Increasing the effectiveness of reward management

An evidence-based approach

Michael Armstrong

Duncan Brown

Peter Reilly

IES HR Network

ies

The Institute for Employment Studies

The Institute for Employment Studies is an independent, apolitical, international centre of research and consultancy in public employment policy and organisational human resource issues. It works closely with employers in the manufacturing, service and public sectors, government departments, agencies, and professional and employee bodies. For 40 years the Institute has been a focus of knowledge and practical experience in employment and training policy, the operation of labour markets, and human resource planning and development. IES is a not-for-profit organisation which has over 70 multidisciplinary staff and international associates. IES expertise is available to all organisations through research, consultancy, publications and the Internet.

The IES HR Network

This report is the product of a study supported by the IES HR Network, through which Members finance, and often participate in, applied research on employment issues. Full information on Membership is available from IES on request, or at www.employment-studies.co.uk/network

Acknowledgement

Increasing the effectiveness of reward management: an evidence-based approach

This paper argues that effective reward management has to be evidence-based. We contend that the lack of evidence for and evaluation of pay and reward practices is a critical blind-spot for many of those involved in reward management. It is holding back advances in the field and creating a dangerous knowing/doing, policy/practice and rhetoric/reality gap, damaging the returns delivered by the major investments organisations make in their employees' pay and benefits. We describe how organisations pursue effectiveness in reward management and distil the lessons learnt from them into a description of a model of evidence-based reward management (EBRM) which has the potential to enable line and HR managers to make better reward decisions and inform confirmatory research.

> *'Little evidence demonstrates the efficacy of rewards, although much evidence indicates that rewards and their design loom large in management attention.'*
>
> Pfeffer (1998)

> *'Compensation is a complex and often confusing topic. Although compensation costs comprise, on average, 65 per cent to 70 per cent of total costs in the US economy and are likewise substantial elsewhere, most managers are not sure of the likely consequences of spending either more, or less on employees or of paying employees in different ways.'*
>
> Gerhart and Rynes (2003)

> *'The study found that few, if any, employers built in a monitoring and evaluation process as part of the introduction of an IPRP scheme. This was because most employers did not have clearly articulated objectives for introducing such schemes against which they could measure subsequent success or failure. Furthermore, little thought appeared to be given to the indicators that could used to measure the effectiveness of the scheme and the type of information that should be collected.'*
>
> Thompson (1992)

Introduction

High performing organisations manage their reward practices in ways that enable them to predict accurately what innovations are likely to work best and to ensure that what they are doing now delivers the expected results. They try their best to avoid what Kerr (1995) referred to as 'the folly of rewarding A while hoping for B'. Such organisations adopt an evidence-based management approach. They appreciate that reward management is not just a soft 'art' and that scientific and evidence-based methodologies are now used increasingly in general management and can readily be applied in the reward field. But despite the very obvious costs of pay budgets, incentive and benefits plans, the spread of sophisticated HR information systems and

shared service centres, the widespread adoption of balanced scorecards and near-universal pay benchmarking, many organisations seem to have little concrete evidence to evaluate or justify their reward practices.

In response to this situation we used a grounded theory approach which involved developing common themes and patterns from the data provided by our case studies, our own experience of evaluating reward practice, and an assessment of evidence and concepts relating to the practice of reward management. This led to the development of an evidence-based reward model designed to aid practitioners in reviewing their reward practices and evaluating their effectiveness.

The basic evidence consisted of an analysis of our extensive experience as researchers, consultants and practitioners. To identify relevant concepts we carried out a literature review. Research was also conducted by the Institute for Employment Studies and e-reward. This consisted of a survey of 192 reward specialists, 7 case studies involving heads of HR or reward, and interviews with three firms of management consultants. The aim of the research was to test our basic proposition on the need for evidence-based reward and to answer the following questions. 1) What were organisations doing about evaluating reward effectiveness? 2) Why was it important to evaluate reward? 3) How should they go about the process of evaluation?

This paper presents an analysis of the literature review and our research. On the basis of this, consideration is given to what is happening or not happening now about evaluating reward management (mainly the latter), why it is not happening, and why it should happen. We then describe the concept of evidence-based reward derived from this research. Finally, we model the process and examine how the model can be used.

Literature review

The literature on the impact of reward is extensive. We identified 49 journal articles concerned generally with establishing the impact of reward, but could find only four studies which dealt specifically with methodologies for measuring reward effectiveness.

General studies

Many of the general studies, for example those referred to in the meta-analyses conducted by Guzzo et al. (1985) and Jenkins et al. (1998), were based on experiments. These often demonstrated a positive link between a reward practice and performance but the methodology was not one that could easily be replicated by practitioners on a regular basis. Other studies, such as those conducted by Hansen (1997) and Stajkovic and Luthans (2001), consisted of an in-depth examination of the relationship between reward and performance, but again, the methodology was beyond the scope of a typical practitioner. Such studies can demonstrate that reward works but they do not provide much help to reward specialists who want to find out for themselves. Two British studies illustrated methods of evaluation that can be used by practitioners. In

their examination of the impact of performance-related pay in the Inland Revenue Marsden and Richardson (1994) used an attitude survey, and Kessler and Purcell (1992) relied on interviews in their review of performance-related pay. But the latter commented that:

> *'There are major difficulties in finding measures of PRP effectiveness. The bottom line measure of effectiveness for any payment system is arguably an improvement in overall organisational performance, assumed to flow from improved employee performance. It is, however, clear that the complex range of factors interacting to determine organisational performance makes it difficult to isolate the impact of a payment system alone.'*

<div align="right">Kessler and Purcell (1992)</div>

Studies of reward evaluation

In their research on the evaluation of changes in pay structures in seven large employers Corby et al. (2003) show that significant decisions are the outcomes of a social and political process, only partly shaped by the evidence and influenced by factors such as the pursuit of self and group interests and limitations of information and understanding. Their advice is for practitioners to have a realistic view of what is achievable, focus on evaluation in only a few key areas rather than compiling a wish-list, use existing mechanisms such as employee attitude surveys and human capital reports as far as possible and consider perceptions and qualitative criteria, not just 'hard' cost and business figures.

Heneman (2002) comments that the evaluation of the effectiveness of a strategic reward system is often overlooked, but it is an indispensable final step in the process of implementing a compensation program. Indeed, assessing the effectiveness of any procedure is just as important, if not more so, than its design and execution. And because it is often complicated to evaluate the effectiveness of a reward programme in terms of financial performance, so-called 'soft factors' such as employee behavioural reactions to the programme are sometimes an acceptable replacement.

Kanungo and Mendonca (1988) advocate a final review stage in introducing new reward systems. This consists of reformulating the reward package objectives or redesigning the reward system, or both, based upon the diagnosis of the present reward system. At this stage, a great deal of learning takes place, as management reflects on the perceptions and expectations of its employees and their impact on organisational goals. It is also a time for important decisions – not merely to respond in a reactive mode, but to take a proactive stance which considers how best the reward system can be creatively employed to cope with the new challenges which constantly confront a dynamic organisation. Therefore, although review is the final step, it is an ongoing process which enables management to keep on top of the situation at all times.

Scott et al. (2006a) suggest a six step approach: 1) set goals and objectives, 2) identify evaluation criteria, 3) select an evaluation methodology, 4) collect and analyse data, 5) interpret findings, and 6) develop and implement programme improvement strategies.

Survey evidence on the extent to which evaluation takes place

The e-reward (2009a) survey of those registered with e-reward (the web site for those involved or interested in reward management) found that 45 per cent of the 192 respondents conducted a full and systematic evaluation of their reward practices, while a further 32 per cent claimed that they had carried out a part-review (this means that they focused on one or two approaches such as market rate surveys or equal pay reviews). Of those who had conduced a full or part-review, 54 per cent were satisfied with the results – not a very encouraging outcome. The methods used by respondents who evaluated reward effectiveness are given in Table 1.

Table 1: Methods used by e-reward survey respondents who evaluated reward effectiveness

Five most popular methods used to evaluate reward effectiveness		Five most popular criteria used to measure reward effectiveness	
Method	Number of respondents	Criteria	Number of respondents
external market survey	113	financial impact	103
staff attitude survey	99	external benchmarking	92
benchmarking	71	HR outcomes, eg labour turnover	91
internal data analysis	66	stakeholder views	70
equal pay reviews	41	business outcomes, eg customer service	58

The Chartered Institute of Personnel and Development (CIPD) 2009 reward management survey of 520 organisations found that private sector service firms were most likely to evaluate (40 per cent), followed by manufacturing and production companies (30 per cent), public service organisations (25 per cent) and voluntary sector employers (19 per cent). Larger firms were more likely to carry out an assessment of their reward practices than smaller employers. 50 per cent of employers with more than 5,000 staff carried out such a study compared with only 29 per cent of organisations with fewer than 50 staff. Yet what is worrying about the survey data from this survey and previous CIPD surveys is that there has been little growth overall over the past four years in the application of these assessment mechanisms and only a minority of organisations were using financial and business data to assess their reward policies. Less than a quarter used business data, fewer than a fifth

conducted financial cost-benefit analyses of their reward changes and attempted to calculate the economic value added, and only one tenth could put a financial cost on their labour turnover. Surprisingly, only 54 per cent of the CIPD respondents stated that they calculated the size of their total remuneration spend (that is pay, benefits and other financial rewards, plus national insurance contributions). Most of them (around four-fifths) were unable to break it down into its constituent parts.

Further evidence on the lack of evaluation was provided by the e-reward survey of contingent pay (e-reward, 2009b) which discovered that just 12 per cent of respondents evaluated the effectiveness of their individual performance-related pay schemes. In view of the time, trouble and expense such schemes generate it is remarkable how few organisations bother to find out how well they work and whether in fact they do improve performance. In spite of the view expressed by Scott et al. (2006b) that 'companies were more likely to cost and at least discuss the bottom-line impact on variable pay programs rather than for base pay programs', it seems that in this important area of reward management – as in others – organisations frequently do things on an unfounded belief in the existence of best practice and on the basis of 'follow-my-leader' approaches rather than reason.

A study for the UK Department of Health (Corby et al., 2003) looked at seven organisations which had introduced new pay structures. The researchers found that only one organisation made any real attempt to systematically evaluate the effectiveness of the changes, and in the others there was a complete lack of evidence on whether the stated objectives for the changes had been achieved.

Why organisations don't evaluate

It could be said that measuring the effectiveness of their reward strategies, initiatives and practices is the Achilles' heel of most reward professionals. This is confirmed by our experience in reward management. Given the current focus on quantitative measurement and analytics, and the large amounts of data now being generated by increasingly sophisticated HR information systems, it is interesting to ask why there has been so little improvement in the overall state of the evidence and rationale for reward practices and changes.

It is possible that this problem is a feature of HR management, caused by its subject matter and the orientation of HR practitioners. But a look at the literature on training and development is instructive (eg Kearns, 2005). Here there is an established framework for evaluating the effectiveness of training interventions, the well-known Kirkpatrick model, and debate is not about whether it should be used but how it can be improved. Yet in reward, despite the greater financial spend in organisations and despite, it might be thought, the more quantitative background and orientation of its practitioners, there is no equivalent model and an absence of this quality and depth of literature and practice in evaluation. Why is this?

As Pfeffer and Sutton (2006) comment, there are no less than six substitutes that managers often use for the best evidence: 'obsolete knowledge, personal experience, specialist skills, hype, dogma and mindless mimicry of top performers'. We have probably all seen examples of at least one of these when trying to justify or make changes to reward practices, particularly the last one. Possible reasons for this lack of interest and substitution include:

1. Perceived lack of time and resources to evaluate (even though stronger evidence of effectiveness might lead to larger resources being allocated to the reward management function).

2. A bewildering array of sources are used to generate management advice – Pfeffer and Sutton mention Shakespeare, Billy Graham, Jack Welch, Tony Soprano, fighter pilots, Santa Claus and Attila the Hun.

3. Lack of training and skills in statistics, finance, quantitative methods, research and other relevant disciplines amongst the HR community (although it might be thought that this would be less true about reward than other HR professionals, given the finance background of some of them and general requirements of most).

4. Sheer laziness when practitioners are not being pushed by others to do it (though HR functions are coming under more pressure to justify their existence).

5. The difficulty, real or imagined, of demonstrating cause and effect when evaluating.

6. The impact of constant change in organisations which creates a culture of constant action rather than reflection, and where the churn of people through posts and projects means that there is little continuity. For example, the Department of Health in the UK did not engage with the Hay/IES evaluation of a £2m team pay pilot scheme because the project team had been disbanded to work on contracts for medical staff.

Respondents to the e-reward survey (2009a) gave specific reasons for not evaluating, as shown in Table 2.

Table 2: Reasons for not conducting reward evaluations

Reason	% of respondents
Lack of resources or time	48
Lack of information or data	19
Senior management indifference	15
Organisation changes	10
Lack of analytical skills	8

Source: e-reward survey, 2009

Many reward practitioners engage in external market benchmarking. This practice has spread from levels of pay and benefits to far more extensive human capital benchmarking which looks at the prevalence and efficiency of HR practices and the HR functions responsible for them. An industry of firms has grown up to supply this market, producing a bewildering array of apparently sophisticated models and statistics to underpin their notions of 'best practice' and 'world class' HR. Benchmarking statistics often seem to focus on the most measurable rather than the most meaningful information and can encourage a 'follow the herd' mentality. So what if it takes longer for me to recruit someone on average than competitors when what really matters is the quality of staff I recruit? So what if all my competitors use performance-related pay; does that necessarily mean it is going to work in my setting?

In defence of reward practitioners, it can be argued that it is difficult to assess pay and reward practices in many settings. A wide range of variables and factors, many of them intangible, are generally involved. As the Corby et al. 2003 study showed, pay management and change is often a highly political process and an attempt to evaluate that ignores this is sure to fail.

There are a number of success and effectiveness criteria available and it may be a question of which to choose and what to do if they come into conflict. For example, a decision may be made to close a defined-benefit pension scheme and reduce pension contributions by the company into a new defined-contribution plan. The financial savings resulting from this move can be easily calculated. But how can these be balanced against the demotivation of existing staff and loss of potential recruits that such a change might cause?

Moreover, it is difficult to carry out controlled research studies and 'experiment' with different approaches to pay and rewards, and compare their effectiveness when people's livelihood and standards of living may be at stake. There are also a whole range of factors that impact on the success of performance-related pay initiatives (for example performance management and communications), which make it hard to isolate pay and rewards to assess their effects. Changes in pay are also typically accompanied by changes in associated HR processes, for example job evaluation exercises are often linked to changes in job content and organisation design.

These were some of the major difficulties that the head of rewards for a large UK bank referred to when we discussed possible improvements in measurement processes and techniques with him. He said that he was interested in the improvements, but the difficulties are formidable. Also, he felt that the board of the bank was mainly concerned with rewards for their top executives and despite the millions of dollars of pay costs for other staff he was not being pressured to show a return on how that pay and employment spend was invested, so long as there were no obvious problems or huge inefficiencies.

The rationale for evaluation based on evidence

A key influence on our thinking about EBRM was the concept of evidence-based management. This was explained by Rousseau (2006) as follows.

> *'An evidence orientation shows that decision quality is a direct function of available facts, creating a demand for reliable and valid information when making managerial and organisational decisions ... the poor information commonly available to managers regarding the organisational consequences of their decisions means that experiences are likely to be misinterpreted – subject to perceptual gaps and misunderstandings. Evidence-based management leads to valid learning and continuous Improvement.'*
>
> Rousseau (2006)

Pfeffer and Sutton (2006) believe that *'managers (like doctors) can practice their craft more effectively if they are routinely guided by the best logic and evidence – and if they relentlessly seek new knowledge and insight, from both inside and outside their companies, to keep updating their assumptions, knowledge, and skills.'*

The tendency is for organisations to ignore research evidence and base their HR and reward policies on generalized 'truths' which have little foundation in that evidence. Because systematic evaluation does not take place there is a danger of important questions such as these remaining unanswered:

- How effective are the pay and reward arrangements in our organisation?

- Do they add value?

- How do rewards affect the levels of engagement and performance of our employees?

- Are our reward policies and other HR policies in areas such as resourcing sufficiently well integrated?

- What's the return on the cost of our management and employee incentive plans, and what would happen if we switched them from an individual to a team emphasis?

- What would happen to performance if we halved or doubled the incentive opportunities?

- Are we getting any measurable return on the cost of our flex and benefits plans?

- Is our pay market positioning right?

- What would happen if we moved up to an upper quartile pay line?

- Do we have the right number of pay grades?

- What would happen if we had fewer or more grades?

- In fact, do we have any evidence whatsoever that our pay and reward arrangements make any difference?

Institute for Employment Studies

The case for EBRM

EBRM as described in this paper is the management of reward systems based on fact rather than opinion, on understanding rather than assumptions, on grounded theory rather than dogma. It recognises that reward systems exist to add value but often don't, and that it is essential to assemble and analyse the evidence on how well they are functioning so that improvements can be made where necessary. It refers to the extensive research conducted over the last 50 years into how reward systems work in organisations and what can be done to increase their effectiveness. It subjects the theories derived from this research to critical evaluation based on their relevance and application in the context of particular organisations. It makes use of the model emerging from our own research (as described below) which identifies its components, ie setting objectives and success criteria, conducting reward reviews, measuring the impact of reward, evaluating that impact, and developing, implementing and applying reward policies and practices on the basis of the evidence assembled by the processes of review, measurement and evaluation. And, as the seven case studies we carried out have demonstrated, the measurement difficulties we have found can be overcome and the benefits of more EBRM can be realised.

Case study evidence and examples of EBRM

The case studies summarized below illustrate in different settings how organisations are wrestling with issues concerning the development, implementation and evaluation of reward policy and practice – each adopting its own approach and in accordance with the organisation's context. They underline a basic principle that was confirmed by the research – that there is no such thing as 'one best way'; only the method that suits the needs and circumstances of the organisation. The organisations were selected as known examples of good practice in this field.

DSG International

This case described how in a difficult economic environment, a complex mix of reward arrangements was simplified to establish a close alignment between rewards and the five components of a new business turnaround plan, primarily through the re-design of executive incentive plans. The change was designed to enhance the perception of line-of-sight between individual performance, group performance and reward. It illustrates the vital role of communications to explain the 'why' of reward change, what it means for the business, and how each component of reward links to the five point plan.

Kent County Council

This case revealed, interestingly, that the Council does not over-emphasize metrics and measuring. They attribute success to a strong and united political direction from the top; a long-term consistency of purpose, but with the appropriate phasing of changes and with adaptation to local circumstances; and a high involvement approach. However, they do look at some statistics, particularly in terms of equal pay,

staff retention in each directorate, and the findings from their biannual staff survey. The latter has shown a growing appreciation of the total reward package across the organisation. Costs are also an issue at the forefront of their minds, with the current pressure on local authority funding.

KPMG

This case described a clear reward strategy that has underpinned KPMG's growth in recent years, focused on the twin objectives of strongly rewarding performance and meeting the needs of a large, diverse workforce with a comparatively young average age profile through a sophisticated total rewards approach. The firm monitors a set of 13 key performance indicators based on each of their reward strategy principles, using a traffic light system of assessment for each indicator. For each of the 13 measures targets are set and results compared with past year's performance.

McDonalds

This case showed how a company with a strong culture of measurement has built its own people-profit chain methodology and produced impressive evidence to demonstrate how rewards can enhance employee engagement and thereby business performance. The operational and cost focus in the business means that reward arrangements are reviewed regularly and changed if they are not found to be delivering. But the subtler processes of consultation and change management are equally vital in maintaining and strengthening reward effectiveness.

Standard Chartered Bank

This case showed how the bank's reward policies, like all of its people management policies, are coordinated and assessed within a sophisticated framework of human capital management and measurement. Since 2005, the bank has maintained a human capital scorecard to gather, organize and report on key trends linked to the achievement of business goals. This information is used as an important input into reward plans and processes. But the alignment of reward policies with the bank's values is especially important and this has been particularly evident in its most recent review of executive remuneration arrangements and incentives in the context of widespread criticism of practices in the sector.

The NSPCC

This case demonstrated that while measures of organisational and reward effectiveness may differ, the delivery of them is every bit as critical, if not more so, in voluntary organisations. It also shows that limited resources need not be a barrier to assessing and demonstrating effectiveness. Establishing links to the core purpose of the organisation was the major driver behind the extensive research undertaken into effectiveness. The culture of the organisation and its values were important considerations, as was ensuring that the values of the people in the organisation were aligned to them.

A technology company

This case looked at a smaller, entrepreneurial technology company and how it is evolving a more logical, structured approach to its pay and rewards in order to better align them with its growth plans, rather than largely reflecting the history of its development. As in our other case studies, the head of reward and development emphasised that reward system development is an evolutionary process that can't just be determined on the basis of abstract reward principles nor solely using 'hard' quantitative measures of effectiveness. A subtler understanding of culture and change processes is at least as important as the technical design of reward plans if improvements are to be put into practice.

The criteria for EBRM

Our research identified the most important criteria for assessing the effectiveness of reward arrangements, as illustrated in Figure 1. While there may be a potential conflict between criteria, of more concern is how few of the criteria most organisations use, beyond the ubiquitous one of market competitiveness.

Figure 1. A framework for EBRM: the ten Cs

Source: IES 2009

The components of EBRM

It is tempting to believe that the process of EBRM is one of linear progression – a succession of logical steps beginning at A and continuing through B, C, D etc. to the inevitable conclusion of a well-constructed reward system. But life is not like that. As Watson (1995) remarked, 'social scientists are prone to see far more rationality in organisational activities than is justified'.

The reality is that EBRM is a much more varied and fluid affair. The evidence from our case studies is that, while the organisations concerned all shared a belief in the importance of reviewing and assessing the effectiveness of their reward practices and all have gone through and now operate some kind of process to effect it, they use different criteria and measures of reward success, as well as different reward approaches.

However, based on the case study evidence and our own experience, we have concluded that there are a number of common components to the process of EBRM and the assessment of reward effectiveness. But these are applied in all sorts of ways; sometimes sequentially, sometimes not, depending on the needs of the situation. That is why we call them components rather than stages. The components we have identified are defined in Table 3 with descriptions of the typical work involved and outcomes.

Table 3: The components of EBRM

| Component	Typical work	Outcomes
1) Set reward objectives and criteria	Executive interviews Senior management seminars Organisation and HR strategy analysis Reward pathway definition, goal setting and gap analysis	Rationale for review process Agreed goals for reward arrangements Criteria to assess reward effectiveness Prioritisation of goals and criteria Defined linkages to business requirements, employee needs and other HR practices Agreed review process
2) Review current reward policies and practices	Project group formation Internal research into employee attitudes and current reward policies and practices External research – market rate analysis, benchmarking good practices, review of relevant research	Full understanding of current reward position Highlighting of key reward issues and problems to address

Component	Typical work	Outcomes
3) Measure reward effectiveness	Decide what to measure – what data, where from, how gathered Specify measures by reference to reward goals and success criteria Collect and analyse data	Information required to evaluate reward effectiveness A set of measures for ongoing evaluation
4) Evaluate reward outcomes	Refer to reward objectives and success criteria Use measures to evaluate extent to which the goals and criteria have been met	Information required to develop and implement new or revised reward practices A defined process for ongoing evaluation
5) Develop future reward directions and practices	Refer to survey results, measures and evaluation to highlight key reward issues and problems to address Agree direction of change and reward architecture for the future Analyse possible alternatives and changes Define objectives of new reward practices Design/develop new reward practices Model and cost changes Involve employees Brief and train line managers	A clear understanding of what has to be achieved and why, which provides the basis for future review and evaluation Fully tested designs and changes based on the thorough analysis of evidence supporting the change Development of organisational capability to implement and operate changes successfully
6) Implement new or improved reward practices	Communicate proposed reward developments Introduce new reward practices Conduct regular effectiveness reviews Develop and implement further changes as required	Changes to rewards which have demonstrably improved their effectiveness An established process for measuring and evaluating reward effectiveness

Source: IES, 2009

Figure 2 shows how the components function in practice. It appears to describe a sequential progress in the form of a continuous cycle from goal setting, through review, measurement, evaluation, and development activities to implementation and further review. This can happen in some circumstances, for example a review by outside consultants as described by the firms we contacted. But as we established from the case studies and our own experience as practitioners, when EBRM is practiced within organisations the components are not necessarily specified, or defined and

managed in an orderly sequence. They are closely interlinked and they may overlap. Objective setting, review and measurement as considered in more detail below affect all the other components, as does evaluation. They can take place at any time (or all at once) and they all directly influence the ultimate activities of development and implementation.

Figure 2: A model of the inter-relationships between the components of EBRM
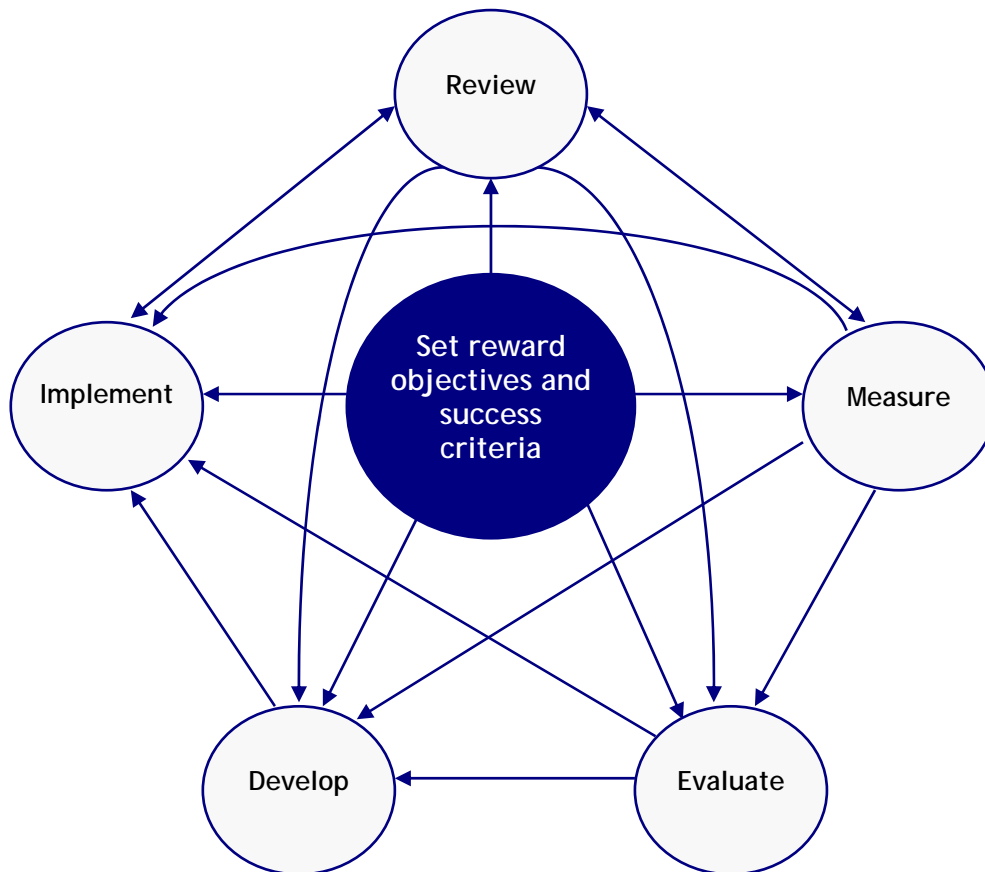
Source: IES, 2009

The model illustrates the complex and varied ways in which EBRM works. But we contend that even in the messiest and most reactive of situations an approach which makes appropriate use of these components will be helpful. Using them appropriately means applying and linking the components in ways which fit the demands of the situation. It becomes a way of thinking that reward practitioners can apply to any situation or issue by asking themselves:

- What are we trying to do here, what's important to this organisation, how do we measure that?

- How are current reward practices helping or hindering what we are trying to do and what evidence do we have of this?

- How might reward changes improve the delivery of the desired outcomes?

- How can we best implement improvements and how can we show ourselves that they are working?

Evaluating reward effectiveness

The evaluation of the effectiveness of reward innovations and reward practice is carried out through the model components of objective setting, review and measurement.

Objectives setting

As Kerr (1999) commented: *'Rewards should be the third thing an organisation works on; measurements should be the second, clear articulation of desired outcomes should be the first'*. The objectives of a reward innovation should be expressed from the outset as part of a business case: *'This is what we propose to do'*. *'This is why we propose to do it'*. *'This is how much it will cost'*. *'This is how the organisation and its people will benefit'*. Success criteria should be defined for each objective. These could be quantitative – eg a reduction in employee turnover, an increase in employee engagement or reward opinion survey scores. They might often have to be qualitative, in effect completing the statement: '*This innovation will have been successful when … happens'*. Examples of possible objectives and associated success criteria are given in Table 4.

Table 4. Reward objectives and success criteria

Reward innovation objective	Success criteria - this objective will have been successfully achieved when:
Develop performance culture	Reports of performance reviews show that performance has improved There is evidence of improvement from other performance indicators
Enhance engagement	Scores in the engagement survey have increased by x %
Increase overall employee satisfaction with rewards	Scores in the rewards survey have increased by x %
Increase key staff retention levels	Employee turnover for key categories of staff has reduced by x %
Attract high quality applicants	Surveys of new starters reveal that x % of them were attracted by the employee value proposition offered by the firm
Develop employee value proposition	There is evidence that attraction and retention rates have improved
Enhance pay competitiveness	Survey data shows that pay levels are competitive in line with market stance policy
Increase employee satisfaction with contingent pay decisions	Scores in the contingent pay section of the rewards survey have increased by x %

Reward innovation objective	Success criteria – this objective will have been successfully achieved when:
Replace decayed job evaluation scheme and use to develop new grade structure	The evaluation scheme is accepted as fair by staff The cost of administering the scheme is within budget Successful appeals against gradings are less than x % of staff The cost of implementation does not exceed x % of payroll
Introduce career family structure to support career planning	There is evidence that career ladders defined as competency levels are being used to guide career planning and development
Reduce grade drift	There is evidence that upgradings are being properly justified by job evaluation
Introduce contribution-related pay scheme	There is evidence that it has improved performance Staff feel that the scheme fairly recognises their contribution
Conduct an equal pay review and act on it	Equal pay review conducted as planned Action taken which reduces the pay gap by x %
Introduce flexible benefits	Take up of scheme Level of satisfaction in reward attitude survey

Source: IES, 2009

Review

A reward review identifies and assesses what is being done about reward. It generally involves researching and gathering both quantitative and qualitative information and evidence on existing reward policies and practices from inside the organisation, as well as collecting information on external reward practices, levels, trends and concepts. It uses this information to make assessments of effectiveness, identify key reward issues and consider the options before deciding on a course of action.

Measurement

There is no single, 'magic' set of metrics that every organisation can apply to improve its reward practices and their contribution to business success. But some measurement is required to indicate what impact reward makes, although it can be overdone. As Marchington (2008) remarked, the HR function sometimes seems to be 'obsessed with measuring its way to credibility'. It is necessary to be selective and realistic and to recognise that while quantification is ideal it is not always possible. 'Soft' measures involving a qualitative assessment of outcomes may be necessary and they can be just as useful. Our research established the possible measures for different aspects of reward (see Table 5), but organisations have to select the measures that suit their circumstances and needs.

Table 5: Possible reward evaluation measures

Reward aspect	Measured by
Reward strategy	Clear reward strategy and annual plan in support of business strategy and plans.
Productivity and reward costs	Overall staff productivity and return on staff costs versus competition
	Profit, value added or sales per employee
	Total pay and reward costs compared to competition
Financial and non-financial rewards	Financial and non-financial recognition for behaviours in line with strategy and values
	Appropriate forms of rewarding performance and contribution in place – individual/team, short/long-term etc
	Proportion of staff covered by methods of rewarding performance and contribution
	Rewards effectively integrated with performance management process
	Risk assessment of bonus plan design – fixed/variable mix, range of performance measures etc
	Clear demonstration of return on costs of bonus
Employment	Ratio of job offers/acceptances
	Staff involuntary turnover/resignation rates and retention of high performance/key skill staff
	Staff turnover and absence levels
Reward management general	Actual market position compared to desired
	Take up and level of activity in flexible rewards
	Equal pay reviews carried out and acted upon
	Quantity, quality and frequency of reward communications – clarity, range of media etc
	Training and evidence of line manager capability
Engagement and satisfaction with rewards	Surveyed overall employee engagement levels
	Employee overall satisfaction with pay and rewards
	Employee opinions that rewards are competitive
	Employee opinions that performance is rewarded and managed effectively
	Employee opinions on level of understanding of rewards
	Managers feel reward arrangements are flexible and meet their needs

Source: IES, 2009

Conclusions

According to Bloom and Milkovich (1995), *'A better blend of research and practice can advance the state of the [rewards] field and demonstrate the critical role that compensation plays'*. We accept the difficulties involved and the influence of social and political processes on reward practices. But we simply have to get better at evaluating and managing rewards and ensuring that what we do is more strongly rooted in evidence on what works and why. Our model of EBRM is intended to provide a framework for doing this. It *describes* rather than *prescribes*. It is concerned with how the process of thinking about the review and evaluation of reward policy and practice is carried out but does not propose a universally applicable method of doing so. We are well aware from our experience and research that all organisations are different and that in each case approaches which fit their circumstances are required.

Although our research has established that many organisations are not interested in assessing the effectiveness of their reward practices, it is encouraging to note that our case studies did reveal how some are taking action. And our survey of practitioners elicited a host of suggestions in the form of 'dos and don'ts' (see Table 6) which provide a practical and therefore fitting conclusion to this paper.

Table 6: Evaluating reward effectiveness: Views expressed by respondents to the e-reward 2009 survey

Do	Don't
Do it! Why would anyone spend £xm pa and not try and understand each element's effectiveness (and leverage it more)? Spend time to decide the measurement criteria up front, otherwise you may need to change them, leading to an inability to measure year on year improvement as you embed your changes.	Assume that one size fits all – you may think that your benefits package is great; your typical employee may find nothing of interest in it. Don't over complicate things – could you explain your bonus arrangements in five minutes to someone who isn't in reward and doesn't work for your company? If not – is it really driving the behaviour you want?
Exploit before you explore. Are people aware of what you already have available, is it consistent with the business strategy and is it valued by employees? If not, stop it and invest the money elsewhere (if you can!) Consider the demographic profile of your organisation and design your benefit package accordingly. Use plain language – don't hide behind jargon. If your organisation has a tone of voice make sure reward communications reflect this.	Chase the holy grail. Reward is not the panacea to all performance and recruitment problems so don't over sell what the reward strategy will do. Do anything unilaterally. Involve as many functions as you can to get senior management buy in. Always be wholly led by market data – do what is right for your organisation to become an industry leader rather than follower.
Accurately position where your organisation fits against competitors and select a few core aims of where you want to be in the future.	Become slaves to the numbers. Ensure you fully understand any underlying issues which may affect the data, before drawing and communicating any conclusions, or proposing any significant changes.

Do	**Don't**
Be realistic about cause and effect. The effectiveness of reward measures can easily be offset if not aligned to other HR strategies or by a lack of management competence.	Measure just for the sake of it – be clear about what you want to demonstrate.
Be realistic in what you think you can achieve and understand whether there is a will in the business to change if change is needed.	Get into assessments of reward effectiveness which are huge 'one-off' exercises which can't be repeated easily on a regular (annual, biennial) basis. The key thing is to be able to repeat, and therefore see whether your reward effectiveness is better or worse than before.
Build review and continuous improvement practices into all of your reward programmes, but recognise that it is not an activity that will happen overnight. It will require a fundamental shift in your management information and project practices.	Get too bogged down in the detail – adapt your communications to your audience to achieve the outcome needed.
Calculate and understand your total reward costs.	Just rely on initial findings from attitude surveys – you need to dig deeper on the items that stand out from the survey.
Decide what corporate changes you want to achieve which can be driven by reward and agree what is to be measured to achieve this.	Just think about the bottom line, there are a lot of things that get you there and they aren't always obvious.
Make sure you align the measures to the goals of your organisation. Without that alignment, senior level buy-in to the outcomes becomes very challenging, and can lead to reward being seen as a nice to do, rather than a must do.	Offer reward solutions that can't be measured and translated into some form of ROI.
Engage stakeholders early on. Manage expectations of stakeholders from outset. Ensure clear objectives and communication strategy.	Over-complicate issues, try to do too much at once, or raise expectations if you are not prepared to follow up on the data received.
Engage with as many people within the organisation as possible. Use response scales that will allow for analysis of volumes of data rather than free text. Keep it simple. Communicate effectively. Act on the data you receive. Break issues down into quick wins and those requiring longer term solutions.	Simply follow the CEO's latest fad. Vow to measure everything. Measuring takes time and effort and raises other people's expectations. If you can't deliver good results, don't promise the business you can
Ensure the process is driven from a single coherent source of information.	
Get the basics right – administration and systems – and build up data collection from there.	

Source: IES, 2009

References

Bloom M C, Milkovich G T (1995), *Issues in Managerial Compensation Research,* Ithaca, NY Centre for Advanced Human Resources Studies, Working Paper Series, 95-24

Bloom M, Milkovich G T (1998), 'Relationships among risk, incentive pay, and organisational performance', *Academy of Management Journal,* 41 (3), pp 283-97

Chartered Institute of Personnel and Development (2009), *Reward Management Survey,* London, CIPD

Corby S, White G, Dennison P, Douglas F (2003), *Does it work? Evaluating a new pay system,* London, University of Greenwich

Cox A, Purcell J (1998), 'Searching for leverage: pay systems, trust, motivation and commitment in SMEs', in *Trust, Motivation and Commitment: A reader,* S Perkins (ed.), Faringdon, SRRC

e-reward (2009), *Assessing Reward Effectiveness survey,* Stockport, *e* –reward

e-reward (2009), *Survey of Contingent Pay,* Stockport, *e* –reward

Gerhart B, Rynes S L (2003), *Compensation: Theory, evidence and strategic implications,* Thousand Oaks, CA, Sage

Guzzo R A, Jette R D, Katzell R A (1985), 'The effects of psychologically based intervention programs on worker productivity: a meta-analysis', *Personnel Psychology,* 38 (2), pp 275-91

Hansen D G (1997), 'Worker performance and group incentives: a case study', *Industrial and Labor Relations Review,* 51, pp 37-49

Heneman R L (2002), *Strategic Reward Management: Design, implementation, and evaluation,* Greenwich, CT Information Age Publishers

Jenkins D G, Mitra A, Gupta N, Shaw J D (1998), 'Are financial incentives related to performance? A meta-analytic review of empirical research', *Journal of Applied Psychology,* 3, pp 777-87

Kanungo R N, Mendonca M (1988), 'Evaluating Employee Compensation', *Californian Management Review,* 31 (1), pp 23-39

Kearns, P. (2005) *Evaluating the ROI From Learning* London, CIPD

Kerr S (1995), 'On the folly of rewarding A, while hoping for B', *Academy of Management Executive,* 9 (1), pp 7-16

Kerr S (1999), 'Organisational rewards: Practical, cost-neutral alternatives that you may know but don't practice', *Organisational Dynamics,* 28 (1), pp 61-70

Kessler I, Purcell J (1992), 'Performance-related pay: objectives and application', *Human Resource Management Journal,* 2 (3), pp 16-33

Marchington M (2008), *Where Next for HRM? Rediscovering the heart and the soul of people management*. IES, Brighton

Marsden D, Richardson R (1994), 'Performing for pay? The effects of "merit pay" on motivation in a public service', *British Journal of Industrial Relations,* 32 (2), pp 243-61

Pfeffer J (1998), *The Human equation: Building profits by putting people first,* Boston, MA, Harvard Business School

Pfeffer J, Sutton R I (2006), 'Evidence-based management', *Harvard Business Review*, January, pp 62-74

Rousseau D M (2006), 'Is there such a thing as evidence-based management?' *Academy of Management Review,* 31 (2), pp 256-69

Scott D, McMullen T D, Sperling R S (2006a), 'Evaluating pay program effectiveness', *WorldatWork,* 15 (2), pp 50-59

Scott D, McMullen T D, Sperling R S (2006b), 'Evaluating pay program effectiveness: A national survey of compensation professionals', *WorldatWork,* 15 (3), pp 47-53

Stajkovic A D, Luthans F (2001), 'Differential effects of incentive motivators on work performance', *Academy of Management Journal,* 4 (3), pp 580-90

Thompson M (1992), *Pay and Performance: The employer experience,* IMS, Brighton

Watson T (1995), *Sociology, Work and Industry* 3rd edition, London, Routledge