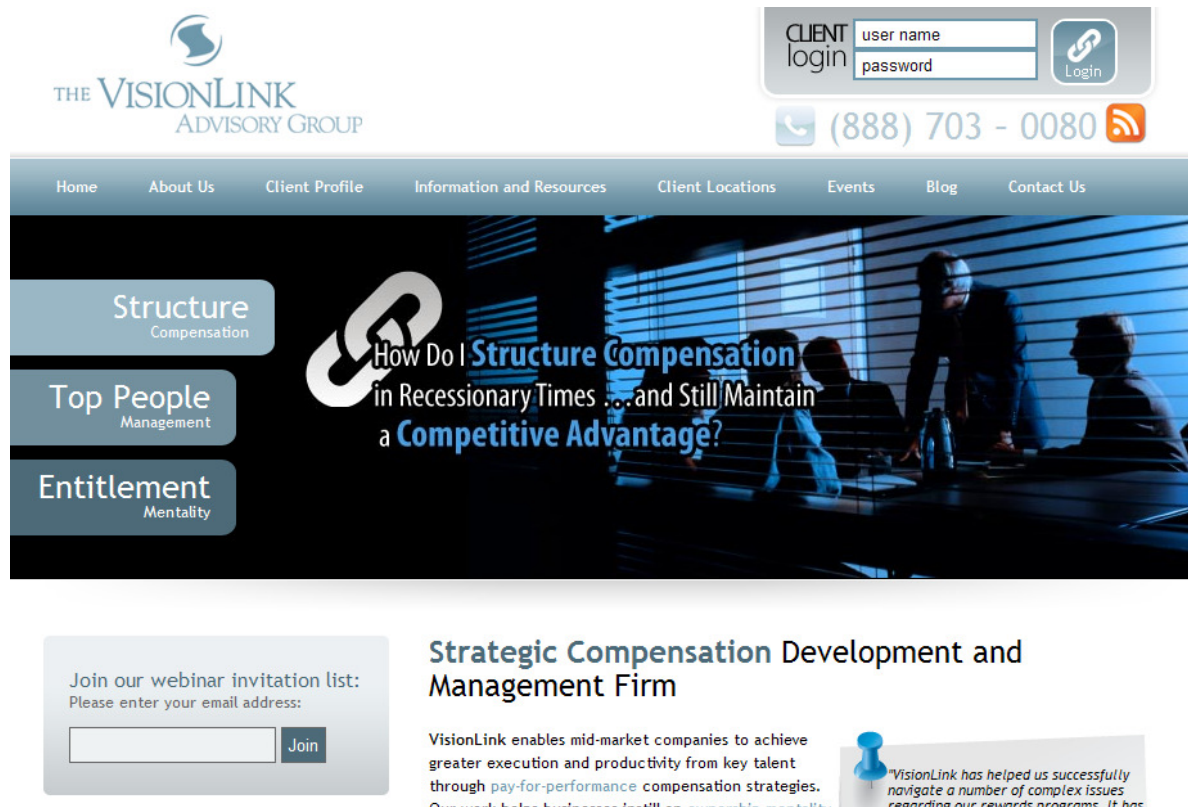
Indicate interest on final survey

# Next Online Seminar:

## “How Shareholders Should View Compensation”

To be held on:  
Tuesday, February 23<sup>rd</sup>, 2010

Check out our website:  
[www.VLadvisors.com](http://www.VLadvisors.com)



You can also subscribe to our blog

# Questions



# 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 and more information about the Alignment Appraisal™.*

# Thank you!



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