

February 24, 2015

Compensation Your P&L Will Love



THE VISIONLINK
ADVISORY GROUP

Today's Presenter:

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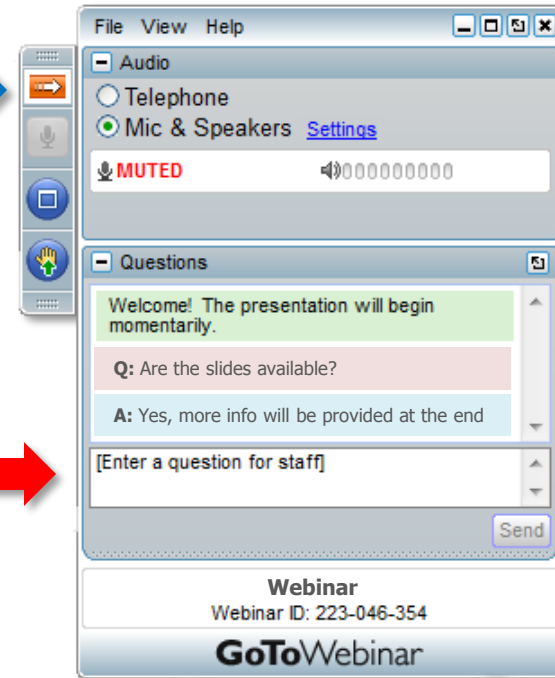
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Information will be provided at the close
of the presentation.

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The VisionLink Advisory Group

- Founded in 1996
- 6 consultants with over 140 years experience
- Over 450 Clients in North America
- Focus: Compensation management that drives growth
- “VisionLink” = rewards alignment between shareholders and employees

Our Goal: Improve the P&L through Comp



How?

Shareholders/CEO

1 Build

**RIGHT BIZ MODEL
SOUND BIZ STRATEGY**



2 Communicate
& Reinforce



3 Attract
& Retain

**ENGAGED
OWNER-EMPLOYEES**

4 Innovation
Execution
Accountability



**HIGHER VALUE
SHARING FOR
EVERYONE**

**HIGHER
PRODUCTIVITY**

5



Focus first on ENGAGEMENT

- An "engaged employee" is one who is fully absorbed by and enthusiastic about their work and so takes positive action to further the organization's reputation and interests. *(highly reliable source)*
- **Strongest indicator of likelihood of productivity gains**



Next: PRODUCTIVITY GAINS

- Productivity is an average measure of the efficiency of production. *(same reliable source)*
- For our purposes, productivity is created in the “real process” and “productivity gains” are distributed in the income distribution process.
 - Your business operations = the real process
 - Your sharing of gains between shareholders and employees = income distribution process

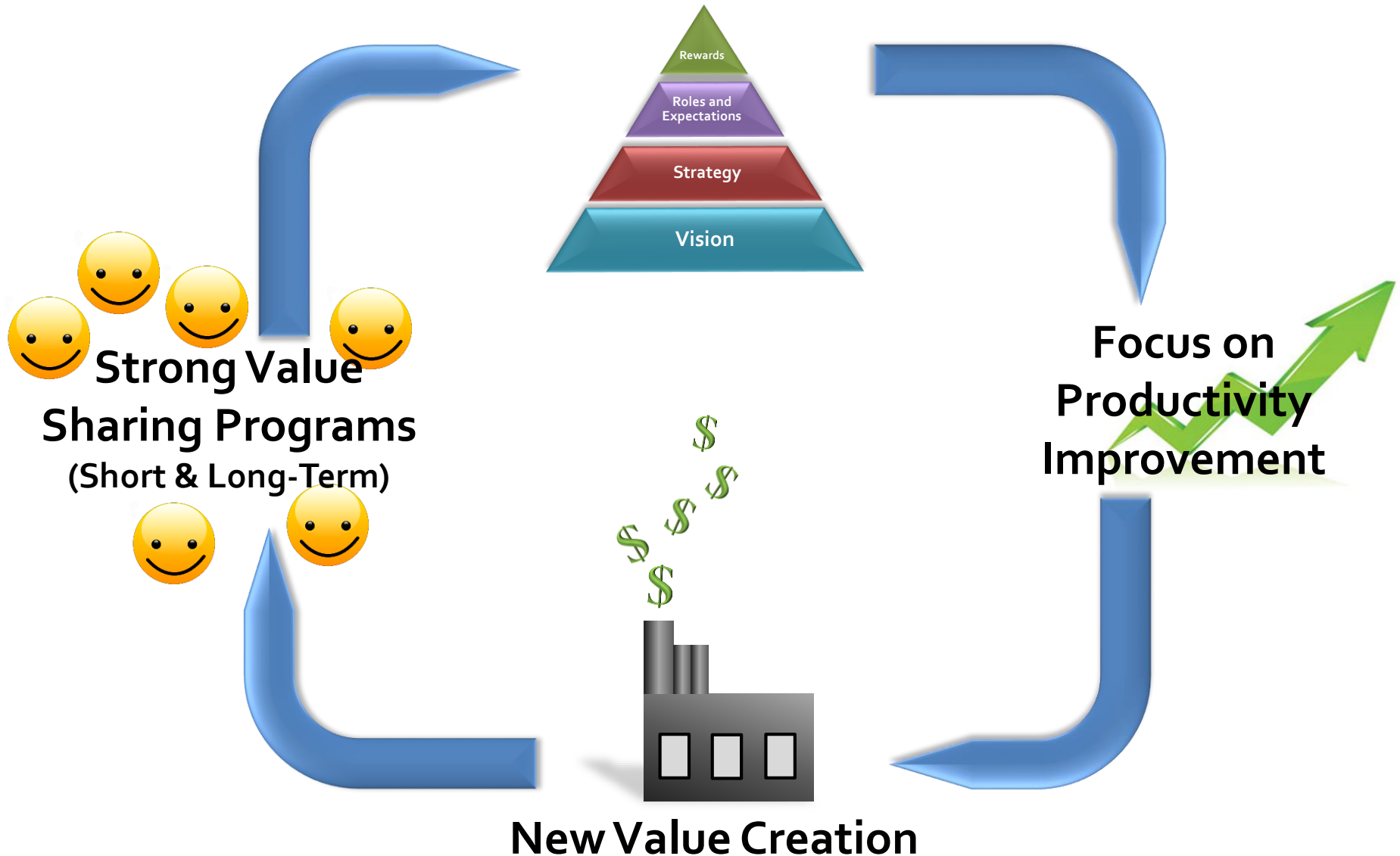


Results of productivity gains

- Something(s) happening faster, cheaper, easier, better
- Will translate to profitability and shareholder value creation
- Should all that value go to shareholders?
 - If yes, indication of a weak value sharing culture; limited opportunity to use the rewards programs to reinforce a partnership culture
 - If no, need a connected rewards program to walk the talk

So let's identify the steps taken by great organizations that are striving to use compensation as a tool for improving productivity—thereby satisfying shareholders. And let's see if this is measurable (provable).

Ownership Mentality



Let's break it down:

- How does the biz model link to pay?
- What's the pyramid got to do with it?
- Why does this produce engaged employees?
- How can we measure productivity improvements and link to pay?
- What approach to compensation plans improves the P&L?



Part 1

Linking the Business Model to Pay Philosophy



Every company searches for an approach to pay that suits their philosophy, values and goals.

Let's call this a pay philosophy.

Here's an example.

<https://open.bufferapp.com/introducing-open-salaries-at-buffer-including-our-transparent-formula-and-all-individual-salaries/>

Bufferapp.com's transparent pay approach

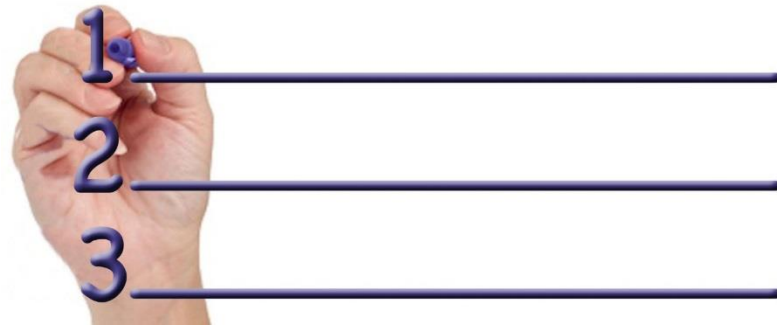
- Open salaries (everyone see's everyone's salaries)
- All salaries are formula driven:
 - Salary = job type X seniority X experience + location

Team Member Details - Fill out this section :-)								Salary
#	Team Member	Role	Experience	Location	Seniority	Choice	Co. Size	
1	Joel	Executive Officer	Advanced	A	CEO	Equity	1-2	\$175,000
2	Leo	Operations Officer	Advanced	A	COO	Equity	1-2	\$161,000
3	Andy	Engineer	Intermediate	SF Engineer	Senior	Salary	3-6	\$124,000
4	Sunil	Engineer	Master	A	C-Level	Salary	3-6	\$163,000
5	Carolyn	Happiness Officer	Advanced	A	C-Level	Equity	3-6	\$148,000
6	Asa	Happiness Hero	Advanced	A	Senior	Equity	7-15	\$84,000
7	Colin	Engineer	Advanced	B	Senior	Salary	7-15	\$102,000
8	Brian	Product Manager	Intermediate	SF Engineer	Senior	Salary	7-15	\$135,000
9	Niel	Engineer	Advanced	C	Senior	Salary	7-15	\$96,000
10	Mary	Happiness Hero	Advanced	A	Senior	Equity	16-30	\$84,000
11	Adam	Happiness Hero	Advanced	B	-	Salary	16-30	\$76,000
12	Daniel	Weekend Warrior	Intermediate	A	-	Equity	16-30	\$71,500
13	Steven	Engineer	Advanced	C	-	Salary	16-30	\$88,000
14	Courtney	Content Crafter	Advanced	B	Senior	Equity	16-30	\$80,000
15	Dan	Engineer	Advanced	A	Senior	Salary	16-30	\$112,000
16	Patrik	Happiness Hero	Advanced	C	-	Equity	16-30	\$60,000
17	Kevan	Content Crafter	Advanced	C	Senior	Salary	16-30	\$84,000
18	Dave	Weekend Warrior	Advanced	A	-	Equity	16-30	\$76,000
19	Rodolphe	Onboarding Specialist	Advanced	A	-	Equity	16-30	\$88,000
20	Michael	Engineer	Advanced	C	-	Salary	16-30	\$88,000
21	Nicole	Happiness Hero	Intermediate	B	-	Salary	16-30	\$71,500
22	Octavio	Happiness Hero	Intermediate	B	-	Salary	16-30	\$71,500
23	Tom	Engineer	Advanced	B	-	Equity	16-30	\$84,000

What are Buffer's stated goals?

- Greater productivity
- More transparency
- Happier work culture

Setting Goals



Admirable

- Openness/transparency
- Simple (anyone can understand the formula)
- Striving to promote “equity,” and “team camaraderie”
- Predictable/manageable (reduce debates over fairness)

The most important thing about a pay philosophy is to have one.

Buffer has one. It fits their culture.
Hopefully, it fits their business model.



What may be missing

- Does it recognize and reward innovation and independent value creation?
 - No, it focuses on seniority, experience and location.
 - It presumes innovation and value creation will be recognized in other ways (or that they're not important, or don't need to be recognized)
- Does it assume that experience = capability and contribution?
 - Possibly
 - Or it's ignoring the correlation (or lack thereof)

My point

- I'm not knocking Buffer's pay philosophy
- I'm only saying that it's not for all companies

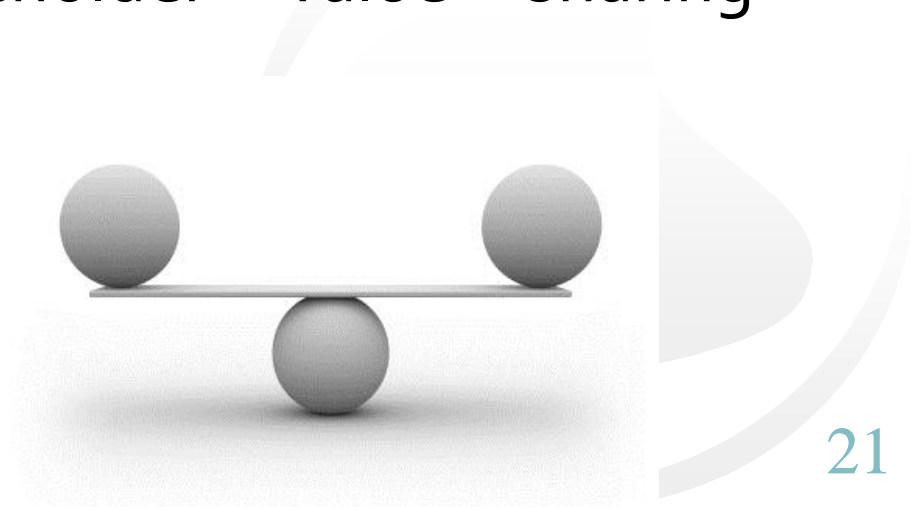


Compensation Philosophy

Defines your beliefs about pay

Lets employees understand the principles and policies that will guide pay decisions

For shareholders, it establishes an understanding of how the employee-shareholder value sharing relationship will operate.



Two Stories

Company A

- Large Call Center
- Workforce – Recent College Grads and Single Mothers
- Owner's primary goal: stabilize turnover and reduce costs
- Incentives: a tool for employee retention and recognition

Company B

- Web Based Technology Company
- Workforce – High Performing, Entrepreneurial
- Owner's primary goal: grow company
- Incentives: a tool for rewarding for product innovation

Two Stories

Company A

- Compensation Philosophy highlights fixed pay over variable pay
- Total Rewards Investment emphasizes Base Salaries & Core Benefits

Company B

- Compensation Philosophy is to highlight variable pay
- Total Rewards Investment emphasizes both short-term and long-term incentives

Conservative Pay Profile

Profile	Base Pay	Short-Term Incentives	Long-Term Incentives	Core Benefits	Retirement
Conservative	High	Low	Moderate	High	Moderate

Provides a high degree of employee security at the expense of variable pay

High base salaries and low incentives

Generally offers high level of core benefits

Cash friendly stable organization

Generally attractive to a younger employee population

Can inhibit the hiring of “high performers”

Rewards performance through merit/promotion

Retains executive leadership through moderate long-term awards

Variable Pay Profile

Profile	Base Pay	Short-Term Incentives	Long-Term Incentives	Core Benefits	Retirement
Variable	Low	High	High	Moderate	Moderate

Provides a high degree of upside earning potential with higher level of risk

Base salaries at or below market

Rewards tied directly to business performance

Entrepreneurial mindset – less cash friendly

Attracts high performers, frightens risk averse

Rewards performance through incentive pay

Promotes high level of value sharing

Attracts entrepreneurial leadership through long-term awards

Moderate Pay Profile

Profile	Base Pay	Short-Term Incentives	Long-Term Incentives	Core Benefits	Retirement
Moderate	Moderate	Moderate	Moderate	Moderate	Moderate

Provides a middle of the road approach to pay

Base salaries at market

Some upside incentive potential

Performance rewarded moderately

Attracts a diverse employee population

Rewards performance through multiple facets

Tries to provide a balanced approach without any distinguishing element of pay

First action

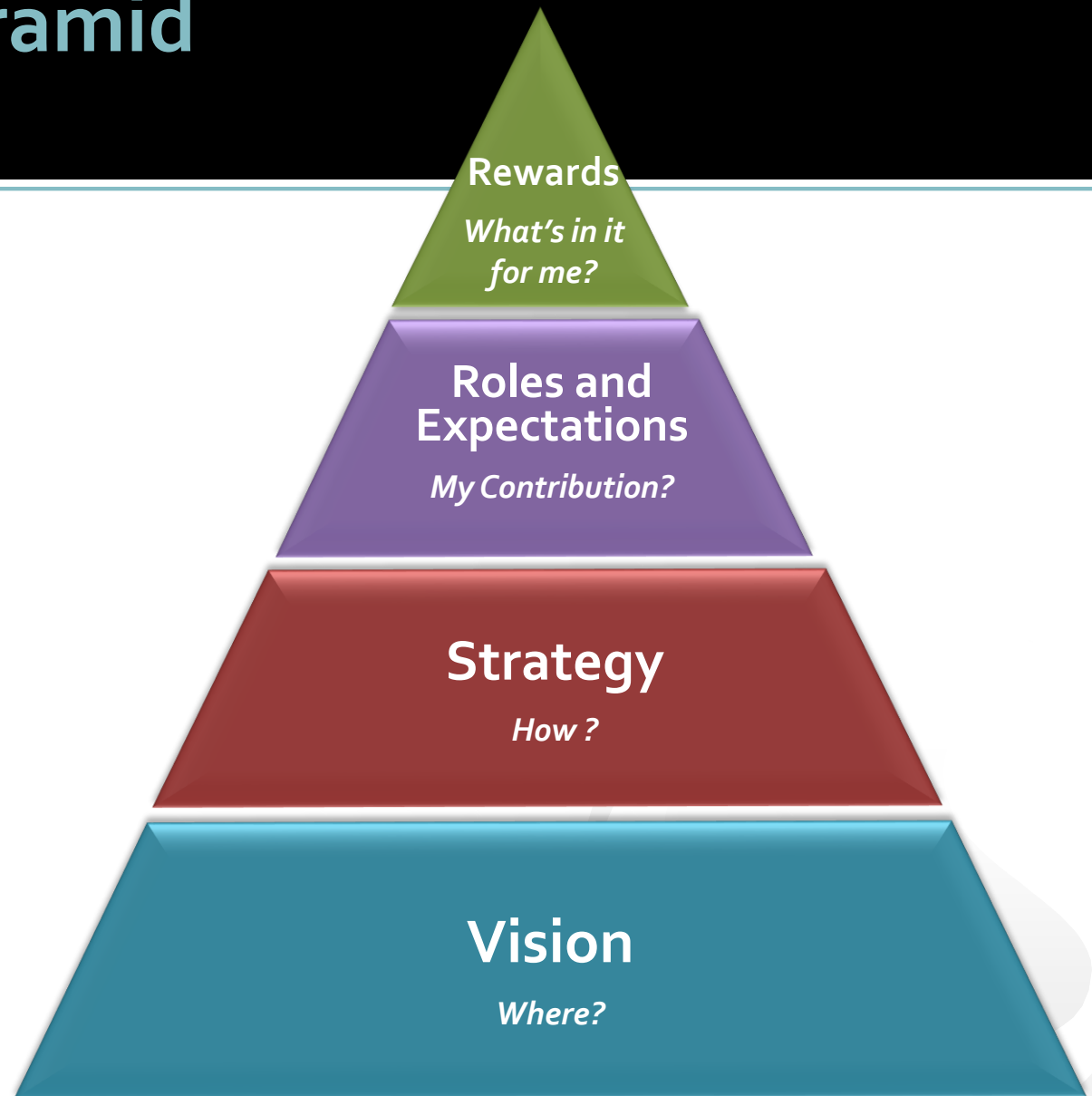
Define your pay philosophy. Write it down.
Make it clear. Get everyone to understand it.

"Choose carefully what you pay for because
you'll likely get more of it."

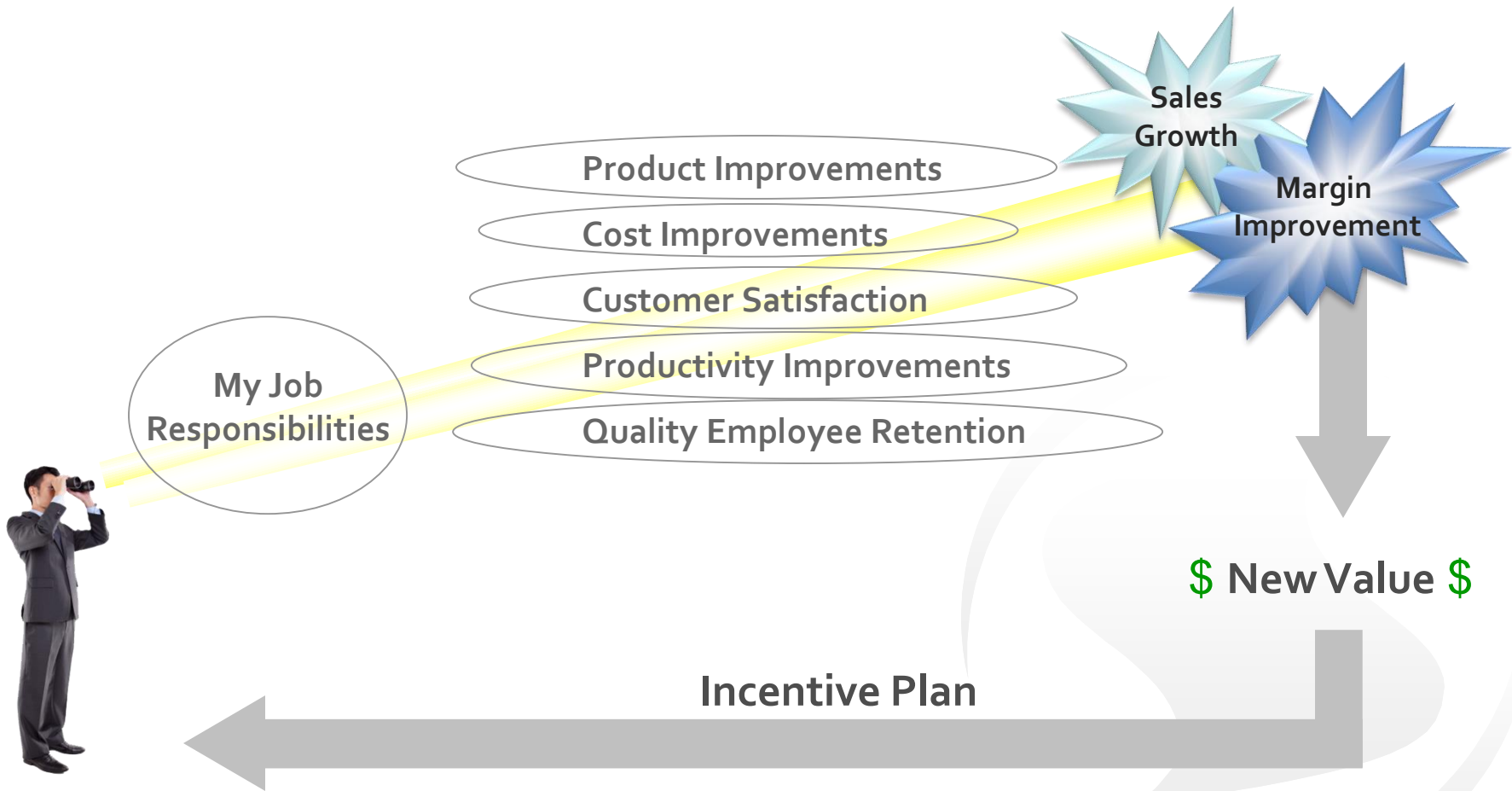
Part 2

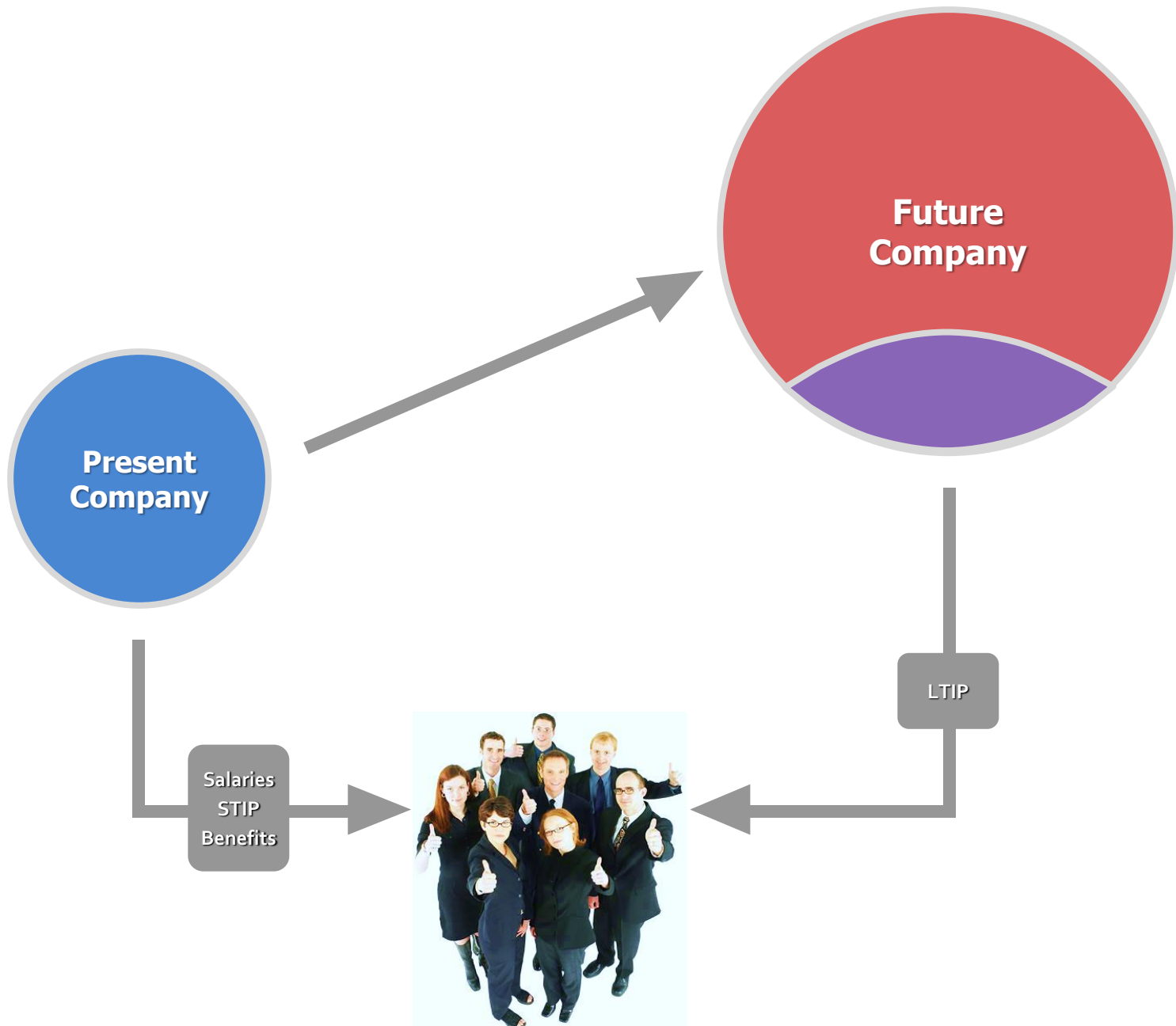
The Rewards Pyramid

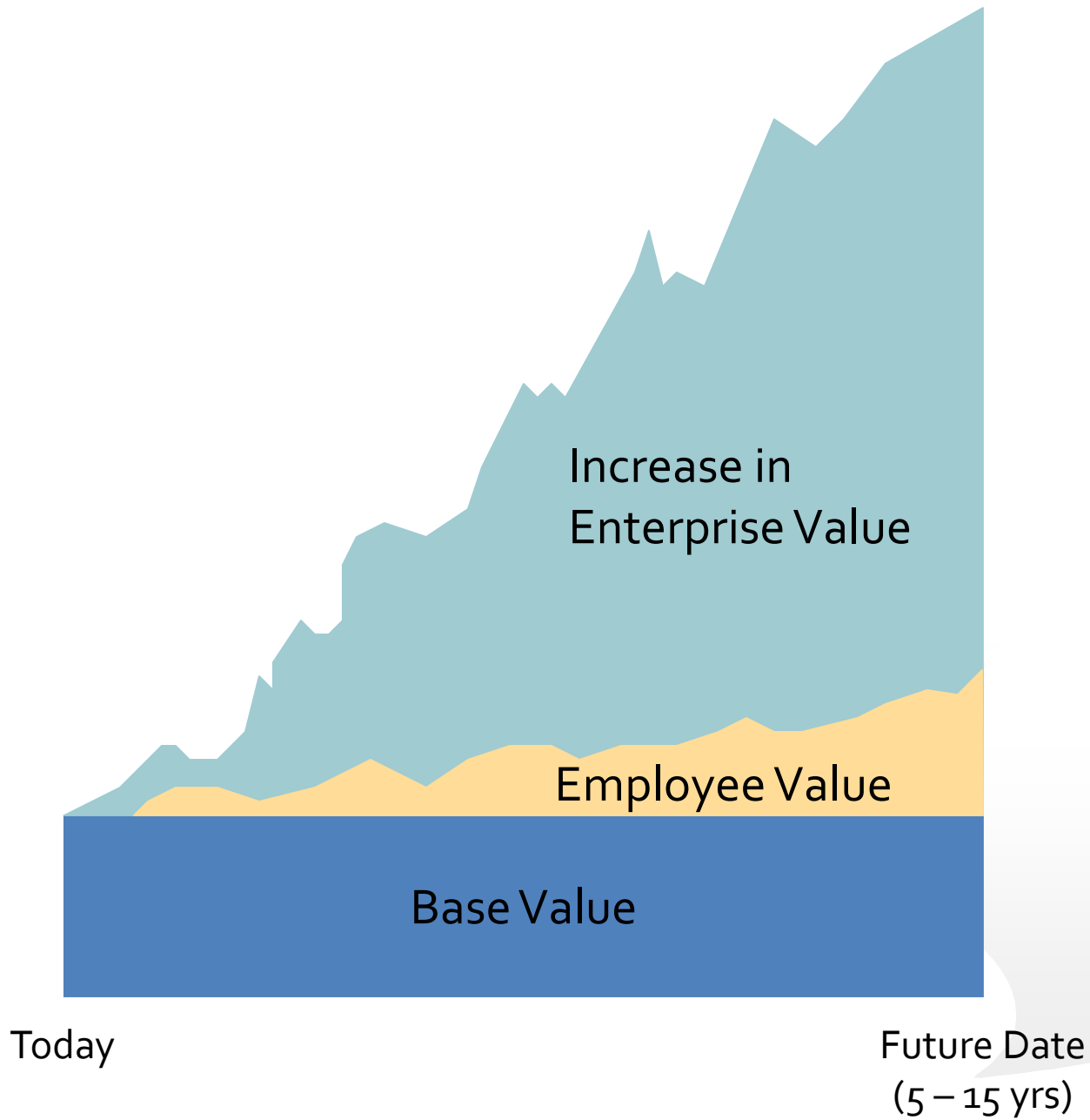
Rewards Pyramid



Line of Sight







Second action

Produce a statement that outlines the Rewards Pyramid for your job. Write down (a) the Company Vision, (b) the Business Strategy, (c) what your contribution will be to its fulfillment, and (d) what rewards (intrinsic or financial) you'll receive.

Then have others do it. See what you learn.

Part 3

Engagement

What type of engagement are we looking for?

- Commitment to innovation
- Intense focus on execution
- High accountability



Let's call this an **"Ownership Mentality"**

When do employees have an “Ownership Mentality”

They have to “get” the following:

- We have a business model and strategy that are sustainable over time and produce a competitive advantage
- We all have to do our part to be productive (do things faster, easier, cheaper, better); no entitlements
- Owners are committed to sharing the financial value we help create—after we’ve produced an appropriate return for them
- That value will be meaningful if we reach our full potential

Your Name Here

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

Third action

Do a simple spreadsheet like the EVS. See how long it takes to obtain the information and calculate your wealth opportunity.

Now consider the impact such a statement might have on your employees. Will it energize? Or discourage?

Part 4

Measuring Productivity

Better yet, let's measure the return on
your compensation investment



Value Creation and Sharing

What Does it Really Mean?

Case Study

(Source: Chief Executive Magazine, May/June 2012 Edition)



**Underwriters
Laboratories**

Keith Williams



Keith Williams



- Assumed leadership of UL in 2005
- Company carrying considerable debt
- Losing market share
- Low employee morale
- UL had become bureaucratic and “siloed”
 - Regional divisions undercutting each other

5 Core Changes



Compensation (Value Sharing):

- Took away local measurements driving management incentive plans—all paid on same metrics
 - “We live together and we die together”
- Aligned everyone behind company success
 - “I call it ‘pay the company first.’”

Williams clearly defined what value creation meant and how it would be shared

Pay the Company First



“Basically, up to the company’s operating profit target, all of the profits go to the company; and only after that target is met, do we start funding the incentive pool.”

Example: If UL’s target is \$80 million--

- 100% of first \$80 in profit goes to company
- The next \$20 million goes to the incentive pool
- From there on, 50/50 between company & incentive pool

Pay the Company First



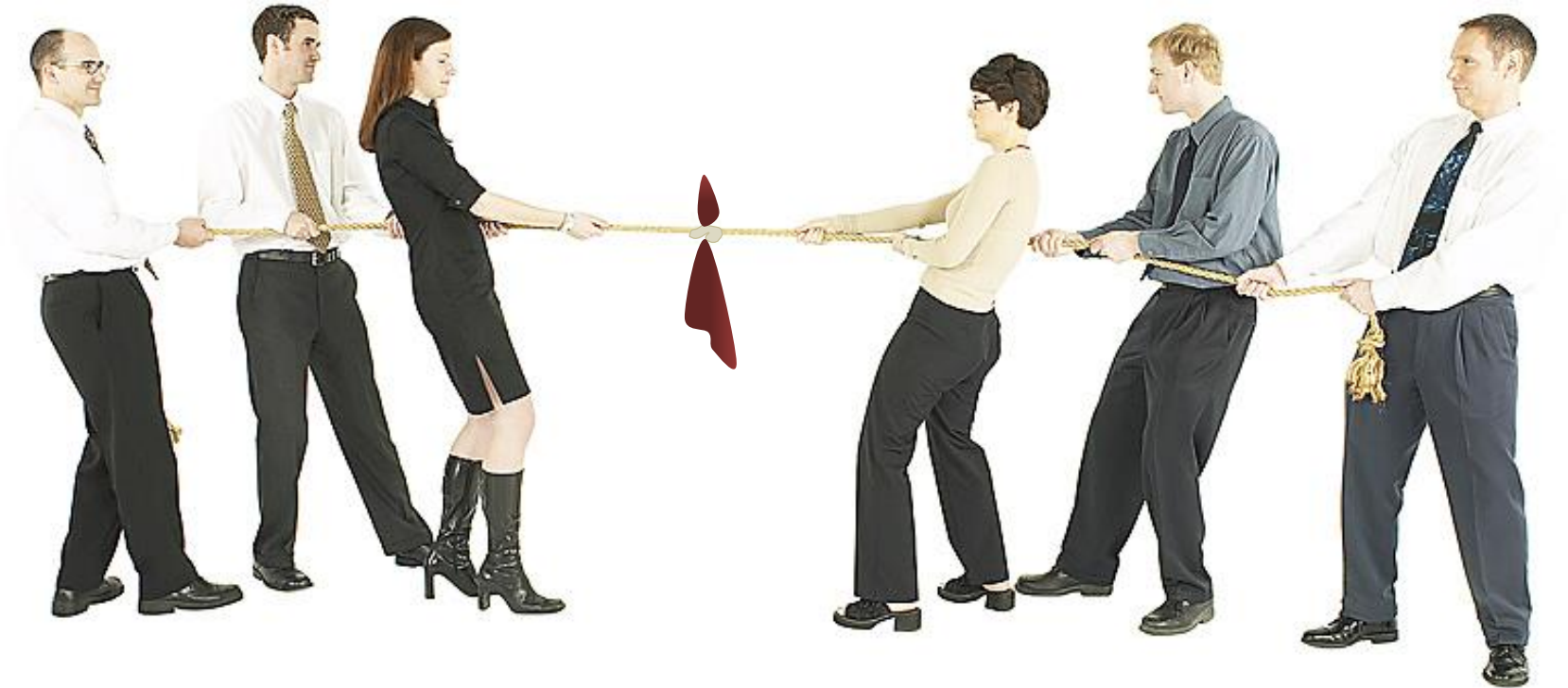
Once value creation is defined, compensation can follow a formula for sharing value in a way that aligns key producers with the company's business plan and priorities.

3 Key Distinctions

- Willing to tie all executive incentives to the same metrics
- Willing to identify a minimum return on equity threshold that must be met before any incentives are paid
- Willing to share significant upside beyond the threshold (no cap)



Expectations



Expectations



Pay the Company First

ROTRI™

Return on Total Rewards Investment™

Measuring the return on your compensation investment



How much is your 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	\$ 20,000,000
Cost of Capital	12%
Capital Charge	\$ 2,400,000
Operating Income	\$ 10,000,000
Productivity Profit	\$ 7,600,000
Total Rewards Investment	\$ 25,000,000
ROTRI™	30.4%

($\text{ROTRI}^{\text{TM}} = \text{Productivity Profit} / \text{Total Rewards Investment}$)

ROTRI™ Example:

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Total Rewards Investment	\$ 25,000,000
ROTRI™	30.4%

Variable Pay Plans (Value Sharing) are financed from Productivity Profit

Fourth action

Calculate your company's ROTRI™

Calculate last year's and compare.

Did it go up or down? Why?

What ROTRI™ should you target for this year?

Part 5

Value Sharing for Value Creators

Who would object?

Traditional Approach

- Salaries based on market standards (the “tyranny of the median”)
- Bonuses are then based on a percentage of salary (with a cap)
- Ownership is restricted to a small group
- Compensation is tightly budgeted

Value Sharing Approach

- Salaries based on your unique skills and expected contribution
- “Bonuses” reflect value you help create (short-term value sharing plan, with no cap)
- Ownership is something to be nurtured in everyone (and a long-term value sharing plan is essential)
- Compensation is a reflection of the return on productivity gains

Why Value Sharing Matters



What Happens When You Do It?

1. Value sharing attracts the best talent and magnifies results
2. Value sharing plans (effectively designed) reinforce the company's business model
3. Value sharing protects against bad profits and promotes good profits
4. Value sharing promotes an ownership mindset
5. Value sharing builds trust and accelerates results



When You Don't Do It:

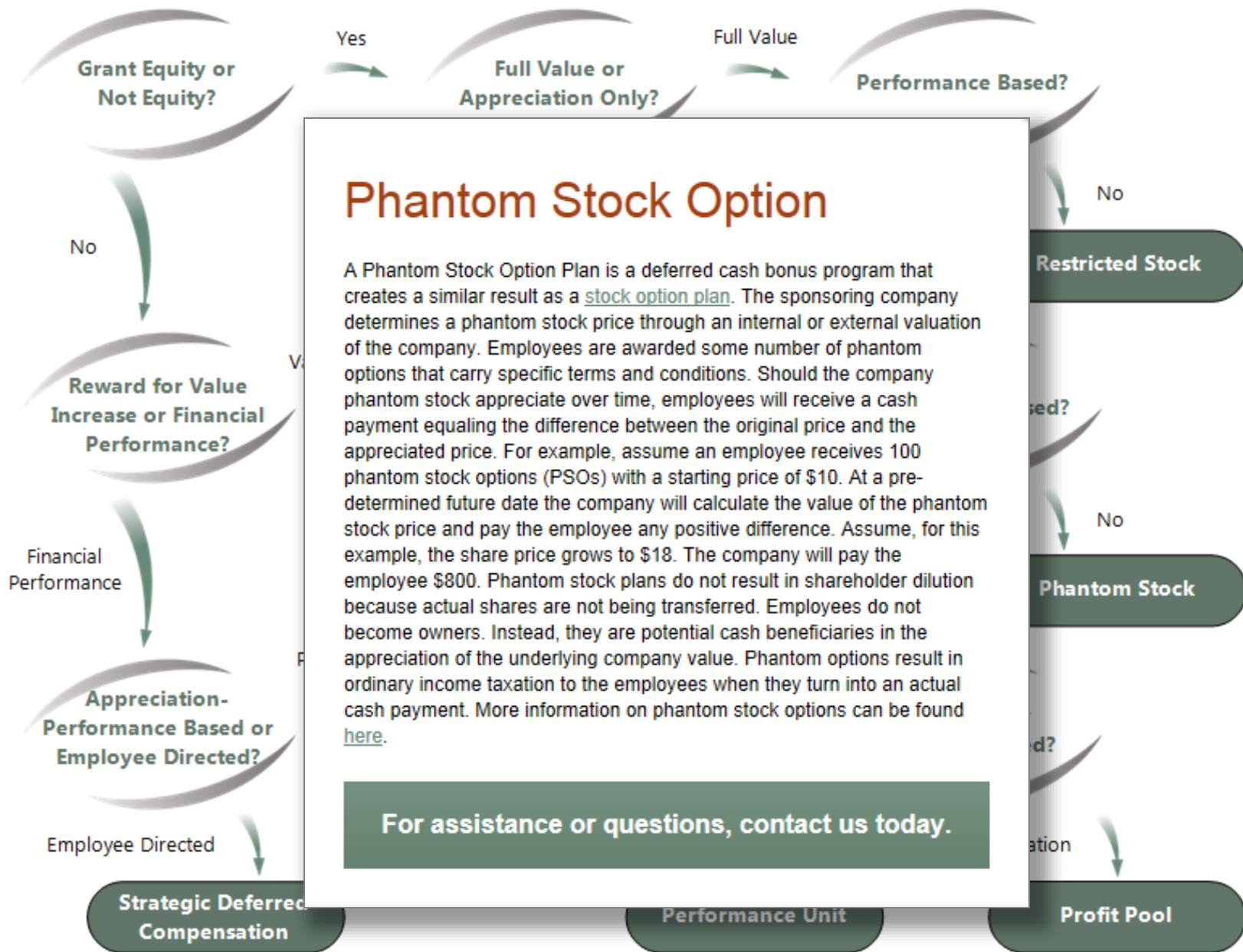
1. You will not attract the best possible talent
2. You can't be certain that pay aligns with the business model
3. You might be promoting bad profits instead of good profits
4. You will not have a complete ownership mindset
5. Employee trust and confidence will not be as strong as possible



How to Share Long-Term Value Effectively

- Picture your future company
- Determine the right value to share with those who help create it
- Select the right plan
- Build it with care and know-how
- Communicate and promote it





Go to "Tools" at PhantomStockOnline.com

Allocate the Investment

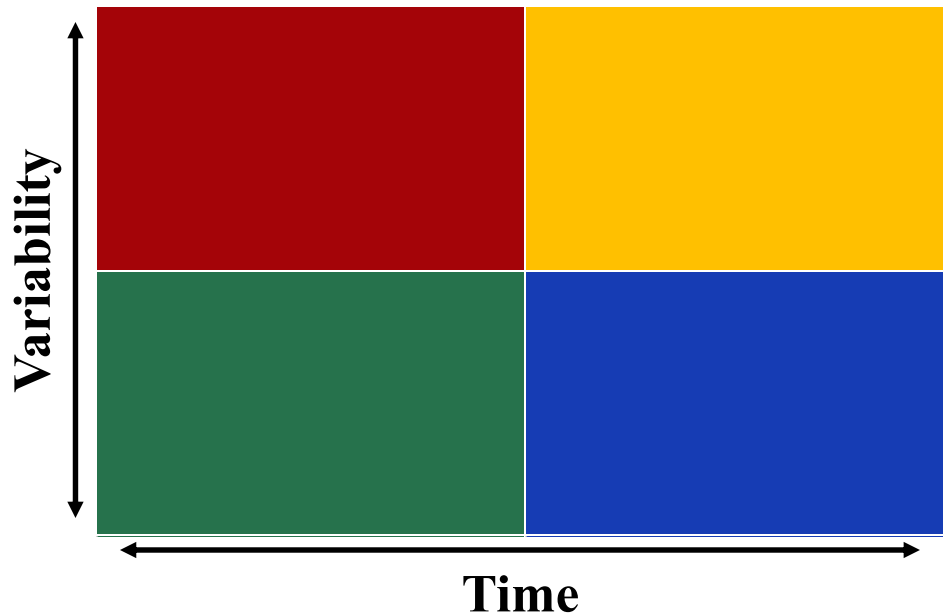
What does your total rewards investment look like?

You may do this for the overall company and within each pay grade.



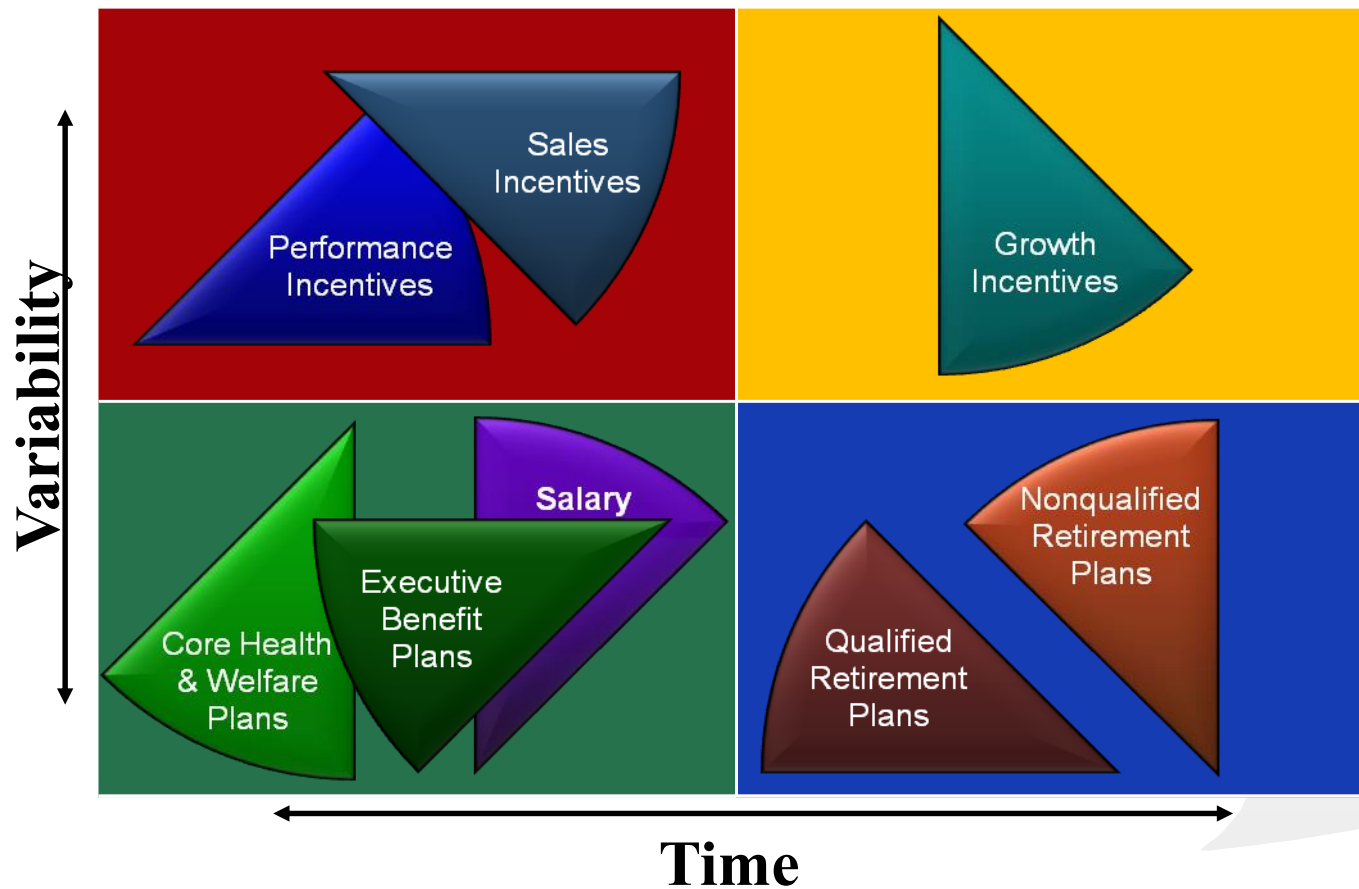
Allocate the Investment

Fixed vs Variable
Long vs Short

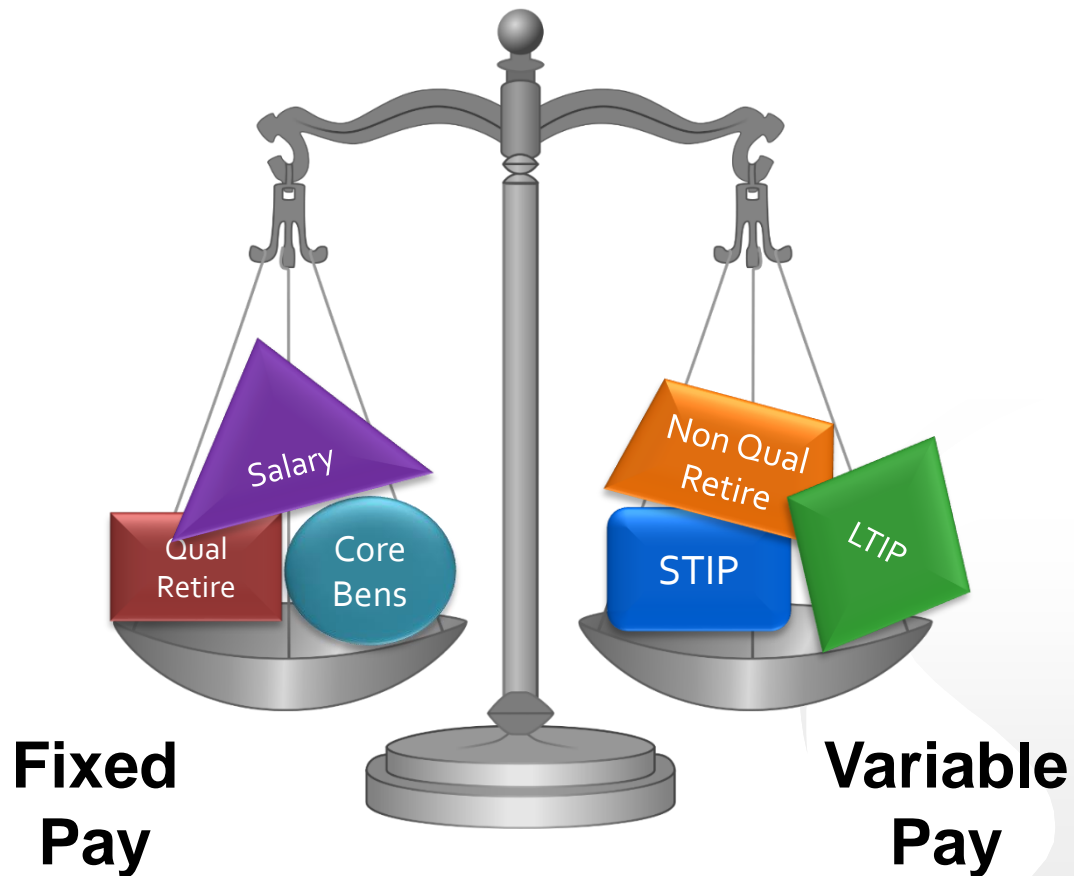


Allocate the Investment

Fixed vs Variable / Long vs Short



Balancing Pay



Remember our two companies?

Company A

- Large Call Center
- Workforce – Recent College Grads and Single Mothers
- Owner's primary goal: stabilize turnover and reduce costs
- Incentives: a tool for employee retention and recognition

Company B

- Web Based Technology Company
- Workforce – High Performing, Entrepreneurial
- Owner's primary goal: grow company
- Incentives: a tool for rewarding for product innovation

Company A Pay Mix

Company A

- Large Call Center
- Workforce – Recent College Grads and Single Mothers
- Owner's primary goal: stabilize turnover and reduce costs
- Incentives: a tool for employee retention and recognition

Pay Mix



Company B Pay Mix

Pay Mix



Company B

- Web Based Technology Company
- Workforce – High Performing, Entrepreneurial
- Owner's primary goal: grow company
- Incentives: a tool for rewarding for product innovation

Side By Side Comparison

Company A



Company B



Fifth action

Create your company pay mix “pie chart.” You could start with the executive group (or any particular pay grade).

Calculate the fixed/variable ratio.

Calculate the short-/long-term ratio.

Ask yourself: Do these make sense?

Your final results:

1. You'll have a pay philosophy tied to your business model.
2. Your employees will understand the connection between the company's vision and their personal rewards (thereby increasing your "ownership IQ."
3. Your employees will respect and appreciate the effort needed to optimize wealth for shareholders and themselves.

Your final results:

- 4. You'll have an effective and consistent way to calculate your return on compensation investment.
- 5. You'll have a strategic reason for the use of every pay component; you can adjust your allocation to accommodate time and variability considerations

Bottom Line

- Higher accountability
- Greater respect for the compensation investment
- Unlimited upside potential for top performers
- Tighter alignment between shareholders and employees
- Stronger ownership mindset
- Greater clarity, believability and meaning



Type Your Questions

Special Offer

One hour consulting call with a VisionLink principal at no charge

Indicate interest on final survey

Next Online Seminar:

"3 Keys to Attracting Premier Talent" *How to Get the People You Want*

**To be held on:
Tuesday, March 24th, 2015**

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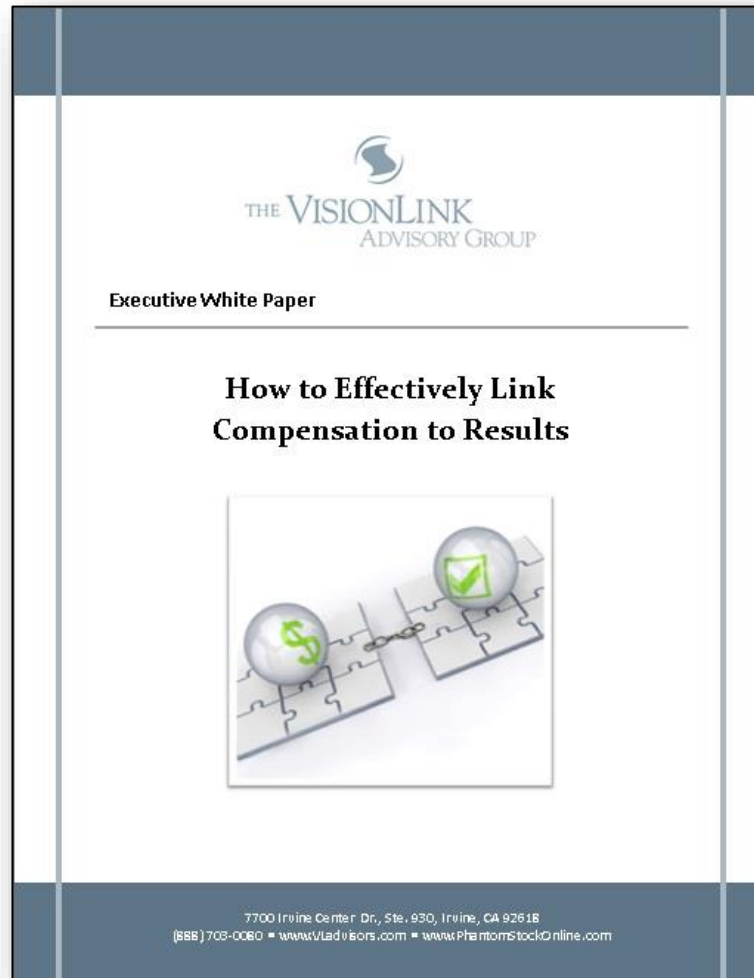
Upcoming VisionLink Online Seminars:

3 Keys to Attracting Premier Talent <i>How to Get the People You Want</i>	March 24 th
Pay, Performance & Productivity <i>How to Place Results at the Center of the Rewards Equation</i>	April 28 th
5 Pay Essentials for Growing Your Company <i>How to Build Tomorrow's Business without Sacrificing the Present</i>	May 26 th
Guaranteed vs. Incentive Pay: What's the Right Balance? (HR Audience)	June 9 th
Compensation as a Wealth Multiplier <i>How to Build Pay Strategies that Increase Shareholder Value</i>	June 23 rd
4 Alternatives to Sharing Stock <i>How to Share Value without Diluting Equity</i>	July 28 th

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WHAT WILL IT CHANGE?

WHERE DO I BEGIN?

A way to share ~~equity~~ *Value*


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We value your input.

You may request a copy of our slides, white paper and more information about the complimentary consultation.



Q&A

Thank you!

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