

## Strategic reward

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Strategic reward management is about the development and implementation of reward strategies and the philosophies and guiding principles that underpin them. It provides answers to two basic questions: 1) where do we want our reward practices to be in a few years' time? and 2) how do we intend to get there? It therefore deals with both ends and means. As an end it describes a vision of what reward processes will look like in a few years' time. As a means, it shows how it is expected that the vision will be realized.

The chapter starts with a definition of reward strategy and an explanation of why it is necessary. Consideration is then given to the structure and content of reward strategies. The guiding principles for inclusion in a reward strategy are discussed next and this is followed by a description of the development process and a note of the criteria for effectiveness. Examples of reward strategy are then given and implementation issues are assessed. The chapter ends with an examination of the important issue of line management capability.

### REWARD STRATEGY DEFINED

Reward strategy is a declaration of intent that defines what the organization wants to do in the longer term to develop and implement reward policies, practices and

processes that will further the achievement of its business goals and meet the needs of its stakeholders.

Reward strategy provides a sense of purpose and direction and a framework for developing reward policies, practices and process. It is based on an understanding of the needs of the organization *and* its employees and how they can best be satisfied. It is also concerned with developing the values of the organization on how people should be rewarded and formulating guiding principles that will ensure that these values are enacted.

Reward strategy is underpinned by a reward philosophy that expresses what the organization believes should be the basis upon which people are valued and rewarded. Reward philosophies are often articulated as guiding principles.

## WHY HAVE A REWARD STRATEGY?

In the words of Brown (2001): 'Reward strategy is ultimately a way of thinking that you can apply to any reward issue arising in your organization, to see how you can create value from it.' There are four arguments for developing reward strategies:

1. You must have some idea where you are going, or how do you know how to get there, and how do you know that you have arrived (if you ever do)?
2. Pay costs in most organizations are by far the largest item of expense – they can be 60 per cent and often much more in labour-intensive organizations – so doesn't it make sense to think about how they should be managed and invested in the longer term?
3. There can be a positive relationship between rewards, in the broadest sense, and performance, so shouldn't we think about how we can strengthen that link?
4. As Cox and Purcell (1998) write: 'The real benefit in reward strategies lies in complex linkages with other human resource management policies and practices.' Isn't this a good reason for developing a reward strategic framework which indicates how reward processes will be associated with HR processes so that they are coherent and mutually supportive?

## THE STRUCTURE OF REWARD STRATEGY

Reward strategy should be based on a detailed analysis of the present arrangements for reward, which would include a statement of their strengths and weaknesses. This, as suggested by the CIPD (2004e), could take the form of a 'gap analysis', which

compares what is believed should be happening with what *is* happening and indicates which 'gaps' need to be filled. A format for the analysis is shown in Figure 43.1.

A diagnosis should be made of the reasons for any gaps or problems so that decisions can be made on what needs to be done to overcome them. It can then be structured under the headings set out below:

1. *A statement of intentions* – the reward initiatives that it is proposed should be taken.
2. *A rationale* – the reasons why the proposals are being made. The rationale should make out the business case for the proposals, indicate how they will meet business needs and set out the costs and the benefits. It should also refer to any people issues that need to be addressed and how the strategy will deal with them.
3. *A plan* – how, when and by whom the reward initiatives will be implemented. The plan should indicate what steps will need to be taken and should take account of resource constraints and the need for communications, involvement and training. The priorities attached to each element of the strategy should be indicated and a timetable for implementation should be drawn up. The plan should state who will be responsible for the development and implementation of the strategy.
4. *A definition of guiding principles* – the values that it is believed should be adopted in formulating and implementing the strategy.

## THE CONTENT OF REWARD STRATEGY

Reward strategy may be a broad-brush affair simply indicating the general direction in which it is thought reward management should go. Additionally or alternatively, reward strategy may set out a list of specific intentions dealing with particular aspects of reward management.

### *Broad-brush reward strategy*

A broad-brush reward strategy may commit the organization to the pursuit of a total rewards policy. The basic aim might be to achieve an appropriate balance between financial and non-financial rewards. A further aim could be to use other approaches to the development of the employment relationship and the work environment, which will enhance commitment and engagement and provide more opportunities for the contribution of people to be valued and recognized.

What should be happening	What is happening	What needs to be done
1. A total reward approach is adopted which emphasises the significance of both financial and non-financial rewards.		
2. Reward policies and practices are developed within the framework of a well-articulated strategy which is designed to support the achievement of business objectives and meet the needs of stakeholders.		
3. A job evaluation scheme is used which properly reflects the values of the organisation, is up-to-date with regard to the jobs it covers and is non-discriminatory.		
4. Equal pay issues are given serious attention. This includes the conduct of equal pay reviews which lead to action.		
5. Market rates are tracked carefully so that a competitive pay structure exists which contributes to the attraction and retention of high quality people.		
6. Grade and pay structures are based on job evaluation and market rate analysis, appropriate to the characteristics and needs of the organization and its employees, facilitate the management of relativities, provide scope for rewarding contribution, clarify reward and career opportunities, constructed logically, operate transparently and are easy to manage and maintain.		
7. Contingent pay schemes reward contribution fairly and consistently, support the motivation of staff and the development of a performance culture, deliver the right messages about the values of the organization, contain a clear 'line of sight' between contribution and reward and are cost-effective.		
8. Performance management processes contribute to performance improvement, people development and the management of expectations, operate effectively throughout the organization and are supported by line managers and staff.		

Figure 43.1 A reward gap analysis

*continued*

<b>What should be happening</b>	<b>What is happening</b>	<b>What needs to be done</b>
9. Employee benefits and pension schemes meet the needs of stakeholders and are cost-effective.		
10. A flexible benefits approach is adopted.		
11. Reward management procedures exist which ensure that reward processes are managed effectively and that costs are controlled.		
12. Appropriate use is made of computers (software and spreadsheets) to assist in the process of reward management.		
13. Reward management aims and arrangements are transparent and communicated well to staff.		
14. Surveys are used to assess the opinions of staff about reward and action is taken on the outcomes.		
15. An appropriate amount of responsibility for reward is devolved to line managers.		
16. Line managers are capable of carrying out their devolved responsibilities well.		
17. Steps are taken to train line managers and provide them with support and guidance as required.		
18. HR has the knowledge and skills to provide the required reward management advice and services and to guide and support line managers.		
19. Overall, reward management developments are conscious of the need to achieve affordability and to demonstrate that they are cost effective.		
20. Steps are taken to evaluate the effectiveness of reward management processes and to ensure that they reflect changing needs.		

**Figure 43.1** *continued*

Examples of other broad strategic aims include:

- introducing a more integrated approach to reward management – encouraging continuous personal development and spelling out career opportunities;
- developing a more flexible approach to reward that includes the reduction of artificial barriers as a result of over-emphasis on grading and promotion;
- generally rewarding people according to their contribution;
- supporting the development of a performance culture and building levels of competence; and
- clarifying what behaviours will be rewarded and why.

### *Specific reward initiatives*

The selection of reward initiatives and the priorities attached to them will be based on an analysis of the present circumstances of the organization and an assessment of the needs of the business and its employees. The following are examples of possible specific reward initiatives, one or more of which might feature in a reward strategy:

- the replacement of present methods of contingent pay with a pay for contribution scheme;
- the introduction of a new grade and pay structure, eg a broad-graded or career family structure;
- the replacement of an existing decayed job evaluation scheme with a computerized scheme that more clearly reflects organizational values;
- the improvement of performance management processes so that they provide better support for the development of a performance culture and more clearly identify development needs;
- the introduction of a formal recognition scheme;
- the development of a flexible benefits system;
- the conduct of equal pay reviews with the objective of ensuring that work of equal value is paid equally;
- communication programmes designed to inform everyone of the reward policies and practices of the organization;
- training, coaching and guidance programmes designed to increase line management capability (see also the last section of this chapter).

## GUIDING PRINCIPLES

Guiding principles define the approach an organization takes to dealing with reward. They are the basis for reward policies and provide guidelines for the actions contained in the reward strategy. They express the reward philosophy of the organization – its values and beliefs about how people should be rewarded.

Members of the organization should be involved in the definition of guiding principles that can then be communicated to everyone to increase understanding of what underpins reward policies and practices. However, employees will suspend their judgement of the principles until they experience how they are applied. What matters to them are not the philosophies themselves but the pay practices emanating from them and the messages about the employment 'deal' that they get as a consequence. It is the reality that is important, not the rhetoric.

Reward guiding principles may refer to concerns such as:

- developing reward policies and practices that support the achievement of business goals;
- providing rewards that attract, retain and motivate staff and help to develop a high performance culture;
- maintaining competitive rates of pay;
- rewarding people according to their contribution;
- recognizing the value of all staff who are making an effective contribution, not just the exceptional performers;
- allowing a reasonable degree of flexibility in the operation of reward processes and in the choice of benefits by employees;
- devolving more responsibility for reward decisions to line managers.

An example of a statement of reward philosophy and guiding principles is given in Figure 43.2.

## DEVELOPING REWARD STRATEGY

The formulation of reward strategy can be described as a process for developing and defining a sense of direction. The main phases are:

1. The *diagnosis* phase, when reward goals are agreed, current policies and practices assessed against them, options for improvement considered and any changes agreed.

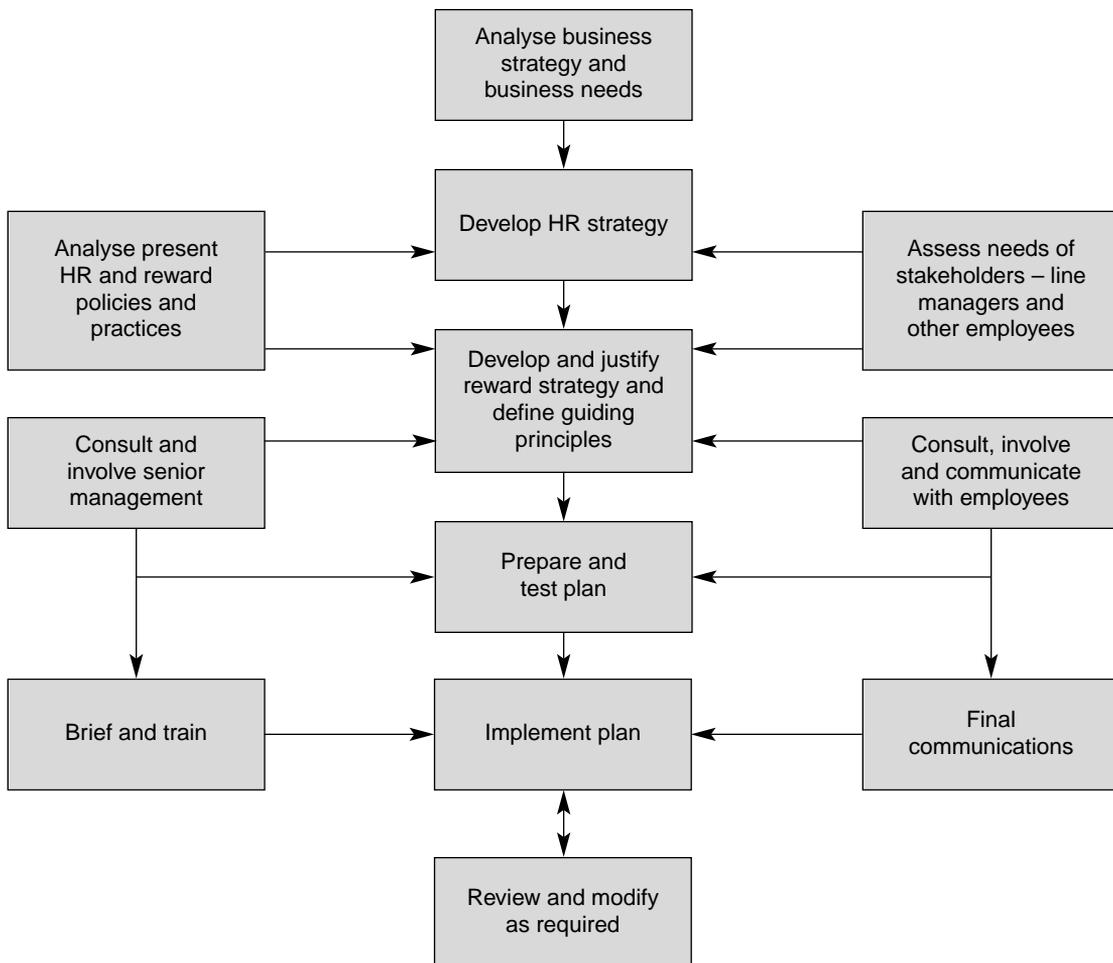
Reward philosophy	Principles
<ul style="list-style-type: none"> <li>We will provide an innovative reward package that is valued by our staff and communicated brilliantly to reinforce the benefits of working for B&amp;Q plc.</li> </ul>	<ul style="list-style-type: none"> <li>Innovative and differentiated policies and benefits.</li> </ul>
<ul style="list-style-type: none"> <li>Reward investment will be linked to company performance so that staff share in the success they create and, by going the extra mile, receive above average reward compared to local competitors.</li> </ul>	<ul style="list-style-type: none"> <li>Basic salaries will be competitive.</li> <li>Total compensation will be upper quartile.</li> <li>We share the success of B&amp;Q with all employees.</li> <li>Increase variable pay as a percentage of overall to drive company performance.</li> <li>Pay for performance.</li> <li>Performance objectives must have line of sight for individuals/team.</li> </ul>
<ul style="list-style-type: none"> <li>All parts of the total reward investment will add value to the business and reinforce our core purpose, goals and values.</li> </ul>	<ul style="list-style-type: none"> <li>Non-cash recognition is a powerful driver of business performance.</li> <li>Pay can grow without promotion.</li> <li>Rewards are flexible around individual aspirations.</li> <li>We will not discriminate on anything other than performance.</li> </ul>

**Figure 43.2** Reward philosophy and guiding principles at B&Q

2. The *detailed design* phase, when improvements and changes are detailed and any changes tested (pilot testing is important).
3. The *final testing and preparation* phase.
4. The *implementation* phase, followed by ongoing review and modification.

A logical step-by-step model for doing this is illustrated in Figure 43.3. This incorporates ample provision for consultation, involvement and communication with stakeholders, who include senior managers as the ultimate decision makers as well as employees and line managers.

In practice, however, the formulation of reward strategy is seldom as logical and linear a process as this. As explained in Chapter 7, strategies evolve. Reward strategists have to respond to changes in organizational requirements, which are happening all the time. They need to track emerging trends in reward management and may modify their views accordingly, as long as they do not leap too hastily on the latest bandwagon.



**Figure 43.3** A model of the reward strategy development process

It may be helpful to set out reward strategies on paper for the record and as a basis for planning and communication. But this should be regarded as no more than a piece of paper that can be torn up when needs change – as they will – not a tablet of stone.

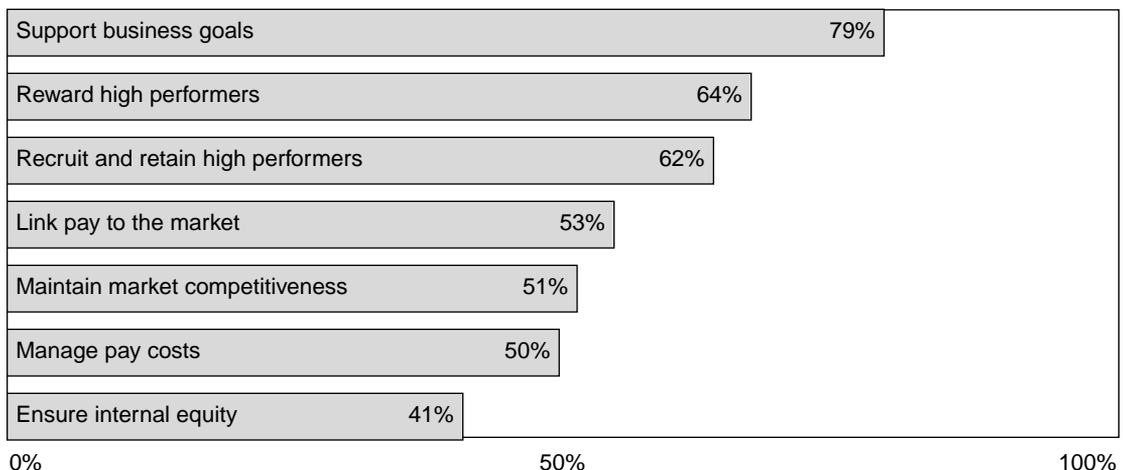
## COMPONENTS OF AN EFFECTIVE REWARD STRATEGY

Brown (2001) has suggested that effective reward strategies have three components:

1. They have to have clearly defined goals and a well-defined link to business objectives.
2. There have to be well-designed pay and reward programmes, tailored to the needs of the organization and its people, and consistent and integrated with one another.
3. Perhaps most important and most neglected, there needs to be effective and supportive HR and reward processes in place.

## REWARD STRATEGY PRIORITIES

The CIPD (2005d) survey into reward policy and practice covering 477 organizations with 1.5 million employees established that 45 per cent of employers had a formal reward strategy that was aligned to the business and human resource strategies of the organization. The top priority, as shown in Figure 43.4, is supporting the goals of the organization, followed by rewarding, recruiting and retaining high performers.



**Figure 43.4** Reward strategy priorities (Source: CIPD 2005d)

## EXAMPLES OF REWARD STRATEGIES

The source of the following examples of reward strategies is e-reward (2004a).

### *AEGON UK*

A good example of the development of a reward strategy is provided by AEGON UK, the insurance group with 4,000 employees. Like many companies, AEGON UK's pay systems and supporting processes such as job evaluation and performance appraisal used to stand alone, apart from other HR processes. The company has adopted a more holistic approach to the development of its new reward system – which it calls the *Human Resources Integrated Approach* – so that from every angle staff can look at the elements of reward, pay management, performance management and career development and observe that they are consistent and linked. The stated objective of this programme is 'to develop a set of HR processes which are integrated with each other and with the business objectives'. In other words, AEGON UK aims to ensure that the processes of recruiting, retaining and motivating people, as well as measuring their performance, are in line with what the business is trying to achieve. *The Human Resources Integrated Approach* is underpinned by a competency framework. The established competencies form the basis of the revised HR processes:

- *Recruitment*: competency based with multi-assessment processes as the basic approach.
- *Reward*: market driven with overall performance dictating rate of progress of salaries within broad bands rather than existing grades.
- *Performance management*: not linked to pay, concentrated on personal development, objective setting and competency development.
- *Training and development*: targeted on key competencies and emphasizing self-development.

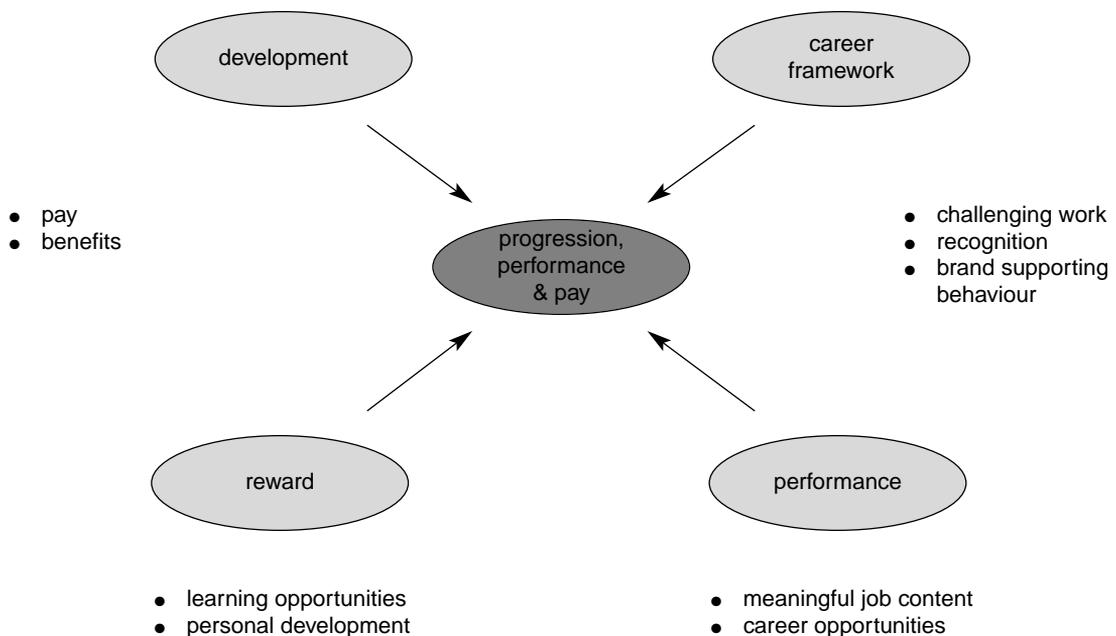
### *Norwich Union Insurance*

*Progression, Performance and Pay* is the name given to Norwich Union Insurance's new total reward strategy. It comprises four main elements:

1. *Reward* – salary and benefits, variable pay, all-employee share option plan and incentive awards.
2. *Career framework* – meaningful job content and career opportunities.
3. *Performance* – challenging work; recognition and brand supporting behaviours.
4. *Development* – learning opportunities and personal development.

As stated in the Norwich Union Insurance's documentation and illustrated in Figure 43.5:

These initiatives... support our commitment to the one team culture reflected in our balanced scorecard. The Progression, Performance & Pay framework is underpinned by the brand values: Progressive, Shared benefit and Integrity. These should be reflected in the way we agree objectives and use the skills, knowledge and behaviours model. Progression, Performance & Pay moves us towards 'total reward' where financial reward is just one element of the reward package. Other elements are benefits, recognition of performance, career opportunities and personal development. In our model these are expressed through reward, performance, career framework and development. This gives us the tools to help build NUI as a great place to work, which attracts and retains quality staff.



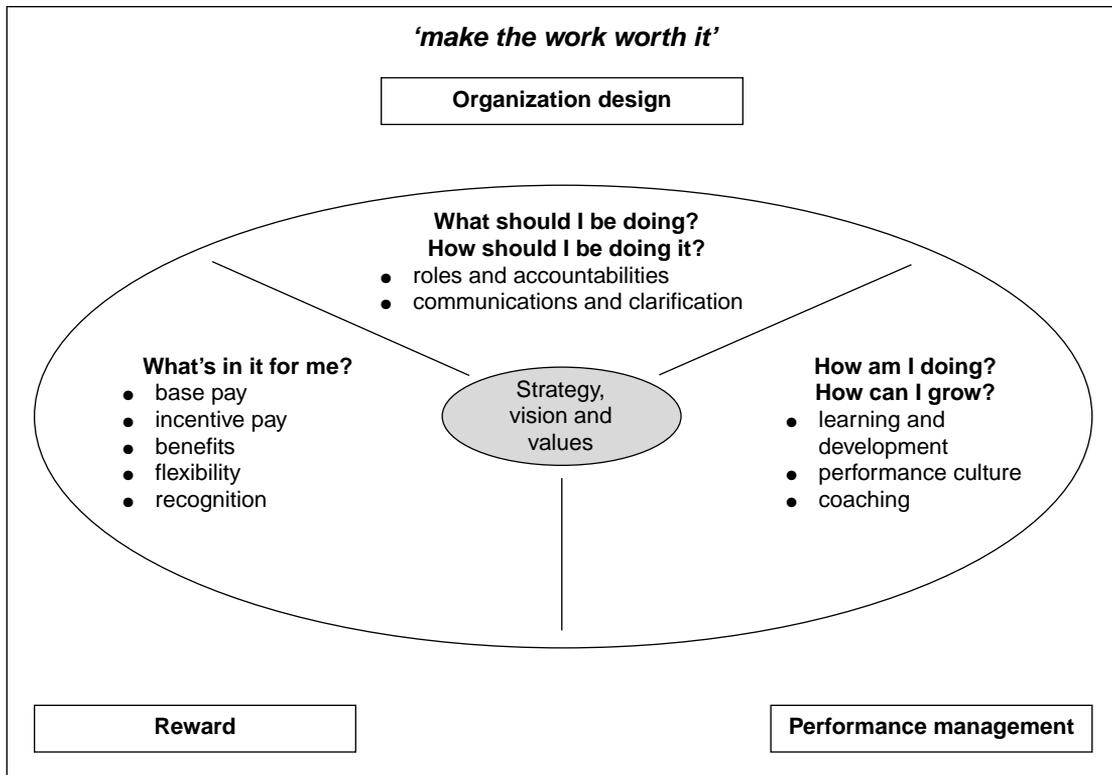
**Figure 43.5** The Norwich Union Insurance Progression, Performance & Pay framework

The framework was accompanied by a commitment from senior management:

- to recognize our best people through career opportunities and reward packages;
- to develop all staff to their full potential;

- to widen career opportunities for all;
- to provide managers with the means to recognize and reward performance locally.

### *Integrated reward at Kwik-Fit*



**Figure 43.6** Integrated reward model – Kwik-fit

### *B&Q*

Will Astill, Reward Manager of B&Q, a retail chain with 25,000 employees, which completed a strategic reward review in 2003, explained to e-reward that:

An overriding theme running through our review was on the desirability of adopting a strategic approach. It wasn't a case of 'let's follow the best practice', nor were we lured into adopting the latest fads and fashions. Applying a bespoke system – taking what someone has done before and adapting it to your organization – will not push you ahead of rivals. Our emphasis throughout the two-year process was on what's right for the business.

### *Other examples*

Other examples are given in Table 43.1 of the ways in which organizations have responded to the needs established by their business strategy and the business and reward issues they are facing. In each case the organizations started with broad-brush statements about their intentions and proceeded from there to prepare action plans and implementation programmes for specific innovations that had been fully justified by a cost/benefit analysis.

**Table 43.1** Examples of reward strategies and their derivation

<b>Organization</b>	<b>Business strategy</b>	<b>Business/reward issues</b>	<b>Reward strategy</b>
Food distribution	Increase efficiency Innovate Cost reduction	Poor team work Inflexible Narrow focus	Broad-banding Team pay Gain-sharing
Engineering manufacturing	Maintain market share Increase competitive edge Develop more sophisticated planning processes	Skill-based pay not working PRP only for managers Performance appraisal ineffective	Link operating plan and performance management Replace skill-based pay Introduce PRP for all
International bank	International growth Enhance customer service Maintain market leadership	Transactional rather than relational approach Incremental scales Pay for jobs not people	Replace incremental scales Introduce contribution-related pay Revise performance management
Care provider, voluntary sector	Growth by improving service delivery Develop new projects Win more contracts	Flexibility Cost of people Competence of people	Competence-related pay Broad-banding

## IMPLEMENTING REWARD STRATEGY

Formulation is easy, implementation is hard. In the UK more attention is now being given to how organizations can make things happen. It is recognized that a pragmatic

approach is required – what’s good is what works. It is also appreciated that implementation presents a massive change management challenge. The practical advice on managing changes in reward systems given by Paul Craven, Compensation Director, R&D, GlaxoSmithKline was: ‘Don’t expect people to change overnight and don’t try to force change. It is better to reinforce desirable behaviour than to attempt to enforce a particular way of doing things.’ The advice given by Nicki Denby, Performance and Reward Director, Diageo was to:

- keep it simple, but simple isn’t easy;
- ensure that the HR department is not developing policies and practices on its own, which are then tagged as just another HR initiative rather than something which is owned by the organization as a whole;
- not only explain the planned changes, the rationale behind them, and how they affect the workforce, but also communicate details of who was involved in the development process so that unnecessary fears are allayed.

Will Astill of B&Q had three pieces of advice on implementation:

1. the value of in-depth employee consultation should never be undervalued;
2. no initiative should be implemented without looking at the return on investment; and
3. evaluate the effectiveness of programmes and take action as required.

## REWARD STRATEGY AND LINE MANAGEMENT CAPABILITY

The trend is to devolve more responsibility for managing reward to line managers. Some will have the ability to respond to the challenge and opportunity; others will be incapable of carrying out this responsibility without close guidance from HR; some may never be able to cope. Managers may not always do what HR expects them to do and if compelled to, they may be half-hearted about it. This puts a tremendous onus on HR and reward specialists to develop line management capability, to initiate processes that can readily be implemented by line managers, to promote understanding by communicating what is happening, why it is happening and how it will affect everyone, to provide guidance and help where required and to provide formal training as necessary.