Reward Strategy — a practical guide

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1. Background

Most organisations aspire to a state where their management of pay is congruent with a wider set of business objectives. For example, in markets where cost leadership is essential, paybill control is an important strategy; in sectors where service quality is paramount for competitiveness, the incentivisation of pay (or the use of approaches to reward which emphasise culture change) might be a more appropriate strategy.

Pay systems require a major effort to change fundamentally. Impediments include history (which limits some choices), line managers (understanding and willingness to administer), trades unions (severely suspicious of some pay approaches), CEOs & senior managers (invariably conservative & ill-informed).

This note describes how IES has helped employers to make changes to their reward strategies and payment systems, and highlights common 'pressure points' and solutions.

2. Business issues

When seeking help with reward issues, organisations most often 'present' with the following kinds of business issues, usually in combination:

- they have made a **structural change** which has affected their grading arrangements. This frequently means fewer but broader grades. Sometimes they want to use this change as an opportunity to alter the way they describe and reward performance, manage progression both within and between grades and the way they define job roles

- they often see changing their approach to reward as a key element of **cultural change**. This is underpinned by a perceived need to encourage employees to be more performance-oriented and to avoid automatic pay increases for poor performers

- **pressure on costs** prompts many organisations to move away from cost-of-living increases to merit increases, or at least to shift the balance between them.

In addition, they may have a new or growing business unit in which they want to introduce a new approach to pay, they may be keen to introduce more non-pay benefits or they may want to introduce supplements to reward teams or to retain specialists.

The contexts within which these issues arise can be varied. Sometimes a company approaches us with a specific pay problem with which they want help. More and more, companies want to lead the process of change themselves, and are suspicious of the 'standard' solutions offered by management consultants.

3. The IES approach

IES frequently works with employers by providing close support to existing internal project teams or project managers. Much of our work on pay operates through the following mechanisms:

- conducting or facilitating initial scoping exercises on the key characteristics of the desired reward system
- providing executive briefings on current developments in pay and their business drivers
- running or supporting workshops for management teams
- providing technical support for internal projects, through project planning, collecting data, benchmarking with other organisations etc.
- audits of pay schemes either before they change of after they've changed, most frequently through employee focus groups and/or employee surveys.

As no organisation enters into a major review of compensation with a 'blank sheet of paper', our experience is that organisations may need to follow something like the sequence of steps set out in Figure 1 if they are to be successful.

Step 1: What is the business and HR strategy?

These provide the foundations for a coherent and integrated compensation strategy. This involves ensuring that other key elements of HR (such as training, employee development, employee relations, communications *etc.*) are not inconsistent with proposed approaches to reward. For example, IES worked with a company whose business strategy demanded greater innovation from its employees, but which reinforced behaviour which was risk-averse.

Figure 1. Changing your pay system: seven key steps
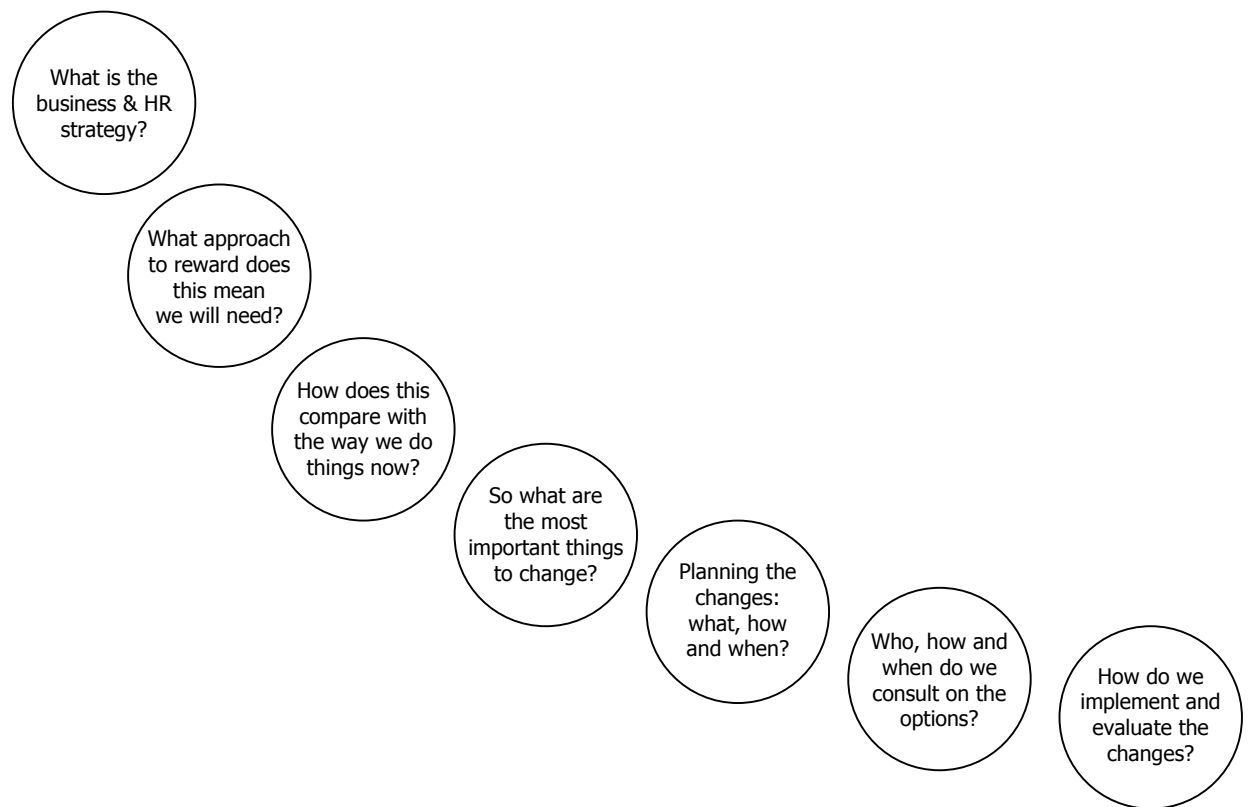
Step 2: What approach to reward does this imply?

At this stage it should be possible to begin to rule in and rule out general characteristics of the reward strategy which will and will not support the business or HR strategy. For example, an emphasis on individual and team excellence and quality may not be felt to be consistent with an approach to compensation which rewards length of service rather than contribution.

Step 3: How does this compare with current practice?

Everyone finds it easy to point out the bad points of a pay system; suggesting changes which will work is often far more difficult. This stage involves devising a set of core criteria to which any new compensation arrangements should comply. This can be a painstaking process because there is frequently a difficult conflict between criteria which everyone thinks are equally important. Thus, in some companies, a core requirement of a new pay system may be that it should increase line manager discretion over the distribution of discretionary pay. At the same time, another core criterion might be that the pay system should be transparent and demonstrably fair. In practice, these two objectives can conflict. This problem needs to be resolved by achieving clarity at the outset on what the 'pecking order' of these criteria are to be.

Step 4: Deciding what needs to be changed

Putting together the requirements of the business and HR strategy, core criteria for a new reward system together with a pragmatic view about what the change priorities should is another important stage in the process. It is important to avoid a long 'shopping list' of changes which are desirable but not achievable. This involves some tough choices about not only the priorities but the sequence in which change is to be attempted. Some of the more straightforward technical changes might take most time to implement if Trades Unions express reservations, and slow the process up. Nonetheless, effort expended at this stage will ensure that work to develop practical pay options is given impetus.

Step 5: Planning the changes

Here, the importance of a detailed project plan for any development work is essential. This involves deciding what activities and tasks need to be carried out in order to arrive a set of costed proposals for a new reward strategy. This plan should include a view about the effort required, the elapse time to allow, the key 'milestones' or decision points on the route, and the precise sequence in which they are to be performed. It is at this stage that accountability for the work and its delivery should be confirmed.

Step 6: Consulting on the proposals

As part of a project plan it must be clear who the key interest groups are with whom some form of consultation will need to take place. These will include an internal 'customer' for the work itself, line managers, trades unions and employees. The nature and extent of consultation will be dependent on a number of factors. Whatever approach is taken, allowance must be made for it to be conducted fully before plans for implementation can be enacted.

Step 7: Implementation and evaluation

Precise arrangements for implementation will often depend on the nature and extent of the changes being proposed. For example, if changes to compensation arrangements require line managers to play a more prominent part in objective-setting or assessing subordinate performance, there is likely to be a need for training to be arranged prior to the changes going live. In terms of evaluation, it is important that the operation of new pay arrangements is monitored against the original success criteria. Too many pay systems wither on the vine because companies like to believe they are working well when they patently are not.

Following these steps, in IES experience, helps ensure greater shared clarity about the principles underpinning a company's reward system, and helps them make more informed judgements about how well the arrangements support the business strategy. In addition, it is frequently easier (having gone through the process) to make changes if dictated by significant shifts in business strategy.

IES and reward strategy

IES has considerable experience helping large employers with their reward strategy, and in researching pay issues. For information on how we can help in this area, see our [consultancy](#) web pages.