Pay is always an emotive issue but the recent recession has focused employees’ attention on it even more than usual. Pay freezes, vociferous debates over bonuses, redundancies and an increase in businesses offering employees reduced hours/part-time work to offset wage costs: this has been the backdrop to remuneration in 2010.

If the economic recovery remains on track, then private sector pay settlements in 2011 are likely to be higher than in 2010. But the recovery is fragile, as Treasury figures showing the UK economy contracted in the last three months of 2010 reveal. Meanwhile, public sector pay is in the spotlight and in December Will Hutton published the Fair Pay Review’s interim report, having been commissioned by prime minister David Cameron and chancellor George Osborne to lead a review into fair pay in the public sector. Hutton recommended a pay multiple of 20:1 between the highest and lowest paid in public sector organisations.

Research conducted by UK professional body, the Chartered Institute of Personnel and Development, finds that the most likely danger facing organisations in pay terms is not that bonus schemes encourage risky behaviour but that reward is being poorly communicated. Money is being wasted because poor communication of pay and reward means budgets are being spent without anyone understanding what their teams are being rewarded for.

In this first HR magazine/WorldatWork survey into pay practices across all economic sectors in the UK, HR directors and senior managers were asked about their pay strategies. It is clear that our findings back up the need for better communication.

Shockingly more than a third of the respondents did not have a strategy around pay. Not quite a third had a clear strategy that could be communicated to staff, helping them to understand how remuneration fits into the organisation’s plans.

Unsurprisingly, 54% had implemented a pay freeze in the past 12 months while more than a third had made mandatory redundancies in 2010. While the scale of City bonuses has made this type of incentive a political hot potato, nearly three-quarters of organisations surveyed had a bonus scheme in place. Without a strategy, though, it is difficult to know whether employees understand such schemes. More importantly, are they delivering the productivity needed for better organisational performance.

Siân Harrington, editor, HR magazine
There are perhaps as many different ways to pay employees as there are employers in the world. Like anything, there is good reward design and bad, but there is rarely one ‘best way’ to reward employees that transcends all industries and companies.

Indeed, data from this survey, conducted with HR magazine, underscores the continuing challenges that many organisations face in designing and communicating effective reward and remuneration plans. Among all respondents, only about 64% indicate that their organisation has either a written or unwritten reward strategy. In other words, more than a third of the companies surveyed do not have a documented reward strategy. This figure is troubling because there is ample evidence of a simple equation which indicates that greater employee communication about reward systems and how pay is determined can mean greater engagement.

Further complicating an already complex situation has been the highly unstable economic situation. During the past 12 months, 54% of UK organisations in the survey instituted pay freezes, and fully half froze hiring. Mandatory redundancy was also a common action, taken by 35% of organisations in the survey.

The high percentage of companies implementing redundancies also illuminates another piece of data, that only about one in three (28%) organisations report having detailed, formal severance schemes; most are not detailed or documented.

In aggregate, the survey data here demonstrates a troubled state of play with regard to reward in 2010-11. One would think that pay, a critical factor in employee attraction and important to employee retention and motivation, would be a prime topic on which organisations should focus in a down economy and reinforce messaging on an ongoing basis. Or, perhaps the state of reward is so unimpressive because organisations have been too busy simply trying to run their businesses in the past two years, and reward systems have been neglected.

The beauty and curse of employee reward, however, is that regardless of whether your programme is hidden in the shadows or front of stage, your employees will always have some opinion about it. The question is: are they going to form that opinion based on well-crafted information that you provide, or at the pub after work? The answer is probably some combination of both, so you might consider providing them with as much relevant information as you can to tip the scale of information in your favour.

Ryan Johnson, vice president, research at WorldatWork
Executive overview

While the term ‘the age of austerity’ continues to be bandied around boardrooms, the fears of redundancy, pay cuts, pay freezes and other ‘difficult decisions’ remain at the forefront of employees’ minds as they live in the shadow of recession, while the emotive subject of pay has become an increasingly serious issue for employers.

These are the key findings from this HR magazine/WorldatWork Pay Practices Survey, conducted during 2010.

This is the first year HR magazine has teamed up with WorldatWork to investigate pay practices across all sectors of the economy. The results make interesting reading as employers move tentatively out of recession and into recovery.

Over the past year, despite evidence of growth in the markets, employers kept a tight rein on their purse strings, fearing a ‘double dip’ in the economy. This is hardly surprising considering conflicting reports from economists, with some predicting that the Government’s Comprehensive Spending Review in October last year could mean job losses of 725,000 in the public sector.

On the back of these figures the Chartered Institute of Personnel and Development, the UK’s professional body for those involved in the management and development of people, concluded that the total count of redundancies over the next four years could peak at 1.6 million.

The HR magazine/WorldatWork Pay Practices Survey 2010 did show that cost-cutting methods loomed large in terms of remuneration and compensation – as the number of employers making redundancies approached a third.

But bonuses continued to be a top financial motivator for staff, with almost three quarters of companies maintaining some form of bonus scheme in their business – and more than half of employers surveyed admitting that a number of staff had received a bonus payment over the past year.

The survey also revealed a move away from financial or monetary forms of reward, with employees increasingly enjoying sabbaticals, flexible working arrangements, remote working and jobsharing. This trend allows employers to keep staff costs lower while also engaging employees with work-life balance perks.

However, the findings and analysis present a stark warning for employers. More than a third have no strategy in place about pay and reward – and in an age of austerity, this is not going to cut it in the boardroom if more difficult decisions have to be made.
A pay strategy should be vital but UK employers are failing to develop one

Given pay is the primary reason people come to work, a strategy around how salary is used should be vital for the savvy employer.

However, the HR magazine/WorldatWork survey found that more than a third of employers (36.4%) admit that they have no strategy around pay at all, while 31% have no written pay strategy. This leaves only 32.6% of employers polled who have a clear plan for how remuneration fits into their long-term plans for the business and communicate it openly with staff.

“The existence of a written strategy has been shown to positively affect employees’ understanding of the organisation’s compensation plans or schemes,” explains Kerry Chou, compensation practice leader for WorldatWork.

According to statistics from WorldatWork, the prevalence of defined pay strategies in UK organisations appears to be much lower than that of the US. Compared to 91% of US organisations that have either a written or unwritten strategy (policy), less than two-thirds (approximately 64%) in the UK indicate having a strategy.

Methodology

HR magazine surveyed 313 business people with a responsibility for HR in their organisation, using an online poll, between September and November 2010. The majority of respondents were HR managers (29.8%), HR directors (13.8%), heads of HR (8%) or managing directors/chief executives (7.6%).

The size of respondents’ organisations varied, with 34.1% working with fewer than 100 staff and 33% in organisations with in excess of 1,000 employees. And, of those polled, 53.6% reported a turnover of more than £10 million over the past financial year, with 6.8% reporting more than £1 billion in turnover.

Respondents represented all sectors of the economy, with 9.5% coming from local government, 10.2% from professional services, 8% from the charity or voluntary sector, 6.2% from business services and 6.2% in education.
Pay methods still most popular way of incentivising staff

Despite the fact most employers do not have a written pay strategy, the vast majority of respondents still use pay methods to incentivise staff. The most common pay schemes were overtime (37.4%), long-service bonuses (28.8%), performance-related pay (25.9%) and job relevant salary structures (25.6%). So, as is evident, during the recession and upturn, most employers were applying various types of salary adjustments for staff as a form of engagement tool.

But group incentives (23.3% use them) and individual bonus/commission structures (adopted by 15.3% of those polled) are also serious considerations for employers, as the changing nature of pay practices unfolds.

Ryan Johnson, vice president, research at WorldatWork, explains why. “Partly because of the recession and partly despite the recession, there has been considerable change to incentives over the past two to three years. Nearly one-third of participating companies report they made changes driven by the recession, while half made changes for other reasons. Together, more than three-quarters of companies made significant alterations to their incentive plans.”

And the findings show the biggest incentive employers have in their armoury is a non-financial one.

Flexible working is used by almost two thirds (62%) of those surveyed while 19.2% compress the working week for staff, 42.8% have adopted some form of remote working arrangement and 20.8% permit job sharing.

Johnson adds: “Compared to other employee reward programmes, flexible working and remote working seem to be rising significantly in several countries.

“It has been a perfect storm – fuel prices, leading-edge technology and the push for work-life flexibility have all come together in the past 12 months to create a pretty dramatic increase in telework.”

WorldatWork research also finds that the US employers are still more advanced in offering work-life balance perks.

Across the pond, 15% offer sabbatical leave programmes, typically unpaid, whereas only 6.7% offer this in the UK. However, they are usually paid.
Cost containment and reduction dominant over past financial year

In spite of bonuses being paid out and employers continuing to put budget behind financial and non-financial engagement schemes, cost containment has been dominant over the past financial year, with a massive 54.3% of employers having been forced to freeze pay. This number rises to 88.5% of respondents from local government organisations. A further 10.2% cut back on staff hours or reduced pay.

But decisions around pay were only one method by which employers are controlling costs. The findings show that other decisions include recruitment freezes (49.8% overall and 80.8% in local government), mandatory redundancies (34.8%) and voluntary redundancies with incentives (21.4%). A tenth of those surveyed had cut employees' pay and almost a tenth (8.6%) had reduced the contribution they made into company pension schemes.

According to WorldatWork's Chou, who drew findings from WorldatWork's most recent Annual Salary Budget Survey, firms on both sides of the Atlantic have taken similar measures to contain or reduce costs.

Pay freezes were the most common strategies for both UK and US organisations. But Johnson admits only 24%-50% of employers in the US took the action to freeze employee pay while in most cases less than a third (18%-36%) of US firms implemented a freeze on recruitment. In the US, 23%-48% of companies have also laid off employees.

"The economic crisis forced many firms globally to take cost management or cost-cutting activities, such as hiring and salary freezes, layoffs and bonus reductions, although there were significant regional differences in the nature and extent of those actions," says Johnson.

"These cost-cutting steps took their toll on workers. Employers acknowledge their cost-cutting actions increased employees' workloads and work-related stress. These measures had a negative impact on employee engagement and workers' ability to balance their work and personal lives. In the next few months, employers ought to reassess their employee value proposition to key in on those factors, both tangible and intangible, that would help them attract and retain talent."
It is time to review severance policies

Even when making redundancies, employers who took part in the survey were divided on the best way to operate their severance schemes. Less than a third (27.8%) had detailed severance policies in writing, outlining the value of severance payments should a member of staff have to go through redundancy consultations, while almost one in every seven employers (15.3%) do not have any written severance schemes and policies at all – and 1.9% only have employment contracts for top executives.

But WorldatWork’s Johnson issues a stark warning for employers who have not reviewed their severance arrangements in recent times. “The distribution of data seems to indicate that organisations want structure and flexibility with regard to their severance plans. It reflects the volatility of the times, where you just don’t know what employee action you might need to take tomorrow,” he says. “Regardless of where your organisation is on the guidance/flexibility continuum, as a minimum all severance policies or philosophies should be reviewed regularly, about once every 12-18 months. “In this day and age, it just isn’t smart to set it and forget it.”

Bonuses most popular form of incentive

When it comes to financial arrangements, bonuses are still the most popular form of incentive with a massive three-quarters of those polled (73.5%) having a bonus scheme in place and 51.8% of all respondents paying staff some form of bonus in the last financial year.

But in terms of recent incentive plan payouts, organisations in the UK that took part in the HR magazine/WorldatWork survey, appear to have a wide variance of results, with 40.3% indicating that their incentive or bonus schemes paid out at or above the target level. Conversely, 33.2% said their payout was either below target or no bonus was paid at all.

Nonetheless, the survey could hide the fact that, while a large number of organisations continue to pay bonuses, they could have cut down on the numbers of people receiving them, focusing on the higher echelons, while those at the coal-face might have had to forgo their Christmas bonus.

Another factor behind the disconnect between high numbers of organisations paying bonuses in spite of pay freezes could be that, with pay frozen, ad hoc bonuses could incentivise the high performers within the business, so the strategy is to give bonuses only to the most deserving.

Bonuses are not adding to a fixed cost base when it comes to pay, so where organisations are forced to freeze pay, they can link bonuses to the profitability of the company and save this cost. But WorldatWork’s Chou claims the situation with bonuses is indicative of the wide-ranging effects the economy continues to have on different organisations, where some appear to be thriving or at least recovering while others remain in deep distress.

She explains: “With the wide variation in payouts by those companies with bonus schemes, and another quarter of organisations with no incentive scheme at all, the opportunity for organisations to provide real differentiation in this aspect of their total rewards programmes versus their competitors appears to be substantial.”
Work-life balance has some way to go

The headline findings when it comes to flexible working and work-life balance perks are that almost half (46%) of the HR professionals or CEOs surveyed in the UK claim somewhere between 1% and 10% of the staff in their organisation, who are able to work remotely, do so at least once per week. A further 1.9% claim everyone in their firm who can work away from the normal workplace carries out their job remotely at least one day per week. However, in spite of these positive findings, just under a fifth (17.3%) admit none of their staff works remotely on a regular basis, regardless of whether or not they could potentially do so.

The bulk of employers fit into the middle when it comes to flexible working, but few allow more than 60% of staff to work flexibly at least once a week. “Dramatic technological advances means that being at work does not necessarily mean being at the office,” muses Adam Sorensen, global rewards practice leader at Worldat-Work. “Managers must learn to manage what they can’t see. Work-life initiatives continue to be an important element in creating a holistic and compelling reward strategy. But simply having work-life policies is unlikely to have a significant impact on engagement and retention. Instead, organisational leaders and line managers must demonstrate a real commitment to creating a work culture that supports employees both on and off the job. Work-life is about valuing people not only for what they produce but also for who they are.”

Significant opportunity to differentiate base pay levels in UK

The base salary should be the foundation for how pay is calculated throughout a company. The survey shows that, of the UK employers who have a basic salary goal, pay is at the middle of the labour market (40th-60th percentile). However, in all cases, more than half of those surveyed do not have a base salary target or goal—or it varies.

For each of the following types of jobs, what is your organisation’s base salary target (or goal) compared to the relevant sector?

<table>
<thead>
<tr>
<th>Type of Job</th>
<th>Below 25th Percentile</th>
<th>25th - 40th percentile</th>
<th>40th - 60th percentile</th>
<th>60th - 75th percentile</th>
<th>Above 75th Percentile</th>
<th>Varies / Do not have a target</th>
</tr>
</thead>
<tbody>
<tr>
<td>Senior management</td>
<td>4.3%</td>
<td>6.9%</td>
<td>19.3%</td>
<td>9.5%</td>
<td>9.9%</td>
<td>50.2%</td>
</tr>
<tr>
<td>Middle management</td>
<td>4.3%</td>
<td>8.4%</td>
<td>20.1%</td>
<td>11.0%</td>
<td>5.4%</td>
<td>50.8%</td>
</tr>
<tr>
<td>Professional (staff with technical degree or skill)</td>
<td>4.4%</td>
<td>10.1%</td>
<td>20.8%</td>
<td>8.7%</td>
<td>4.7%</td>
<td>51.3%</td>
</tr>
<tr>
<td>Sales</td>
<td>5.9%</td>
<td>10.0%</td>
<td>19.9%</td>
<td>4.4%</td>
<td>5.5%</td>
<td>54.2%</td>
</tr>
<tr>
<td>Administrative</td>
<td>6.3%</td>
<td>12.8%</td>
<td>20.2%</td>
<td>7.0%</td>
<td>3.0%</td>
<td>51.0%</td>
</tr>
<tr>
<td>Production (back office)</td>
<td>8.7%</td>
<td>11.7%</td>
<td>17.7%</td>
<td>7.8%</td>
<td>2.8%</td>
<td>53.4%</td>
</tr>
<tr>
<td>Staff on a graduate scheme</td>
<td>8.1%</td>
<td>7.2%</td>
<td>16.7%</td>
<td>5.7%</td>
<td>1.5%</td>
<td>62.7%</td>
</tr>
<tr>
<td>Other</td>
<td>4.9%</td>
<td>5.4%</td>
<td>14.6%</td>
<td>4.4%</td>
<td>2.4%</td>
<td>68.3%</td>
</tr>
</tbody>
</table>

Chou explains: “As is the case with the prevalence of pay strategies, the existence of a strategy for base salaries versus market is less common in the UK than in the US.” But she adds: “The vast majority of US companies (73%-86% depending on job category) target the 40th-60th percentile of the market, while only 15%-20% of UK companies do likewise. In fact, 50%-68% of UK organisations indicate they have no specific target, while only 4%-9% of US companies responded similarly.”

The survey also revealed that UK employers who took part were more likely to have targets at the extremes, such as below the 25th percentile or above the 75th percentile, than their US counterparts. For example, 9.8% have a basic salary goal for their most senior executives above the 75th percentile.

“This wide variation in practices, similar to variable pay practices, should provide UK organisations with significant opportunities to differentiate base pay levels versus others when competing for workers in the labour market,” says Chou.
Market pricing leads way in setting pay

Within the group of employers that adopt some form of pay strategy, just under half (48.2%) of the HR staff or CEOs who took part in the HR magazine/WorldatWork survey, still look to other organisations in the market to compare salaries when deciding on a pay strategy for their own employees, using the market pricing idea. This means, in essence, staff will be paid a ‘going rate’ for the job they do.

The next most popular pay strategy is the ranking method (used by 22% of survey respondents). Here employers create a hierarchy within their own business and ‘rank’ jobs from the high echelons where staff enjoy the highest salaries, through a number of comparable levels, down to the lowest ranks within the business.

Although much more unpopular with employers as a pay strategy, paired comparison is used by 8.6% of employers. This matches each job description within an organisation to other jobs, in a bid to ensure all employees are paid fairly in what they do, compared to their colleagues across the business.

A similar number of those polled (12.5%) have opted for a point-based strategy (point factor), where each part of an employee’s job description, duties and/or roles is given a defined number of points and the staff with the highest points receive the highest salaries.

Finally, the most complicated strategy put to respondents and used by 8.6% is the job component method, which measures an individual’s salary against at least two independent variables, within the market and within the company to value the worth of the job. Put simply, this is a mixture of the ranking method and market pricing.

Chou says: “Market pricing is the most prevalent job evaluation method in both the UK and US, although it is more prevalent in the US. While less than half of the firms we surveyed in the UK utilise market pricing, the percentage is closer to 70%-75% in the US. But the ranking method is much more prevalent in the UK than the US, where less than 4% of employers make use of this system.

Senior roles likely to match survey models

When it comes to matching employees’ jobs to survey models, it is again senior management roles that are given precedence. More than a quarter (26.2%) of those polled claim more than 80% of senior management roles are directly matched to a survey model, compared to 22.8% that match more than 80% of production jobs to surveys.

At the other end of the scale, almost a third (30.8%) match less than 20% of senior management roles to survey model jobs while almost half (47.1%) agree this is the case for production staff.

On the whole, the results are polarised, with the vast majority either matching 80% or more, or 20% or less staff to survey models.

Chou elaborates: “In terms of job matching to survey sources, UK organisations are somewhat dichotomous in practice. While 29%-42% match at least 60% of their positions with survey sources, 30%-47% match less than 20% of their positions. This is another point of contrast between the UK and US, with 59%-69% of US companies matching at least 60% of their jobs and only 4%-8% matching less than 20% of jobs.

“The percentage of jobs that can be matched to surveys has a direct impact on an organisation’s ability to accurately assess their position versus the market,” she warns.
Multiple sources increase data validity

In all cases, 45%-57% of UK organisations use only one survey source when market pricing jobs. The next most common was the use of two sources, with the least common response being three sources.

According to WorldatWork, by comparison, the most common response by US companies is three sources, with 41%-54% indicating they would take this route. One source was the least common response when WorldatWork carried out its own research across the pond.

The UK trend clearly shows that the more senior the staff member, the more time is taken to survey market pricing, with more than a quarter of those who took part in the poll (26.2%) using three surveys for senior management and 22.8% using three for middle management, when recruiting or devising a pay package. This number drops substantially the further down the organisation you look, with only 15.3% of respondents looking at three surveys for production jobs.

“The use of multiple survey sources can increase the validity of data, as several sources can be compared and contrasted for each position in question,” explains Chou.

“In the extreme, too many survey sources make data management difficult and the marginal utility of additional data is usually more than offset by the increase in complexity and costs associated with additional surveys.

“A single source of data can be sufficient in situations where the source is an industry or sector standard that is universally recognised and participated in.”

How many surveys does your organisation typically use for each job when conducting a market pricing analysis?

<table>
<thead>
<tr>
<th></th>
<th>1 survey</th>
<th>2 surveys</th>
<th>3 surveys</th>
</tr>
</thead>
<tbody>
<tr>
<td>Senior Management</td>
<td>25.2%</td>
<td>45.3%</td>
<td>28.5%</td>
</tr>
<tr>
<td>Middle Management</td>
<td>22.8%</td>
<td>47.5%</td>
<td>29.6%</td>
</tr>
<tr>
<td>Professional</td>
<td>19.8%</td>
<td>46.3%</td>
<td>34.0%</td>
</tr>
<tr>
<td>Sales</td>
<td>17.0%</td>
<td>52.4%</td>
<td>30.8%</td>
</tr>
<tr>
<td>Administrative</td>
<td>14.9%</td>
<td>57.1%</td>
<td>28.0%</td>
</tr>
<tr>
<td>Production</td>
<td>29.2%</td>
<td>55.5%</td>
<td>15.3%</td>
</tr>
</tbody>
</table>

Conclusion

This is only the first year of the HR magazine/WorldatWork Pay Practices survey, but the evidence suggests the results next year could be significantly different, given the changing economic climate.

One example of this could be a move away from cost reduction and cost containment strategies. And, as the markets continue to perform well, employers adopting a market pricing strategy may well reappraise their stance.

Nonetheless, polarisation when it comes to pay, which has been evident throughout this year’s findings, will continue between the public and private sectors, with the public sector forced to cut back and the private sector experiencing tentative buoyancy.

But, given the comparisons between the United Kingdom and the United States outlined in this report, the key for employers is governance around pay – an area where UK employers appear to be less developed than their US counterparts.

Employers are strongly advised to take an objective approach to their pay strategies, using robust technology, data and open communication to ensure fairness in paying staff what they deserve.
To win at business, it is critical that your organisation be prepared as the global economy starts to turn around. Motivating and keeping your number one asset — human capital — is a foundational principle to achieve success. WorldatWork can equip your HR team with innovative global reward education and resources, designed to help establish or improve your organisation’s total reward scheme. In addition, you can increase your knowledge for making strategic HR decisions by learning from best-practice examples. Contact us to learn how we can help you achieve your goals.

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