SAP SuccessFactors

SAP White Paper
Compensation

Making Compensation Pay

Increasing the ROI from monetary investments spent on employees

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Recent transformations in performance management and compensation practices are making it possible for companies to rethink traditional compensation approaches and reward employees in more meaningful ways. As companies increasingly decouple performance management and compensation, pay decisions are no longer constrained by performance management methods that were not necessarily designed with compensation in mind.

Opportunities and Challenges Associated with Novel Compensation Methods

Enabled by flexible cloud technology solutions, companies are using more diverse compensation methods such as spot awards and non-monetary rewards to engage and motivate employees on a more frequent, ongoing basis. Greater expectations for pay transparency from employees are also creating opportunities for companies to build trust and ensure the right messages are being delivered regarding pay. But these changes also pose risks. Table 1 summarizes current trends in compensation and the opportunities and risks they provide. For example, eliminating performance ratings and allowing managers to make pay decisions without any form of rating can result in inaccurate, biased decisions. Increased use of ongoing spot awards can potentially undermine their value and reduce intrinsic motivation. And unsuccessful attempts to communicate information about pay can cause serious harm to employee trust and motivation.

To support companies with effectively adapting to the next generation of compensation strategies, the Human Capital Management (HCM) Research Team for SAP SuccessFactors solutions conducted a study to gather insights from busi-

Table 1. Trends affecting compensation, the opportunities and risks they pose and recommended solutions.

The Trend	The Opportunity	The Risk	The Solution
Companies are consciously decoupling performance management and compensation.	Pay decisions are no longer constrained by performance management methods that may not have been designed with compensation in mind.	Allowing managers to make compensation decisions without ratings to guide them can result in inaccurate, inequitable decisions.	Require managers to use consistent, structured criteria to guide pay decisions and to justify decisions.
Companies are leveraging more continuous and diverse rewards.	More frequent, dynamic rewards (including spot awards and non-monetary rewards) can engage and motivate employees to be more productive.	Handled incorrectly, alternative rewards can frustrate employees and reduce intrinsic motivation.	Require managers to communicate and to justify reward decisions. Rewards should also be regularly monitored for equity issues.
Employees have increasing expectations around pay transparency.	Being transparent about pay can help companies build trust with employees and ensure they have accurate information.	When conversations about compensation are handled insensitively or inappropriately, they can harm employee trust.	Provide training to managers on how to communicate pay information/decisions effectively.

ness leaders, compensation professionals, managers and front-line employees regarding the current and future state of monetary and non-monetary rewards. We also conducted an extensive review of academic empirical research studying the psychology of compensation and its impact on employee attitudes and performance. Our findings suggest that while companies spend an enormous amount of time and money optimizing employee compensation levels, few can say with certainty that compensation decisions generate a significant return on investment. In other words, companies can say how their money is spent, but not necessarily whether that money is spent wisely.

The study found several significant shortcomings in the practice of compensation, yet also found that most compensation professionals have relatively few concerns about the state of their compensation practices. While this may seem odd, it isn't entirely surprising. This is because, at least on the surface, companies often see to be doing everything they should be. According to a survey of 52 HR, Business and IT Leaders from SAP customer organizations, companies are focused on providing the right rewards to the right people, give managers the autonomy they desire to make compensation decisions, and provide compensation training to managers and employees. But a deeper look reveals the problem is not one of process design. It is one of process application.

For example, while 73% of surveyed organizations report providing compensation training, only 25% believe employees in their organization understand how compensation decisions are made or that managers can effectively explain compensation decisions. Most compensation professionals we interviewed assumed managers were having good conversations about pay with employees. But the employees we interviewed often reported receiving no explanation about how pay decisions that affect their lives are made. The current state of compensation might therefore be summed up as "the processes are okay, but the practices are not".

So why don't companies address this? We believe it is because of the cultural taboo around discussing pay. People are reluctant to voice concerns around a topic that is often viewed as sensitive and impolite. Employees may not like the process, but they do not want to come across as "whining about pay" or acting greedy. As a result, people accept it rather than actively question it. In many ways, the mark for success in compensation seems to be "if people aren't complaining, it must be okay". This is understandable but still surprising. We can think of no other ongoing process that has an operating cost close to that associated with compensation yet receives so little scrutiny to determine whether the money spent on that process is generating a positive return on investment.

As long as gaps exist between the perspectives of employees, managers, compensation professionals and business leaders, compensation will remain a "black box" process that ceases to maximize its potential to influence employee behavior and positively impact overall company performance. To close these gaps, organizations must stop making untested assumptions about what is working and start ensuring better alignment exists between organization expectations, manager actions, and employee outcomes. This paper is an attempt to help companies achieve this goal.

The paper starts with a review of the information used to guide the recommendations. We then discuss the three trends identified in Table 1 in more detail: decoupling performance management from compensation, leveraging more continuous and diverse rewards, and increasing pay transparency. Last, we discuss an underlying issue affecting all aspects of compensation – the disconnect between how compensation decisions are made and employees' understanding of the compensation process.

To close these gaps, organizations must stop making untested assumptions about what is working and **start ensuring better alignment exists** between organization expectations, manager actions, and employee outcomes.

Part I. Research Methodology

In phase I of this study, we reviewed academic empirical research on the psychology of compensation and employees' motivation and performance. This research was published in highly regarded peer-reviewed journals including the Journal of Applied Psychology, Journal of Vocational Behavior, Annual Review of Organizational Psychology, Journal of Personality and Social Psychology, among others.

In phase II, we conducted in-depth interviews with compensation professionals from SAP customer organizations. These customers ranged in size from 2,000 to more than 50,000 employees and included a variety of industries including Aerospace & Defense, Banking, Building Materials, Insurance, Pharmaceutical, Trading, Technology, Telecommunications, and Video Games. The topics covered in these conversations included:

- **Planning –** How are compensation budgets determined in the organization?
- **Decision-Making –** Who in the organization is responsible for determining how to distribute compensation between employees? What methods are used to guide these decisions?
- **Communication –** How are decisions explained to employees and who is responsible for initiating this communication?
- **Monitoring –** How is it ensured that effective compensation decisions are being made?

In phase III, we conducted in-depth interviews with managers and front-line employees in collaboration with Baylor University. These individuals worked for a variety of different organizations and industries including Banking, Construction, Cyber Security, Engineering, Finance, Government, Healthcare, Insurance, Legal, Logistics, Marketing, Military, Pharmaceuticals, Professional Services, Technology, and Travel & Transport. The topics covered in these conversations included:

- **Understanding –** How well do employees/managers understand the compensation methods used by their company, who is responsible for making compensation decisions, and what methods are used to guide these decisions.
- **Communication –** How well are compensation decisions communicated to employees, and who is responsible for this communication.
- **Motivation –** How do reward processes affect employee motivation.
- **Transparency –** How transparent are their organization's compensation processes, and what would they like to change.

In phase IV, we surveyed HR, business and IT leaders from a variety of SAP customer organizations across North America. These organizations varied greatly in size, ranging from less than 1,000 to more than 50,000 employees, and industries, including Automotive, Banking, Consumer Products, Defense & Security, Engineering, Constructions & Operations, Healthcare, High Tech, Industrial Machinery & Components, Insurance, Oil & Gas, Professional Services, Retail, Telecommunications, and Travel & Transport. The topics covered in the survey included:

- The amount of decision-making discretion given to by managers related to compensation
- Training provided to managers and employees on compensation practices
- Expectations related to the communication of pay decisions to employees
- Beliefs about employees' perceptions of fairness and motivation

Part II. Three Trends Changing the Nature of Compensation Today

Most of the major changes happening in compensation could be categorized under three major trends. First, a trend to decouple compensation methods from the methods used for performance management. Second is a shift toward the use of more frequent and diverse monetary and non-monetary awards. Third is a move to greater transparency around pay levels. Each of these trends will be discussed in more detail with an emphasis on how to capitalize on the opportunities each presents while minimizing the risks it creates.

TREND #1: COMPANIES ARE CONSCIOUSLY DECOUPLING PERFORMANCE MANAGEMENT AND COMPENSATION

What's fueling this trend?

Making effective compensation decisions often requires companies to compare employees against one another based on the value they provide to the organization. In contrast, effective performance management requires providing employees with coaching feedback that emphasizes an employee's strengths and weaknesses relative to their own performance. This feedback tends to be most effective when it avoids comparing employees against each other. Compensation and performance management processes both share common goals around maximizing employee engagement and motivation, but compensation and performance management emphasize very different means of achieving these goals. Despite this difference, in the past performance management and compensation were often so tightly linked that many companies struggled to do either well. Today, many companies are decoupling performance management and compensation practices. In particular, they are replacing traditional annual performance reviews linked to pay cycles with processes focused on providing more continuous feedback without any direct link to pay.

Opportunities presented by this trend

Compensation processes can now focus solely on making effective compensation decisions without being constrained by developmentally oriented performance management methods that were not necessarily designed with compensation in mind. This means compensation professionals can reimagine pay processes to ensure compensation decisions are reflective of the true goal of compensation, which is to maximize the motivation and productivity of employees through effective recognition and reward.

Risks posed by this trend

Although a company does not need traditional performance ratings to make effective compensation decisions, allowing managers to make pay decisions without any form of structured rating method can pose risks to decision effectiveness. The most critical of these risks include:

- Confusing pay variance for accuracy. Companies that eliminate performance ratings often continue to see significant variance in how managers allocate pay. This differentiation is sometimes used as justification that the process is working since managers are not paying everyone the same. But paying people different amounts is not the same as paying people fairly or accurately. As two interviewed compensation professionals described,

"We've seen greater differentiation, but can't say whether the differentiation is dependent on performance because we don't have ratings."

"We did away with performance rating scores which helped us move away from our old compensation merit matrix to processes that are more fluid. HR gives managers general guidelines for decision-making, but it's tough to monitor whether managers are using these guidelines effectively since there are no ratings."

- Creating an environment primed for biased pay decisions. The best way to reduce unfair and potentially illegal biases in pay decisions is to ensure that decisions are based on clearly defined performance criteria. This can be difficult to achieve across large populations of employees without the use of some form of rating. Companies should also be careful not to mistake a lack of explicit complaints about inequity as evidence that equitable decisions are being made. As one compensation professional put it, "We don't believe anybody needs ranking or rating to know who their highest performers are. But the risk [of no ratings] is how you know you are creating equity across the company."

- Frustrating high performers while pleasing low performers. Eliminating a formal connection between performance and compensation can demotivate high performers who want to be rewarded for their contributions. It can be particularly frustrating for high performers to discover their lower performing colleagues are getting pay raises equal to or even higher than the ones they receive. In contrast, low performing employees may prefer a compensation process that does not link pay to performance since it benefits them more than high performers. The result is a process that decreases engagement and retention of high performers while increasing engagement and retention of lower performers. Consider perspectives of this employee we interviewed:

"I know I work harder than other people. But it's hard to want to continue to work harder if I'm getting the same bonus as everyone else."

Recommendations to leverage opportunities and mitigate risks

In most cases, companies that eliminate formal performance ratings are not eliminating rating employees altogether. They are simply changing the methods used to determine ratings. As one compensation professional described, "Six or seven years ago, we dabbled with eliminating ratings. Today, ratings are back, but we're rethinking their purpose and putting our focus on results instead. We feel we need to modernize the way we view compensation decisions and think about it more from a business point of view. Are we spending our resources in the most effective way?"

There are several methods companies that eliminate traditional performance ratings can use to maintain the ability to accurately measure, identify, and reward employee performance. Some of the most common of these methods include:

- Replacing individual manager evaluations with manager calibration sessions.
- Replacing ratings of performance with ratings of potential or employee value.
- Evaluating employees based entirely on goal accomplishment.

Alternatively, some companies are eliminating some of the issues associated with performance ratings by removing managers' decision-making responsibility for pay decisions. For example, one company described compensation decisions as being the responsibility of cross-functional leadership teams in their organization as opposed to managers. Managers and employees at this company talk throughout the year about performance and career development and once a year collaborate to create a qualitative description of the employee's major accomplishments, capabilities and development goals. This description then goes to a workforce management team consisting of senior operational leaders and HR business partners who integrate the data about individual employees with broader data about the existing organization, external market trends, and future business strategies to decide how to invest compensation, staffing, and development resources. Although managers provide extensive information to help this team make compensation decisions and are responsible for explaining how decisions are made to their employees, managers do not make actual pay decisions for their direct reports. This company described seeing better relationships between managers and employees as a result of the change, largely due to a shift in managers' role from "judge" to "advocate". As another customer in the early stages of a similar shift put it, "We want to say to managers 'Forget about the pay piece. You just focus on performance'. If we can isolate the compensation piece and deal with it centrally, we can get our managers focused on managing better. Right now, we have pay processes that require a lot of review, guidance etc. by HR generalists for managers. We think a better use of time for them [managers] is to focus on employee performance and business outcomes."

In any case, it is critical that companies have methods in place to ensure that pay decisions are based on actual employee performance and not on an employee's negotiation skills or a manager's "intuition". Studies across a variety of work settings have found that gender differences in rewards (i.e., salary, bonuses and promotions) were fourteen times larger than gender differences in performance evaluations. Research has also shown that white men are significantly more likely to be given a raise after asking than are women or employees of color. Despite managers' best intentions, allowing managers to make pay decisions without clearly defined criteria to guide those decisions can be a formula for increasing bias and inequity.

TREND #2: COMPANIES ARE LEVERAGING MORE DYNAMIC AND DIVERSE COMPENSATION METHODS

What's fueling this trend?

A recent study found that 71% of organizations plan to increase their use of alternative rewards including spot awards, non-monetary rewards, additional PTO and career development opportunities. The ability for organizations to offer more flexible, frequent and diverse methods of rewarding employees is in large part due to advances in technology that enable companies to more easily allocate, deliver and track the use of different kinds of ongoing rewards.

Opportunities presented by this trend

Having more flexible, continuous and diverse reward processes can be a significant differentiator for companies. A 2018 survey found that 'financial rewards/benefits' was rated as the most important factor when choosing to work for an organization for millennial employees and the second most important factor for Gen Z employees. Psychological research also shows that the expectation of reward closely following achievement of a significant performance goal is positively associated with employees' perceptions of autonomy and believing that a company values their contributions and cares about their wellbeing.

Risks posed by this trend

To effectively motivate and engage employees, the use of spot rewards must be handled the right way. Research shows that when tangible rewards are expected and only loosely linked with performance level, they can decrease employees' intrinsic motivation toward work. Equity can also become an issue when using spot awards. Many of the compensation professionals we spoke with described managers having total discretion over spot awards with no review from HR so long as the amount below a specified value (e.g., less than $1,000). It is important to remember that pay is pay, and even small awards (monetary or otherwise) will frustrate and demotivate your employees if they are distributed inequitably or without explanation.

Recommendations to leverage opportunities and mitigate risks

Requiring managers to justify their reward decisions (e.g., explain what the employee did to earn a reward) can be useful to help ensure fair, equitable decisions are being made.

It is also important for managers to recognize that money is not the only type of reward valued by employees. Many of the employees interviewed as part of this study reported wishing their organization made greater use of non-monetary rewards, such as gift cards, points programs, and even more flexible work arrangements (i.e., additional PTO, opportunity to work from home, etc.). As one employee described, "We have great incentives, but it would be nice if they handed out smaller things during the quarter. Even if it's just something simple like the top performer gets a prize, tickets to a game, whatever. That would be good motivation." Even simple verbal recognition from managers can make a big difference in employees' feeling valued and appreciated.

As another employee stated, "Money has an impact, but not the biggest impact. I like to do a good job. I want to feel needed and wanted in the company. My company is really good about verbal recognition. Any time I do something small, they are good at verbally communicating that they appreciate my help."

Understanding that non-cash rewards and verbal recognition can be just as satisfying and motivating to employees as monetary rewards creates an opportunity for companies to encourage desired behaviors from employees in a more frequent and cost-effective way.

TREND #3. EMPLOYEES HAVE INCREASING EXPECTATIONS AROUND PAY TRANSPARENCY

What's fueling this trend?

According to a 2018 study, only 24% of employees agreed or strongly agreed that their company's pay processes were transparent. However, the majority of companies (58%) report aiming to become more transparent than in the past. The efforts to become more transparent are in large part accelerated by employees' ability to access online crowdsourced salary data. As one compensation professional described, "Employees have more access to pay information than ever before. We have to be prepared. If employees aren't getting the information they want from their employer and they can get it somewhere else, what does that do to trust?" Indeed, many of the employees interviewed as part of this study reported seeking pay information from external websites. As one employee stated, "Absolutely I seek compensation information elsewhere – mostly Glassdoor and similar sites. There's a lot to be said for knowing your compensation and how it compares [with others]." An obvious concern for organizations is that data available on crowdsourced sites may be inaccurate and cause unwarranted alarm. As one compensation professional described, "I do get quite a few emails about things people saw on Glassdoor. Glassdoor is an incomplete measure. But it's all about how you respond."

Opportunities presented by this trend

Increasing transparency around a topic that has historically and intentionally been kept very private can be a major challenge for organizations. In our survey of HR, business at IT leaders from SAP customer organizations, "Transparency around compensation processes" was rated as the third-most relevant challenge facing companies today. But refusing to give employees insight into how, when and why they are paid the way they are paid will inevitably do more harm than good. As one compensation professional put it, "With a black veil over the compensation process, problems and suspicion will always exist. We haven't had the proper philosophical debate about how transparent we want to be on pay. It's a difficult question. But it feels like you have to go through the pain of being transparent to come out in a stronger, better place."

There are many advantages to embracing pay transparency, such as an opportunity to build trust and increasing employee motivation, satisfaction, and perceptions of fairness. For example, one study found that 82% of employees said even if their employer paid lower than the market average for a position, they would still feel satisfied with their pay so long as they understood the rationale behind it. Other research has shown improving transparency and fairness of pay processes to be 65% more effective at reducing employee turnover intentions than paying employees more relative to the market.

Risks posed by this trend

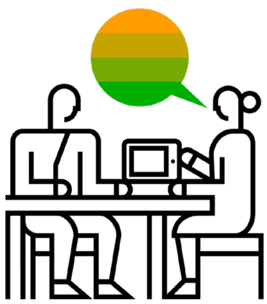
However, any benefits associated with increasing transparency around pay are contingent upon companies being able to explain to employees how the pay decisions are made, who is responsible for making these decisions, the criteria that is used to guide these decisions, and how they can influence the outcomes of these decisions in the future. This information must also be communicated in a sensitive and appropriate way. Effective communication is something often easier said than done. As one compensation professional described, "One example [of the importance of communication] is that many of employees still don't see the linkage between performance and pay, despite our having a strong pay-for-performance culture. I think this is due at least in part to our managers' ability or inability to deliver that message. So much of pay is about perception; an employee could be getting really great pay, but if they don't believe that, it doesn't really work."
Recommendations to leverage opportunities and mitigate risks.

There are many reasons why effective conversations about pay may fail to take place. For example:

- Employees perceive compensation to be an "off limits" conversation topic and don't feel comfortable going to their manager with concerns or questions
- Managers don't understand how components of the compensation package are determined themselves and thus find it difficult to explain these things to employees
- Managers don't want to have potentially uncomfortable conversations with employees about pay decisions
- Managers don't grasp the importance of effectively communicating the process and outcome of pay decisions

The best way to ensure managers have the necessary conversations about pay is to train them on how to do so. But this training must go beyond simple "do's and don'ts". It must give managers an opportunity to practice navigating difficult conversations. Companies should also reflect on their transparency philosophy and the message they send to employees when it comes to talking about pay. Is the company truly as open about discussing pay as it wants to be? When answering this question, remember that in the modern internet era, if companies do not provide employees with accurate data about their compensation levels, their employees may seek this information from a less accurate source.

The best way to ensure managers have the **necessary conversations about pay** is to train them on how to do so.



Part III. Closing the Compensation Communication Gap

Compensation is rooted in the belief that employees are more motivated when they receive tangible rewards for the contributions they make at work. This belief is at the core of the entire concept of "pay for performance". But it only works if people understand the relationship between their actions and the rewards they receive. Yet our research suggests that employees often don't understand how compensation processes work and managers don't feel comfortable or confident talking about pay. At the same time, many compensation professionals seem to believe that unless managers or employees say something is wrong, that everything must be right. Assuming your compensation processes are well understood by employees without testing this assumption is a risky endeavor. Our research suggests that most companies have a long way to go when it comes to ensuring employees understand the relationship between their actions and how the company makes compensation decisions that impact their lives. And if there is one thing companies should want to avoid doing, it is paying people effectively but failing to communicate, so pay becomes a source of frustration rather than motivation.

Table 2. Five recommendations for more effective communication practices.

Recommendation	Description
Make compensation training informative and ongoing.	Identify the information all managers and employees should know and deliver that information in a way that is comprehensible, engaging and interactive.
Survey managers and employees to identify knowledge/confidence gaps.	Talk with managers and employees about their perspectives related to compensation and use results to drive changes to practice/philosophy.
Emphasize the prioritization and importance of effective communication.	Managers should be required to justify their compensation decisions and should consider having good conversations with employees about their pay.
Train managers on how to communicate difficult pay decisions.	Train managers to effectively communicate pay decisions, focusing on appreciation, accurate explanation, and future actions.
Encourage compensation conversations across the organization.	Conversations about pay should not only occur by managers to employees; employees should also feel comfortable initiating communication and sharing their perspectives, questions and concerns upward in the organization.

To close the compensation communication gap, companies first have to ensure they have compensation methods worth talking about. For example:

- Do we have a standardized, consistent and equitable method for differentiating between employee contributions and investing more in employees who provide more to the company? Or alternatively, do we tend to pay all people the same (bad) or just let managers make pay decisions based on untested intuition (worse)?
- Have our rewards (monetary or otherwise) evolved to ensure we attract the best talent and motivate employees throughout the year? Or do we focus only on rewards that occur within the two-week annual compensation cycle?
- Effective communication starts with having a process worth communicating. However, good processes are only one piece of the puzzle. Even world class compensation processes are bound to fail if they are poorly communicated to the managers and employees whose lives are affected by them. In this sense, communication is like the wings on an airplane. It doesn't matter how much power you put into the engine; without good wings, the plane will not get off the ground. The same can be said for compensation. Without effective communication, even the most sophisticated pay processes and thoughtful decisions will fail to motivate and engage employees.

The following are five recommendations to ensure more effective compensation communication practices:

1. MAKE COMPENSATION TRAINING MORE INFORMATIVE AND ONGOING

Many of the employees interviewed for this study reported having only a basic understanding of compensation practices and feeling as though talking about pay was an off-limits topic. Many of the managers interviewed admitted struggling to have good conversations with employees, either because they did not understand how compensation decisions were made themselves or because they were unsure of what information they should and shouldn't share with employees. While the best way to deliver information and set expectations about compensation is likely through compensation training, existing training strategies are clearly not working as well as they should be. While 73% of surveyed organizations provide compensation training to employees and managers, only 57% believe this training for managers on how to explain compensation decisions is effective and only 51% believe training for employees on how compensation decisions are made is effective. Our interviews revealed that managers and employees often left compensation training feeling overwhelmed and confused rather than confident and well-informed.

One of the biggest problems with most compensation training is that it tends to only occur once. As one employee described, “I was provided onboarding information related to compensation, but it’s been so long now that I can’t remember most of it. I didn’t get re-onboarded after promotions.” When training is only provided to employees during onboarding, information can quickly become out of date or forgotten entirely. Understanding compensation, particularly aspects related to justifying why some people are paid more than others, can quickly become complex. Simple, one-time training programs are unlikely to be effective for such a sensitive topic.

A knowledgeable manager prepared to make effective compensation conversations with employees will be able to answer the following questions:

- What is the organization’s compensation strategy?
- How does this strategy align with actions expected of managers? For example, how are managers expected to differentiate between employees? Is the organization comfortable giving some employees something and others nothing?
- What is the organization’s philosophy around transparency? What information are managers permitted and expected to share with employees?
- How are compensation decisions made across the organization? What steps are taken to ensure compensation decisions are made fairly, consistently, and equitably?

An employee who is well-informed regarding compensation decisions will confidently agree with the following statements:

- I understand how my pay is determined.
- I know how my pay compares with my peers.
- I feel comfortable going to my manager with questions about compensation.
- My manager explains pay decisions to me in a timely and appropriate manner.
- I know what I can do to increase my perceived value within the organization and earn more.

Some of this information can be communicated through online learning modules and corporate portals. But it is also valuable to include a live and interactive component to compensation training where managers and employees have an opportunity to ask questions and ensure their understanding.

2. SURVEY MANAGERS AND EMPLOYEES TO IDENTIFY KNOWLEDGE GAPS

Efforts should be made to find out what is and isn’t working when it comes to compensation communication. Do your employees understand how compensation decisions are made? Do your managers feel comfortable having difficult conversations with employees about pay? Do not assume you know the answer to these questions until you ask. As one compensation professional described, “We provide training directly to managers and employees related to compensation, FAQs, etc. But we did focus group interviews this year and the reality is that neither employees nor managers understand the compensation program. They don’t understand how decisions are made. It’s not resonating. It’s just too overwhelming alongside all of the other information managers and employees have to regularly take in. This is something we have to address moving forward.” This is also one of the best ways to challenge existing assumptions about the effectiveness of compensation training and communication.

For example, imagine learning that only a small percentage of your managers are able to explain the rationale behind pay decisions. This is the sort of finding that can trigger investments in new or additional training material.

3. EMPHASIZE THE IMPORTANCE OF EFFECTIVE COMMUNICATION TO MANAGERS

One of the best ways to ensure conversations about compensation take place is to make the conversations a priority. Managers should be comfortable explaining their compensation decisions to others. And they should consider having good conversations with employees about pay as part of their job as a manager. The employees we interviewed found it confusing and frustrating when decisions affecting their pay (even in a positive manner) were not explained to them. As one employee said, "Supervisors or managers are responsible for communicating that [bonuses or raises]. But they don't do it well, it's very vague. I found out the day they were handing out the check, 'hey, here's a bonus'". Another stated, "I usually won't know I got a bonus until it appears in my pay check. A lot of times it just shows up." It may be useful to emphasize the impact communicating compensation decisions has on employee attitudes to convince managers of the value of having compensation conversations, even when those conversations are uncomfortable and managers would prefer to avoid having them.

4. TRAIN MANAGERS TO COMMUNICATE PAY DECISIONS SENSITIVELY AND APPROPRIATELY

Talking about pay can be difficult and uncomfortable. It is important that managers know how to have these conversations in a manner that is sensitive and appropriate. For example, do managers know how to respond if an employee brings forward salary data they found online and asks for a raise? Do managers know how to explain to an employee that they are not receiving a raise in a way that makes an employee feel hopeful about the future as opposed to demotivated? While there is not a magic phrase that will be appropriate for every situation, there are several things managers should keep in mind when navigating compensation conversations. Whether the outcomes of a pay decision are good or bad, conversations between managers and employees should focus on more than just a number. Managers should show their appreciation for the employee's contributions, share how decisions were made (i.e., explain the criteria used to guide the decision) and explain what the employee can do in the future to earn more.

5. ENCOURAGE COMMUNICATION ABOUT COMPENSATION UP, DOWN AND ACROSS THE ORGANIZATION

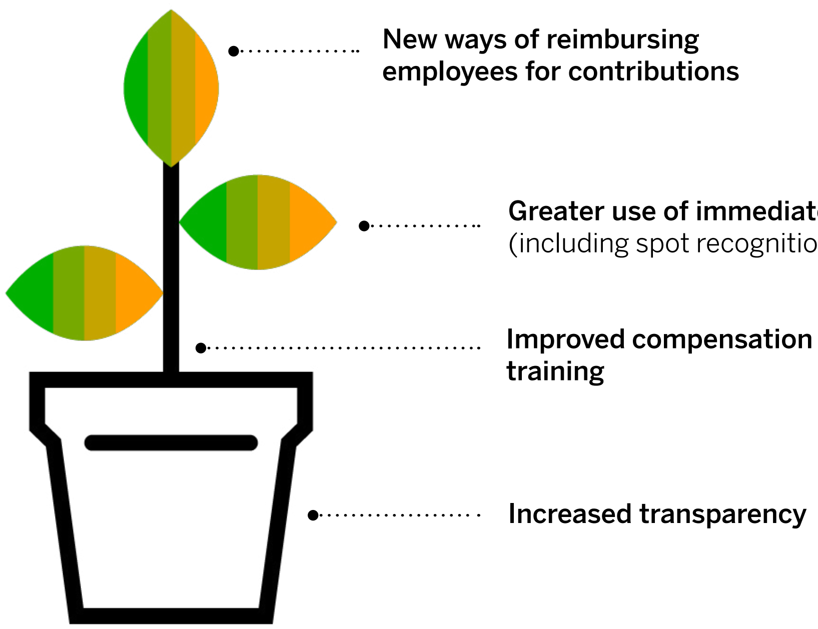
70% of conversations about pay happen between managers and employees. Employees interviewed as part of this research perceived their manager as being the "information gatekeeper" and person responsible for initiating communication about pay. Yet many managers we spoke with assumed that if employees had questions or wanted to talk about compensation, that they would come to them. The result was that conversations about compensation often ceased to exist altogether. Expecting managers to anticipate an employee's desire to talk about pay may be unreasonable. But it is not unreasonable to require managers to check in with their employees about compensation and ensure that employees feel comfortable coming to them with questions or concerns. Compensation is too complex and important a topic to rely on one-way, top-down communication alone. Conversations that start with employees and are communicated upward are also necessary to ensure alignment across the entire organization.

Part IV. Conclusion: Where is Compensation Headed from Here?

Throughout this paper, we have described various trends affecting the nature of compensation and the role technology has played in enabling these trends. In the future, we suspect technology will continue to play a major role in advancing compensation practices. However, we predict the most significant revolution in compensation will be much less about the amounts companies pay employees and more about the impact these amounts have on employee productivity and overall company performance. In other words, we do not believe the answer to the compensation problems facing organizations today is just to pay people more money. This solution is economically unviable, and psychologically, unfounded. In fact, psychological research has shown that employees understanding of how salaries are determined in their organization (and believing that process is fair) is often far more important to job satisfaction and trust in management than the actual levels of those salaries.

To increase understanding around compensation, organizations will have to put more focus on transparency and communication. We predict many of the future changes in compensation methods will involve ensuring managers and employees feel comfortable and confident talking about compensation. This will require more frequent and effective compensation training with a specific focus on improving managers' ability to explain compensation decisions and employees' ability to understand these decisions. It will also require a shift in mindset around who is responsible

Figure 1.
Predicted compensation changes (in order from soonest to latest)



for initiating conversations about pay. To be truly impactful, communication about compensation must occur not only top-down (i.e., compensation professional to manager, manager to employee), but also bottom-up. Employees must feel free to express their questions or concerns related to compensation, and business leaders should care about where knowledge and confidence gaps exist within their organization.

We also predict several other changes to take place in the coming years. Figure 1 describes these changes in order of "soonest" to "latest". Many of these have already begun to affect the nature of compensation but we expect they will only increase in the future.

FIRST IS INCREASED TRANSPARENCY AROUND COMPENSATION

This refers not only to transparency around salary levels, but also how salary and other compensation decisions are made. Employees already have more access to salary information today than ever before due to crowdsourced data held on sites like Glassdoor and Indeed. Many organizations are recognizing that being more transparent and increasing communication with employees about how compensation decisions are made can help mitigate the confusion and frustration that occurs when employees come across (potentially inaccurate) comparison data.

SECOND IS IMPROVED COMPENSATION TRAINING

While 73% of surveyed organizations provide compensation training to managers and employees, this training tended to occur most frequently through email or newsletters and resources posted to a company intranet or portal. Only 41% of organizations reported providing training through live hosted webinars or learning courses. Our interviews with compensation professionals also revealed that training focused specifically on interpersonal skills and teaching managers to have difficult conversations tended to be relatively rare. We expect to see a greater focus on training to help employees to understand the various components of their compensation package and how compensation decisions are made in the organization, and helping managers navigate uncomfortable conversations about pay.

THIRD IS A GREATER USE OF IMMEDIATE PAY

We have already seen organizations making greater use of "on the spot" awards and bonuses but believe we will also begin to see organizations offering immediate or "instant pay" options for employees when it comes to their paychecks. According to a USA Today article, a number of organizations are already making use of services that let employees access half the pay they earn on a given day immediately following their shift's end. For hourly employees and particularly those employees who live paycheck to paycheck, the opportunity to access funds immediately can be a significant stress reliever. While there are inevitably jobs where immediate pay options will be more or less appropriate, we believe waiting until the end of the month to be paid will soon become more the exception than the rule.

FOURTH AND FINALLY IS A CHANGE IN WHAT IT MEANS TO TANGIBLY REIMBURSE EMPLOYEES FOR THEIR CONTRIBUTIONS

While alternative rewards are already quite popular in many organizations, we believe the next generation of these rewards will play a major role in salary negotiations and even serve as alternatives to traditionally offered benefits. For example, offering employees housing or daycare options. In the long run, constraining "compensation" to money alone does not make sense. People do not work only for money, but for a lifestyle. Personalized reward options can serve not only to increase employee engagement but also to decrease stress.

Recent transformations in performance management, technology-enabled advances in compensation practices, and growing acceptance around new methods of compensation make it possible for companies to radically rethink traditional compensation approaches and reward employees in more meaningful and impactful ways. But all these innovations hinge upon better transparency and understanding. Regardless of their type or value, rewards will not work if employees do not understand the relationship between their effort and those rewards. Ensuring maximal impact from compensation is not just about spending more money; it is about changing how money is spent and improving transparency so that people understand it.

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