

## **WHITE PAPER**

### **“What You Need To Know to Make Variable Pay an Effective Segment of Your Organization’s Total Compensation Plans”**

#### **Variable Pay – Defined**

Variable pay refers to compensation that is received in addition to the base pay. The amount received may be linked directly to individual, team, division and/or organization performance, and is determined (typically) by a variety of measures important to the organization.

- It may be known in advance as an incentive; or
- As an after the fact reinforcement as a bonus.

Typically, payment can be made in many forms: cash, stock, time, or something else.

**Why?** What are the advantages of having “variable pay” as a part of your total compensation philosophy?

When asked these questions, here are some of the answers that were listed:

- Given it is listed as a significant element of our organization’s compensation philosophy, having variable pay as a part of all employee compensation has a tendency to reinforce the fact that we embrace change as a value within our culture.
- It aligns with our “pay for performance” appraisal and management programs.
- It has the intended effect of suppressing any “entitlement” mentality.
- As indicated above, it communicates our organization’s values to employees.
- Because we change it annually to track with our business plan, it has the added advantage of focusing employee attention and activities on those priorities that best align with the current year’s plans.

As indicated above, it must be a part of your organization’s **Total Compensation Philosophy**.

#### **Employee-centered –**

In order for variable remuneration to be effective it must be structured to effectively meet an incumbent’s sense of what Maslow referred to in his Hierarchy of Needs Theory as “self actualization”. There then will be a “buy-in” of results, a sense of meaningful work, and acceptance of the feedback metrics necessary to assure efficacy of the plan.

The employee must also see that their variable compensation plan provides career development, growth, opportunities, and, most of all the security that comes from performance-based rewards.

### External Direct Financial and Non-Financial Rewards –

In addition to base pay, total compensation philosophy of most organizations address such external elements as short-term and long-term/deferred variable salary plans. Also, most organizations include both insured and non-insured employee benefits; award plans; training workshops; and cross disciplinary enrichment assignments.

Finally, the overall culture of an organization, which include quality of life issues such as balance of personal and work life must also enter into the “environment equation”. In today’s changing work place this includes flex-time, working from home, and wellness programs.

### A Variable Compensation Plan fits one of two theories –

As mentioned earlier, a variable pay plan is either “incentive” or “bonus” based:

- Incentives – Such plans adjust behaviors due to anticipation and subjective weighing of future rewards. If an incumbent is to be successful within such a plan they must set, gain approval, and achieve predetermined goals. Such a plan is always being aligned with the organization’s goals and strategic imperatives so as to look to the future one year or more out.
- Bonuses – In such plans behaviors occur due to incumbents’ experience in reinforcement and objective measurement of value of past rewards for past performance. In these organizations, incumbents are “encouraged” to continue successful behavior based on the principle that “past experience (of receiving rewards) will be predictive of future events (more similar rewards)”. Such a plan is always looking back at past events/performance.

### Do you and your organization really want a variable pay plan?

Now you have come to the portion of this mini-white paper where you must ask yourself this question – “Does your organization really want/need a variable pay plan now?” In order to answer this question, you must first answer the following questions:

- Why are you moving to a variable plan?
- What are the core objectives?
- Can the employees impact the objectives?
- Is the organization ready for variable pay?

- What level of trust is there?
- What level of communication exists?
- Can you measure objectives?
- Who is the champion of the program?
- How committed to change are the Senior Leaders?
- Is this the right time?

### How to Design a Variable Compensation Plan –

As with the design of any compensation plan there are ten elements that must be fully considered:

1. Intent
2. Eligibility
3. Participation
4. Performance Criteria-Measurements
5. Goals within Measurements
6. Funding
7. Pay Outs and Timing
8. Benefits Impact
9. Administration
10. Evaluation - Plan Success

If you have interest in pursuing the design of a new variable pay plan and/or revisiting your existing one, contact Perry Resources, Inc. and we would be more than interested in walking you through these ten steps and the more than thirty-five critical questions that this process includes.

You can reach us at –

Perry Resources, Inc.  
[jimperryhr@bellsouth.net](mailto:jimperryhr@bellsouth.net)  
James (Jim) K. Perry, Jr.  
404 – 234 – 2408 (cell #)  
678 – 366 – 1205 (Office #)