

The "Learn & Earn" Series™

July 19, 2012

"Do Incentive Plans Really Work?"



THE VISIONLINK
ADVISORY GROUP

Today's Presenter:

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Course Credit

Per State Requirements:

To receive CPE credit for today's course, you must respond to at least 75% of the monitoring events – given in the form of polls.

Each person taking the course must respond to the monitoring events from their own computer. You may not share a computer when taking the course

We're happy to provide a copy of today's slides and course syllabus/summary. 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

Course Objectives

- Understand the appropriate role of incentives
- Identify the key elements of an effective incentive plan
- Define the relationship between incentives and performance

Key Concepts



- Incentive plans can backfire
- Well-designed plans reinforce not force
- Incentive plans reward for results, not simply behavior
- World class incentives are trend breakers.

Chapter One

An interesting debate



The Compensation Environment

Issues in Current Economy:

Employers

- Concerned about adding to workforce but want to remain competitive
- Concerned about taking on fixed compensation commitments

Talent Pool

- *Unemployed* concerned about getting pegged at lower comp
- *Underemployed* concerned about ways to “leverage” opportunities
- *Satisfactorily employed* concerned about being paid for value they help create (discussions about equity, etc.)

Media

- Concerned about “fairness”

**This is not a new issue...
just a more public one**

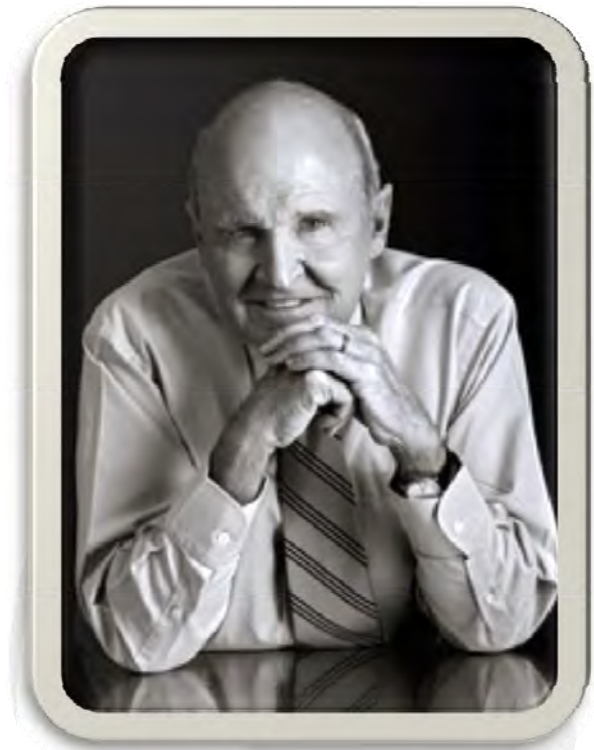


Remember Jack Welch?

\$9 million annual retirement benefit, plus perks—very controversial at the time

However...

- Less than 3/100ths of 1% of value created during his tenure (0.03 of \$396B)
- Total comp during his entire period of service was less than 2/10ths of 1%
- Would you pay that?



Value Sharing



Overarching Solution:

Value paid for value created

Share Value from Value Created

**Fast Company Blog:
"Superstar Athlete"
Compensation
by Kevin Kruse**

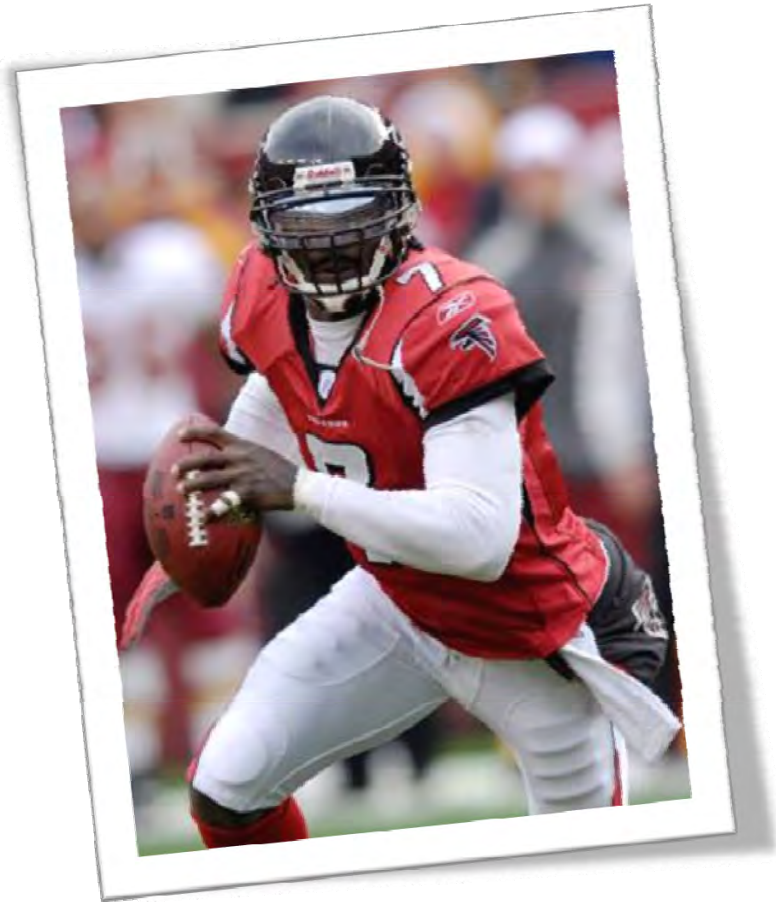


Fast Company Article

Michael Vick Comp Package:

\$100 million

Made him the highest paid athlete in the NFL, however...



Fast Company Article



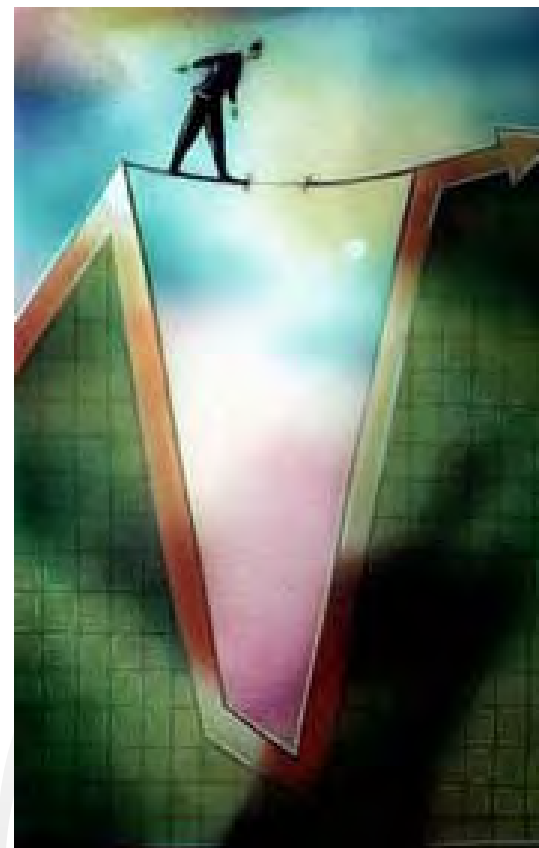
Michael Vick Comp Package:

\$100 million over six years

- *\$40 million guaranteed*
- *\$60 million at risk, based on performance*

For every \$1 of base pay Vick can earn an extra \$1.50 based on results

“This ratio provides the proper risk versus reward for both parties. Vick will earn his whopping \$100 million only if he stays healthy enough to lead the team for the next six years and only if he achieves certain on-field results. The variable amount in his contract must be ‘re-earned’ each year. **This demonstrates that organizations are willing to pay a high premium for great performance.**”





“This athletic analogy describes the concept of variable compensation (a model where an employee receives a low base and dramatically higher performance bonuses), and how risk-sharing (in this case between athlete and team) can be applied to help encourage more hiring by employers at a time when job creation globally is arguably our biggest economic challenge.

“With U.S. unemployment stuck at 9% and job creation on everyone's mind, why aren't more companies looking at this model?”

“While compensating employees like professional athletes--albeit on a smaller scale--might sound like a crazy concept, it has the potential to help overcome the current fears held by companies and the unemployed alike.”

Poll #1



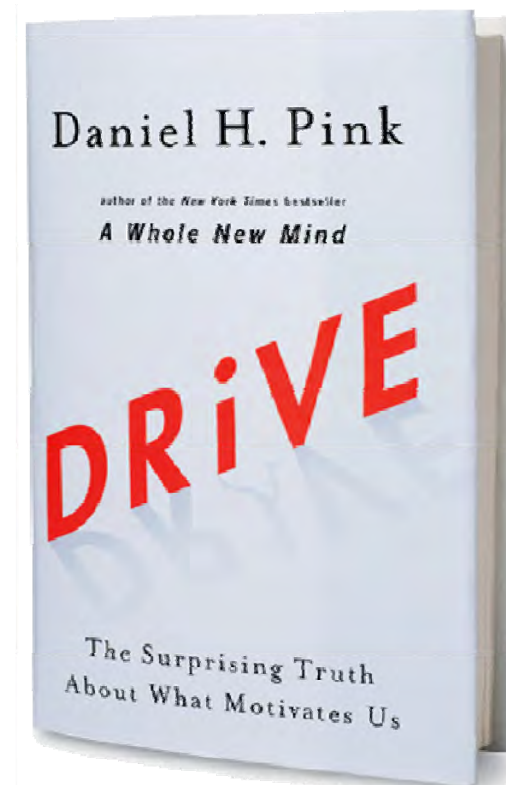
Current Questions



- Do Incentive Plans Work?
- CEOs: "I'm Paying \$1 Million to my Top 5 People, What am I Getting for It?"

Do incentives work?

Recent “discussion prompt”:
Dan Pink’s book—Drive



The Obvious Question

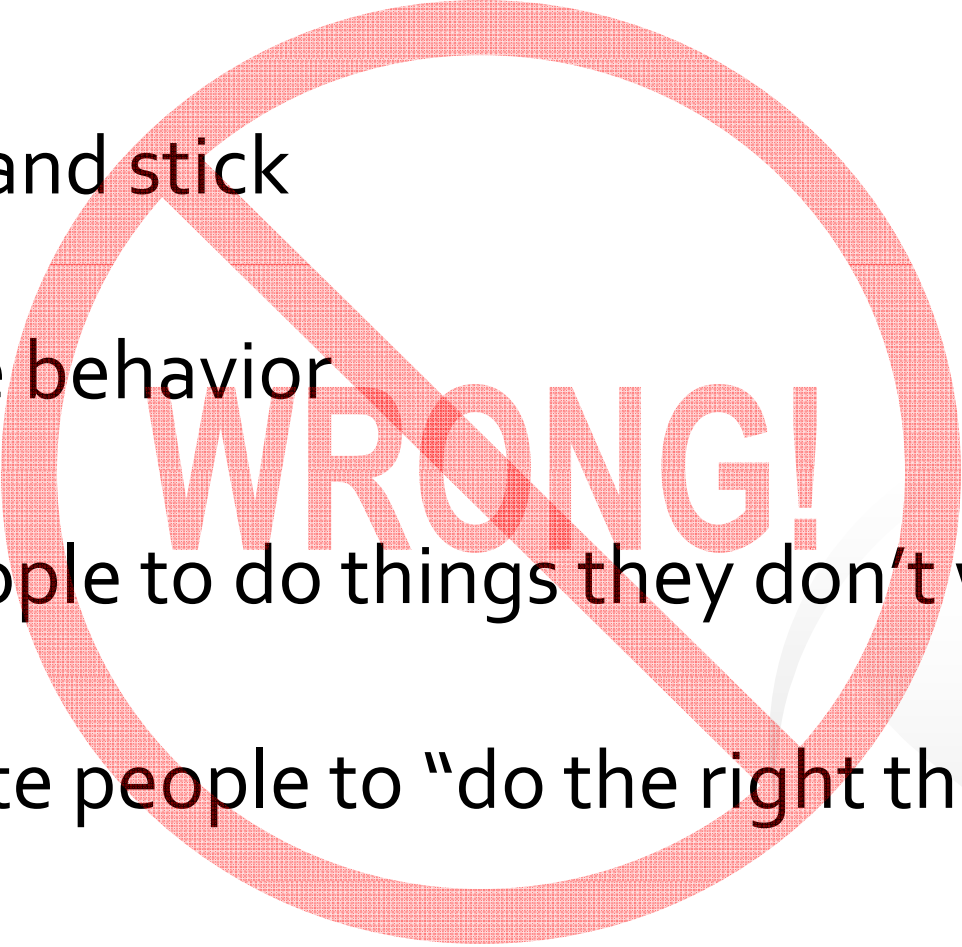
Can we develop a culture that supports intrinsic motivation and offers extrinsic rewards?



Chapter Two

Reinforce, don't force

Approaching Incentive Planning

- 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
- Communicate the outcomes and results
- Rewarding high performers
- Recognize special circumstances and achievements
- Build a unified financial vision



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

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



Fast Company Article



Michael Vick Comp Package:

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Chapter Three

The Rewards Strategy “Must”

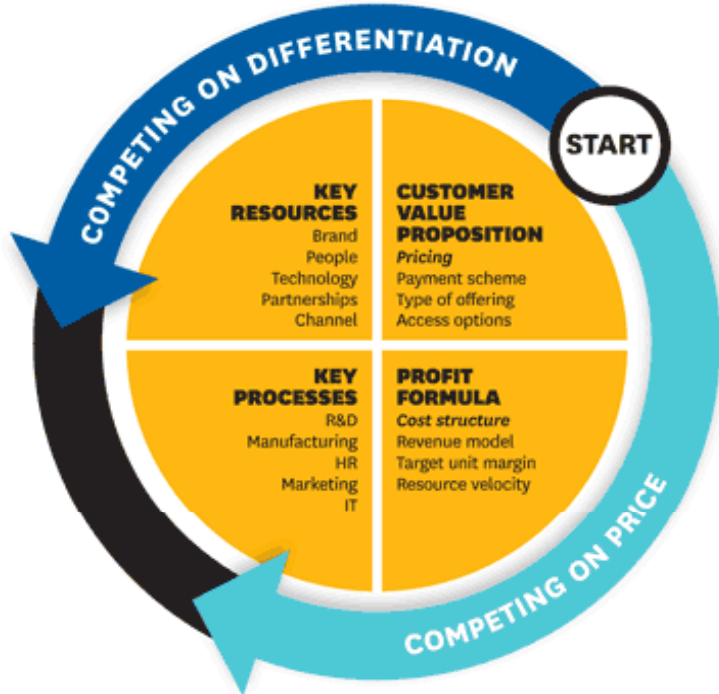
Purposes of a good incentive plan

Yes, it is to:

- 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
- Build a unified financial vision for growing the business



The "Must"



It **must** reinforce the logic of the business *model*, not just the business *strategy*

Graphic: Copyright, Harvard Business Review, January/February 2011 Edition

What are you trying to do when you introduce a new compensation plan?

Communicate what's important so execution will align with the business model



The Compensation Framework



Poll #2



Chapter Four Alignment



Key Business Issues

- Define and remove barriers to company progress
- Extend the core value offering & core audience
- Accelerate execution of business model, processes and strategies
- Identify & facilitate new growth drivers
- Maintaining the performance engine



Key Business Issues



- Expand the company's market reach & audience
- Stay ahead of trends and responsive to the marketplace
- Codify expectations and accountability
- Manage change and encourage innovation
- Become a magnet for the best talent
- Be a great company

CEO Worry List



Sales

Productivity

Competitive Advantage

Execution

Talent

Defining Value Creation

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



Addressing the Worry List

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

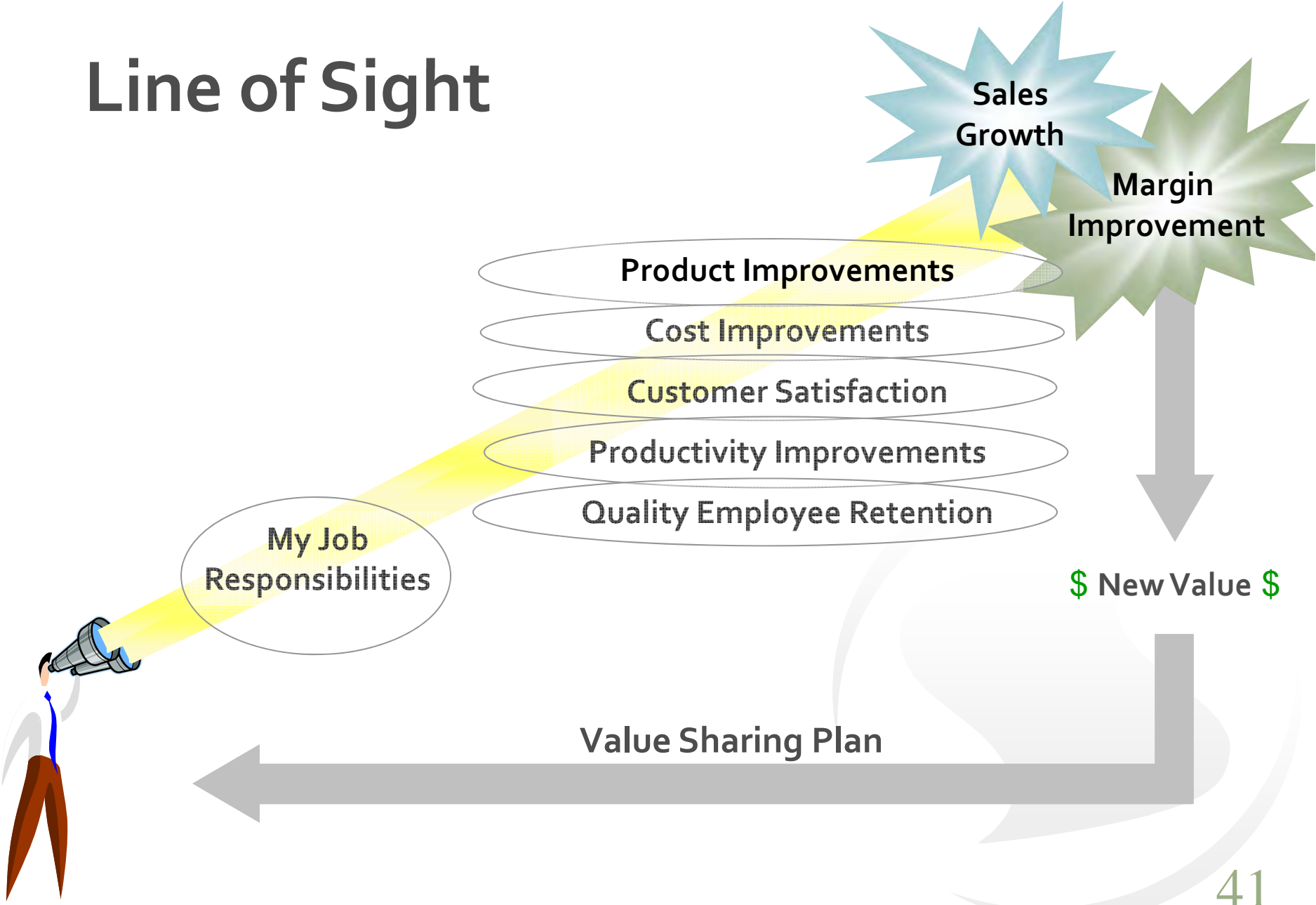


Chapter Five

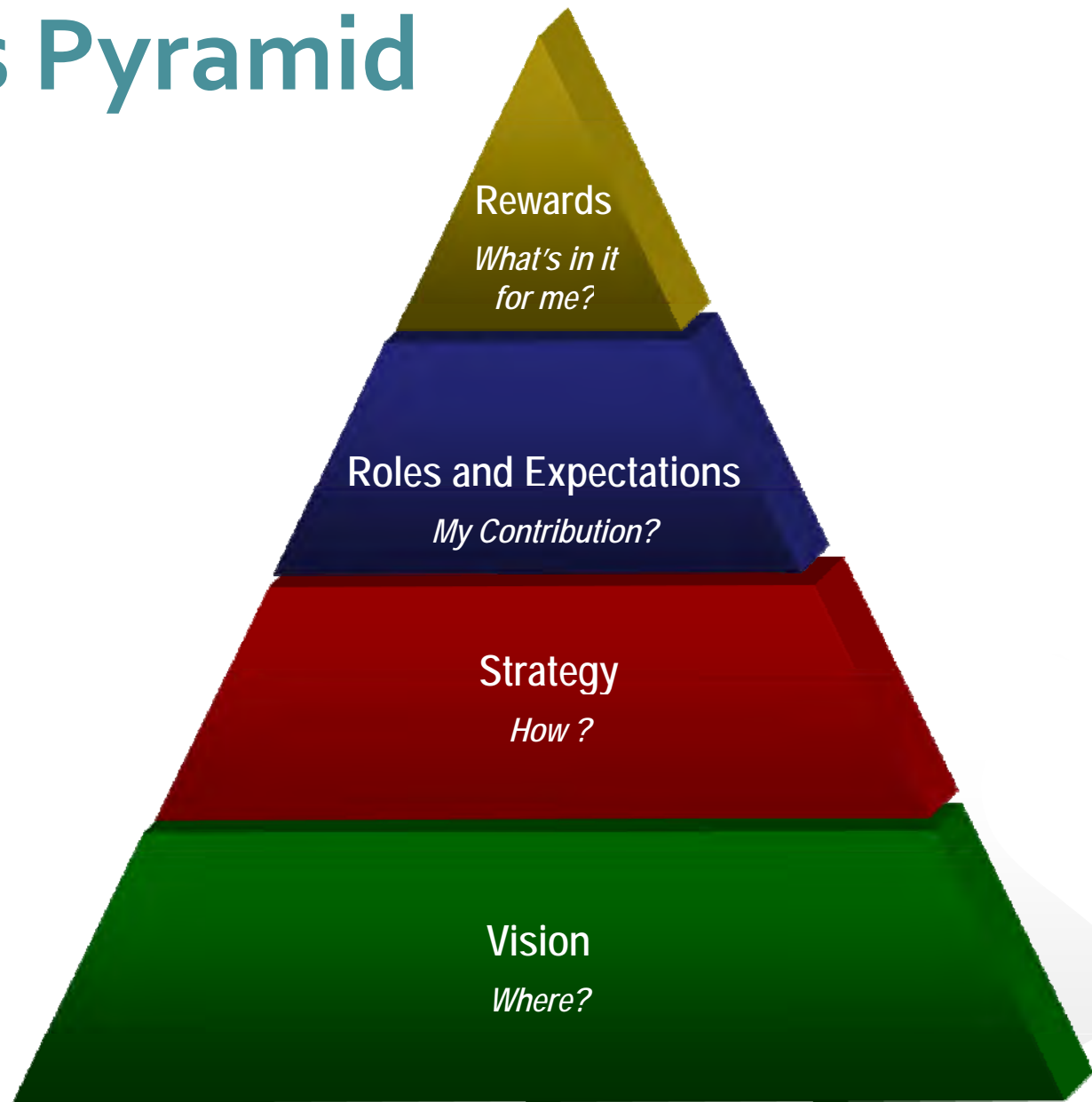
Connect the Dots



Line of Sight



Rewards Pyramid



Rewards to Results



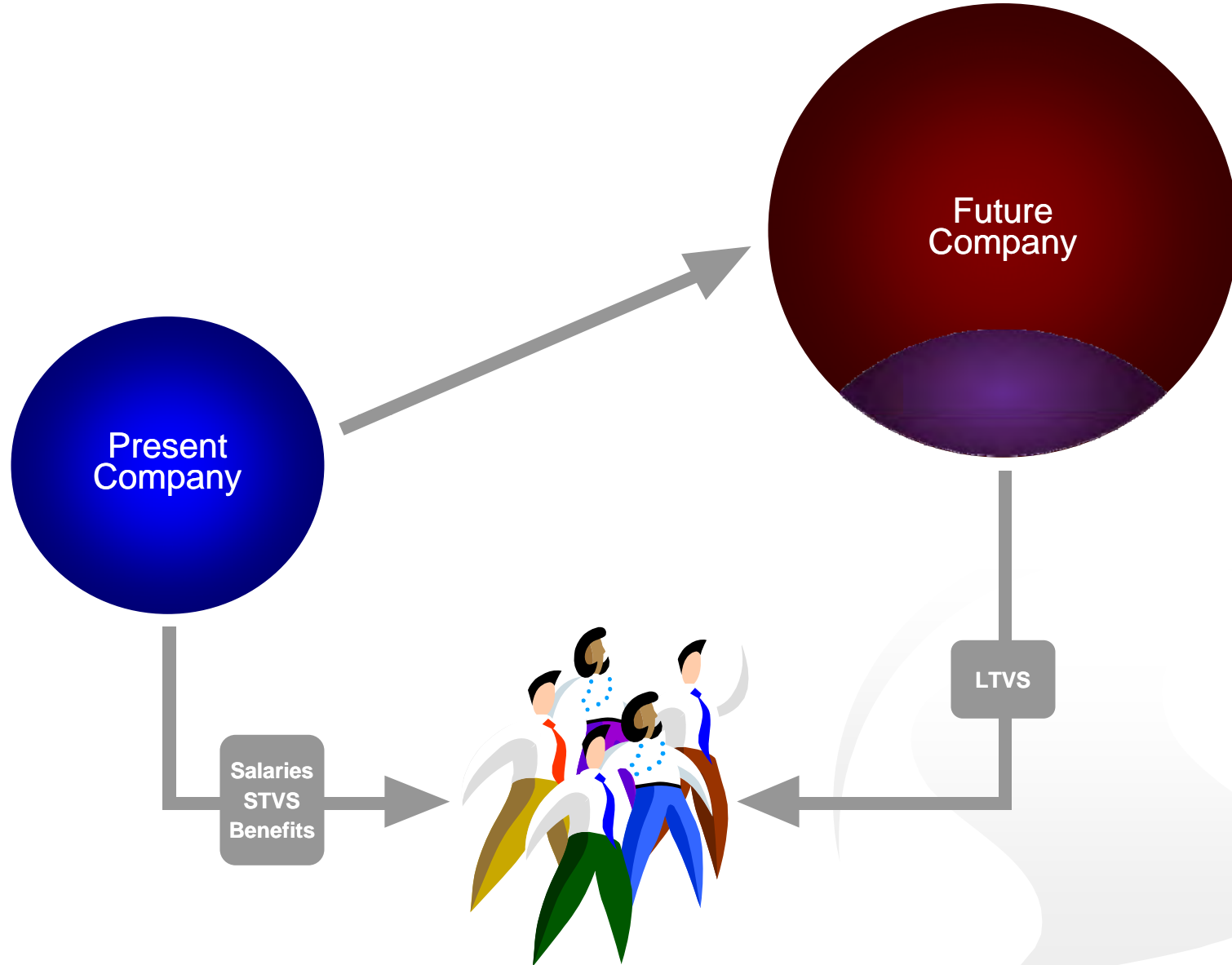
Chapter Six

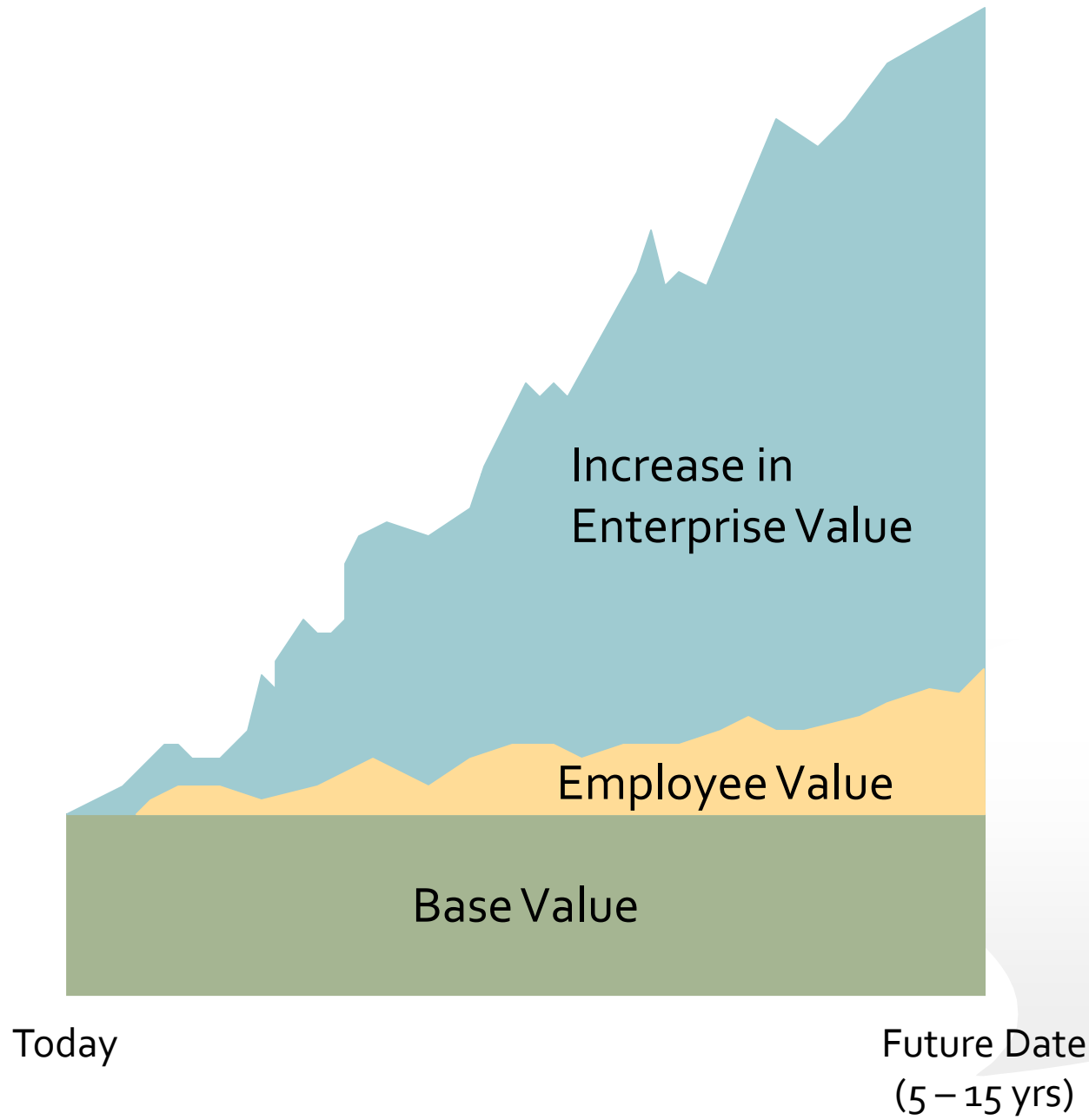
Don't Follow the Trend

The Trend

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







Why?

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



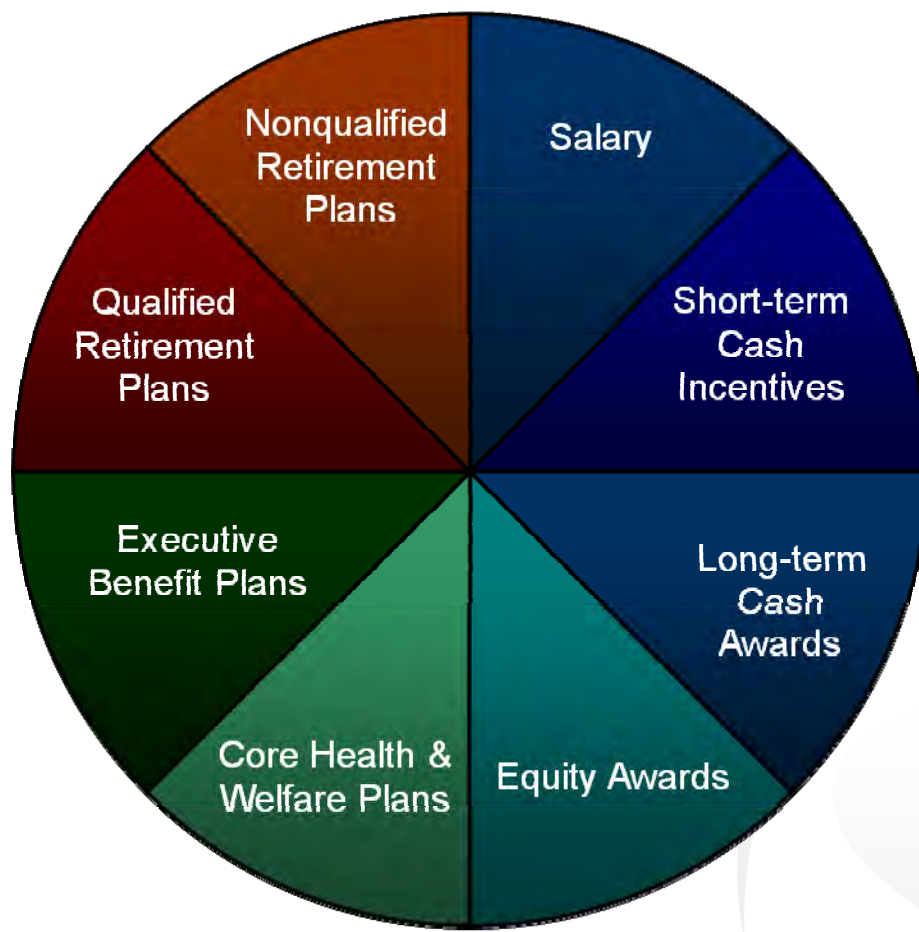
Poll #3



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.



Form of Pay	Purpose	Standard	Investment	ROI
Salaries	Provide for the current cash needs of our executives	40-50th percentile for peer group	\$500,000	Achieve ROA standard of 0.75%
Short-term Incentives	Enhance current cash payments to executives for achieving top and bottom line annual goals	30-40% of base salary	\$168,000 (Target)	15% revenue growth and 12% margin
Long-term Incentives (Cash)	Retain execs; focus them on long-term earnings growth; align with shareholder interests; meet wealth accumulation needs	15-20% of base salary	\$84,000 (Target)	Long-term growth in earnings (double earnings = share 13% of new value)
Long-term Incentives (Equity)	Retain execs; focus them on long-term earnings growth; align with shareholder interests; meet wealth accumulation needs	15-20% of base salary	\$84,000 (Target)	Long-term growth in earnings (double earnings = share 13% of new value)
Core Benefits	Meet basic security needs of the executives	50th percentile for peer group	\$25,500	ROA of 0.75%
Executive Benefits	Enhance basic security needs and meet market standards for perquisites	50th percentile for peer group	\$24,000	ROA of 0.75%
Qualified Retirement	Provide wealth accumulation opportunity for executives	40th percentile (3% of salary)	\$15,000	ROA of 0.75%
Supplemental Retirement	Strengthen rewards value proposition to help recruit and retain executives; meet wealth accumulation needs	30th percentile compared to companies that have plans	\$135,000	ROA of 0.9%

Employee Value Statement

Year	1	2	3	4	5
5-Year Plan Achievement Level	100%	100%	100%	100%	100%
Current and Inflated Salary	\$ 160,000	\$ 166,400	\$ 173,056	\$ 179,978	\$ 187,177
Cash Incentives Paid at Target	\$ 64,000	\$ 66,560	\$ 69,222	\$ 71,991	\$ 74,871
LTIP Vested Value at Year End	\$ -	\$ 74,000	\$ 186,000	\$ 311,000	\$ 448,000
Retirement Plan Value (at 7%)	\$ 17,120	\$ 36,123	\$ 57,169	\$ 80,428	\$ 106,086
Total Cash Received	\$ 224,000	\$ 232,960	\$ 242,278	\$ 251,970	\$ 262,048
Total Wealth Accumulation	\$ 17,120	\$ 110,123	\$ 243,169	\$ 391,428	\$ 554,086
Total Paid or Accumulated	\$ 241,120	\$ 567,083	\$ 942,407	\$ 1,342,636	\$ 1,767,343

When Incentive Plans Work, and When they Don't

- DON'T, if “work” means you try to positively improve results by tying incentives to targeted KPIs designed to manipulate behavior
- DO, if “work” means you use them to forge a stronger relationship with employees and engage them in a unified vision for growing the business



Next CPE Course:

“The Eight Fatal Compensation Mistakes”

To be held on:
Thursday, November 1, 2012

If you have three or members that can attend, we will make a specific presentation just for your firm on a mutually agreed upon date.
(Indicate interest on survey.)

Next Public Webinar:

“Success Stories in Pay for Performance”

Next Tuesday,
July 24, 2012

Check out our UPDATED website:

www.VLadvisors.com

The screenshot shows the homepage of The VisionLink Advisory Group. At the top left is the logo, and at the top right is a 'Client Login' button and a phone number: (888) 703 0080. A navigation bar contains links for Home, About Us, Client Profile, Knowledge Center, Speaking Engagements, Events, Blog, and Contact Us. The main content area features a large image of a mountain peak. Below the image are three article teasers: 'WHAT IS PHANTOM STOCK?', 'HOW SHOULD I SHARE VALUE?', and 'HOW DO I END ENTITLEMENTS?'. To the right of the image is a featured article titled 'How should I Share Value?' with a 'Learn More' button. Below the main content is an 'Events' section with a list of dates and topics, and a 'Join our webinar invitation list' section with an email input field and a 'Go' button. At the bottom, there are three columns with the headings 'ASK THE RIGHT QUESTIONS', 'FOLLOW THE RIGHT PROCESS', and 'CHOOSE THE RIGHT COACHES', each with a brief description.

You can also subscribe to our blog

Check out our NEW website:
www.PhantomStockOnline.com

The screenshot shows the Phantom Stock website homepage. At the top left is the logo "Phantom Stock The Equity Alternative" with a green arrow pointing up and to the right. To the right of the logo is a dark green navigation bar with white text: "KNOWLEDGE CENTER", "TOOLS", "BUILD A PLAN", "BLOG", "ABOUT US", and "CONTACT". In the top right corner, it says "POWERED BY VISIONLINK".

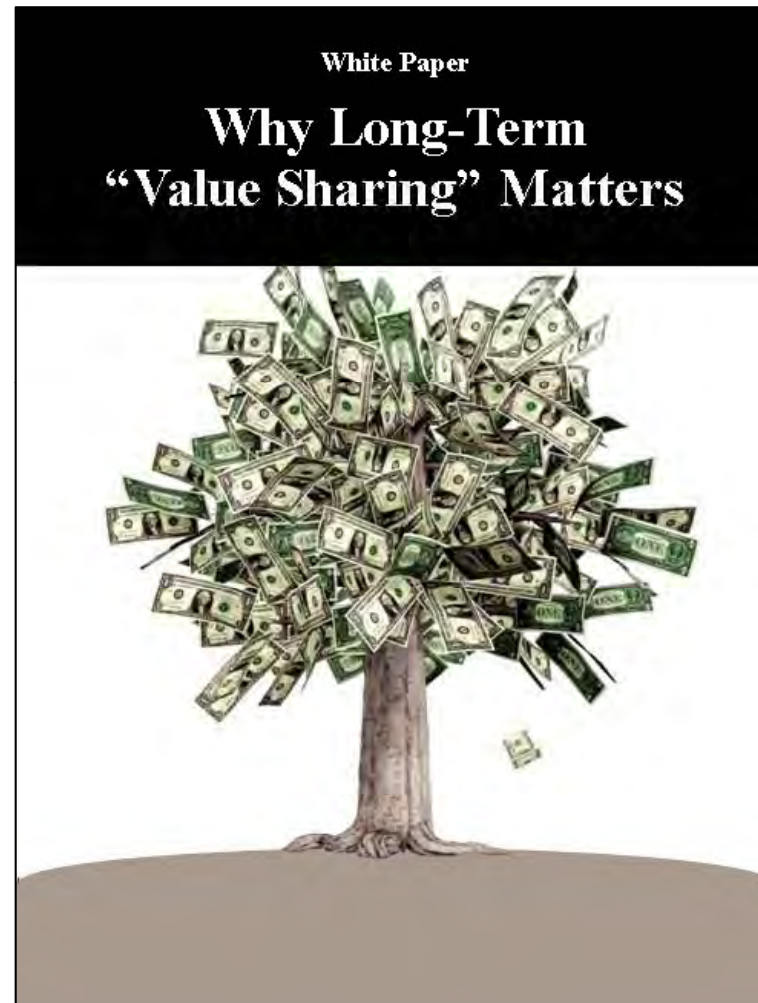
The main content area features a large light gray banner. On the left, there are three stacked green arrow-shaped buttons pointing right, labeled "WHAT IS IT?", "WHAT WILL IT CHANGE?", and "WHERE DO I BEGIN?". To the right of these buttons, the text "A way to share ~~equity~~ Value" is displayed, where "equity" is crossed out and "Value" is written in red cursive. In the top right corner of the banner, there is a red play button icon and the text "Phantom Stock Watch overview".

Below the banner is a grid of four white boxes, each with a title, an icon, and a short description:

- KNOWLEDGE CENTER**: Icon of a blue circle with a white 'i'. Description: "Explore our wiki and find the answers to your Phantom Stock questions."
- TOOLS**: Icon of a brown briefcase. Description: "Decide whether Phantom Stock is a fit for your company."
- BUILD A PLAN**: Icon of crossed wrench and screwdriver. Description: "For 'do-it-yourselfers.' Follow this guide to create your own plan."
- BLOG**: Icon of an orange RSS symbol. Description: "Read the latest discussions about Phantom Stock and other value sharing strategies."

At the bottom of the page is a dark green footer bar with white text: "Knowledge Center Tools Build a Plan Blog About Us Contact" on the left and "© 2010 PhantomStockOnline.com" on the right.

NOW AVAILABLE!



Express interest on the final survey

Thank you for attending

Please complete our survey form immediately following our presentation.

This will be counted as a monitoring event.

You may also request a copy of the slides from today's presentation

Questions?



Thank You!



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