

Topic: Enterprise Compensation Management Systems

Title: Review of Compensation Schemes and  
Enterprise Compensation Management Systems

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## Executive Summary

The compensation scheme is a key element that organisations have to differentiate themselves as an employer of choice in the competition to attract new employees and retain existing employees. Modern compensation schemes typically include fixed pay and incentive elements, and the balance between these elements makes each organisation's scheme unique. The fixed pay components are typically paid in cash, while the incentive payments can be paid as cash, equity (shares), or a combination of the two. The compensation scheme supports the broad range of Human Resources (HR) practices, such as performance and talent management, which are designed to encourage and reward employee behaviour that is aligned with and supports the organisation's goals.

Despite the significant advances in the functionality and innovation of software, the use of these applications in HR departments is limited, or used to manage in the same old processes rather than as a catalyst to introduce innovation and process improvement. This is especially true of compensation reviews, with many organisations continuing to use spreadsheets or similar low tech solutions to manage the review process, despite the obvious issues and errors that are associated with using such tools. Considering that the review is how the organisation allocates the compensation budget for the following year, budgets that even for medium sized (i.e. 1,000 employees) organisations start in the US\$100's million, the continued use of spreadsheets is concerning.

An alternative to the continued use of spreadsheets are Enterprise Compensation Management Systems (ECMS). This report will review the compensation review process, the elements that comprise modern compensation schemes, the various classes of ECMS tools that are available, and finally a *Best of Breed* ECMS solution.

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# 1. Introduction

## 1.1 Introduction

*Wage and salary administration can be a complex task and at the same time be the Cinderella element of personnel work: lacking in sophistication, strategy, consistency, direction and original thought. Subject to short-term reaction decisions, the management of pay has traditionally seen little innovation. (Smith, 1993, p.45).*

The Hay Group (2009) reported in ***Reward in a Downturn April 2009*** that during periods of economic growth organisations were able to take simplistic approaches to pay, relying on benchmarking and annual increments to determine employee compensation packages. This indicates that despite all the advances in the functionality and innovation within ERP, HRMIS, Performance Management System (PMS) and other HR systems in the intervening years noted by Smith (1993) still applies to many organisations. This situation has been changing as the GFC impacts the financial status of many organisations, causing them to have renewed focus upon their compensation schemes. The result has been that many organisations are realigning their compensation schemes to more directly support the organisations strategic goals, the need to compensate key talent, market comparability and the organisations financial capability to pay (Hay Group, 2009).

The remuneration strategy is one link in a chain of HR initiatives and processes that support each other and the organisation. The interdependence of some of these processes is illustrated in Figure 1, which shows various HR and business activities involved in PMS. While the most obvious link is between performance and reward (remuneration), the linkages to other processes (e.g. business strategy and career development) are no less significant. Parker (2001) found that the structure of the compensation package was critical to the organisation's ability to attract and retain employees, with the package needing the flexibility to cater for local (geographic) variations, while supporting the organisations global objectives. High performance organisations such as Stockland view their compensation package as critical to their ability to recruit and retain employees (N MacDonald, pers. comm. 8 September 2009).

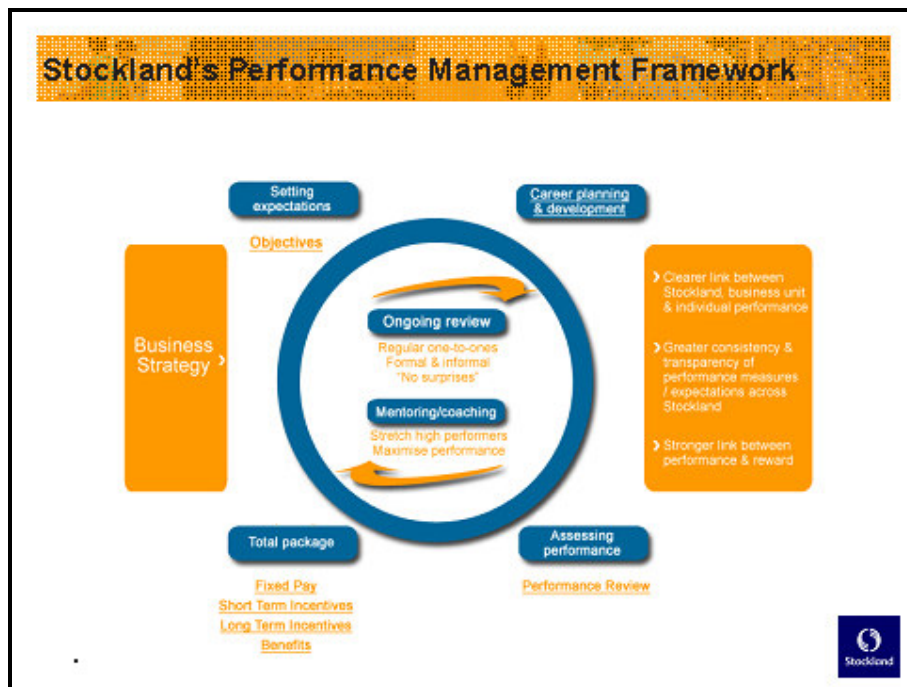


Figure 1: Stockland PMS showing the linkage between strategy, performance and compensation processes within Stockland's PMS (N MacDonald, pers. comm. 8 September 2009).

## 1.2 Compensation Strategy

Compensation strategies, and especially executive compensation strategies, have evolved considerably over time. Prior to the 1990's, compensation was primarily based on fixed pay, with incentive payments being a relatively minor component. Ellerman (2001) noted a trend beginning in early 1990's to implement pay for performance for executives, where the objective was to reduce the fixed component of compensation packages, and increase the incentive (at risk) component of compensation. The incentive components were paid predominantly in equities (stock or shares) rather than cash, thereby linking the value of the executive compensation to the organisations performance and increased shareholder value.

Authors such as Parker (2001) and White (2005) state that compensation packages must support the organisations global objectives, while at the same time being flexible enough to cater for local (geographic) market variations. Figure 2 shows the advantages and disadvantages associated with compensation schemes that have a global (universally applied) and local (unique to each local site) focus. For most

organisations, the optimal solution will lie between the two extremes, and will be unique for each organisation. As stated by Ellerman (2001), once the organisation has selected a compensation strategy, it must be prepared to invest the necessary resources (personnel, time and money) into designing, developing and implementing the compensation scheme consistently across the organisation so that it supports the business strategy.

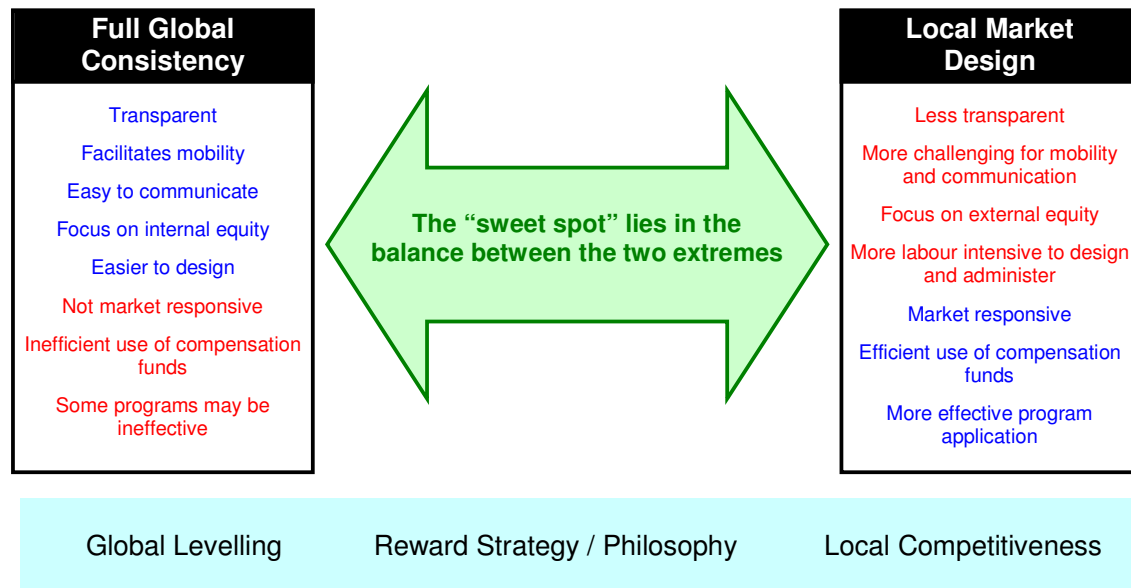


Figure 2: The global consistency spectrum of rewards strategy ranges from organisation mandating consistent application of reward strategy globally, through to the local organisations having ability to design reward scheme to fit local conditions (White, 2005, p.27)

A balanced scheme provides savings in annual compensation by not rewarding under performers, aligns employee behaviour with the organisation goals by providing incentives for, and rewarding employee behaviours that increase organisational performance and shareholder value (White, 2005). Watson Wyatt Worldwide (2006), reported in *Aligning Rewards With the Changing Employment Deal* on the results of survey of 262 US organisations with more than 1,000 employees and found that organisations were increasingly linking pay increases to performance. The increases typically ranged from 0% for employees not meeting performance expectations, 1.5% for employees who partially met expectations, and 5% for employees who exceeded expectations. The report concluded that this shift

in strategy allowed organisations to deliver larger increases to the organisations best performers.

Fuentelsaz et al. (2000) found that compensation schemes can be a indicator of an organisations control system (see Table 1). Organisations that endeavour to control employee behaviours will predominantly exhibit characteristics in the left hand column, while those endeavouring to control results will exhibit characteristics in the right hand column.

| <b>CONTROL OF BEHAVIOUR</b>                      | <b>CONTROL OF RESULTS</b>                                      |
|--|--|
| Fixed remuneration (salary)                      | Variable remuneration (commissions)                            |
| Management supervises behavior more than results | Management supervises results more than behavior               |
| Low span of control                              | High span of control   |
| Significant contact with management              | Limited contact with management                                |
| Performance evaluated subjectively               | Performance evaluated on the basis of a few observable results |
| The firm supports the risk                       | The employee supports the risk                                 |

Table 1: Characteristics of systems that endeavour to control either behaviour or results (Fuentelsaz et al., 2000).

### **1.3 Impact of Global Financial Crisis**

Dillon (2009) noted the significant impact of the GFC upon public perception of organisations compensation schemes, especially executive performance bonuses. In the wake of the GFC, countries such as the US are considering legalisation to increase shareholder say over executive compensation schemes, including approval rights, and establishing stronger link between performance and compensation. In Australia, the Australian federal government commissioned the Productivity Commission to investigate executive remuneration. The draft report was released on 30<sup>th</sup> September 2009, with final report scheduled to be presented to the Federal Government on 19<sup>th</sup> December 2009. As a consequence, the compensation schemes of many organisations are expected to undergo major changes in design and administration in the future.

Another impact of the GFC that was reported (22<sup>nd</sup> October 2009) in mass media (Aversa, 2009) was plans by the US Federal Reserve to review compensation policies of the largest financial institutions in the US. The Federal Reserve Chairman, Ben Bernanke was quoted as saying "Compensation practices at some banking organizations have led to misaligned incentives and excessive risk-taking, contributing to bank losses and financial instability. The Federal Reserve is working to ensure that compensation packages appropriately tie rewards to longer-term performance and do not create undue risk for the firm or the financial system." The plan would give the Federal Reserve the power to veto any compensation schemes that it considers as ill-conceived or inappropriate, with the intent of ensuring that future compensation schemes do not encourage the high risk ventures that contributed to the GFC.

Studies by Ellerman (2001), Bates et al.(2003) and Hay Group (2009) have each noted that during difficult economic times such as the GFC, pay for performance has greater significance for organisations and greater impact upon employee behaviour. The impact of the GFC upon the amount of compensation organisations are currently paying employees has been significant. In survey of 2,000 organisations in 88 countries, the Hay Group (2009) found that 69% of organisations had paid their employees less than their target STI, and 38% of organisations were redesigning their STI bonus schemes. The survey reported similar impact upon LTI bonus schemes as result of the GFC. A specific example of changes wrought by the GFC, UBS AG (UBS, 2009) released a public statement regarding their 2009 compensation detailing significant reductions in discretionary budgets (85%), payments to individual employees (58% to 95%), and the implementation of a new compensation model that is designed to strengthen the alignment of employee interests with shareholders interest.

## 2. The Remuneration Review Cycle

*"The annual salary review process can be very complex and time-consuming, and for many organisations, these reviews are inaccurate, late, or both. Mainstream ERP and HR systems offer a limited toolset to assist with salary reviews." Judges citation, 2007 Consensus Software Awards <http://www.remunerate.com.au/Consensus2007.html>)*

Figure 3 shows the sequence of steps that organisations typically perform in the lead up to the remuneration review cycle. The process starts with the setting of the organisations business plan and performance goals, followed by review of the organisations financial performance and individual employee's performance. The financial performance of the organisation determines the review budgets, while the results of employee performance reviews provide guidance regarding the employee's share of the budgeted pool. ECMS tools are used by line managers to make the actual recommendations before they are approved and uploaded into the master HRMIS or ERP.

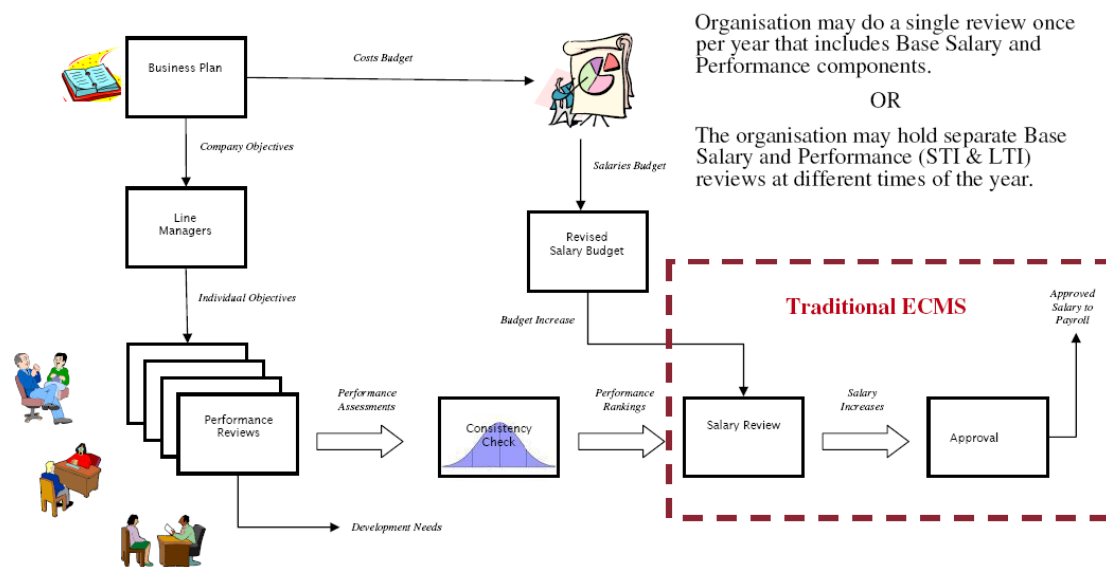


Figure 3: While every organisation has unique elements to their remuneration process, there are certain steps that will be common to many organisations. The red dashed box indicates that functions that are traditionally performed by ECMS tools.

Each organisation will approach the review cycle in a unique manner. Figure 4 illustrates the review cycle that The Boots Company PLC (UK) follows for its remunerations review as of 2002. The figure shows the sequence and timing

between the various steps in the review cycle, starting from the setting of company goals through to reward allocation.

## ROLE MODELS AT EVERY STEP

*The team of performance management champions is involved in every piece of performance management throughout the year*

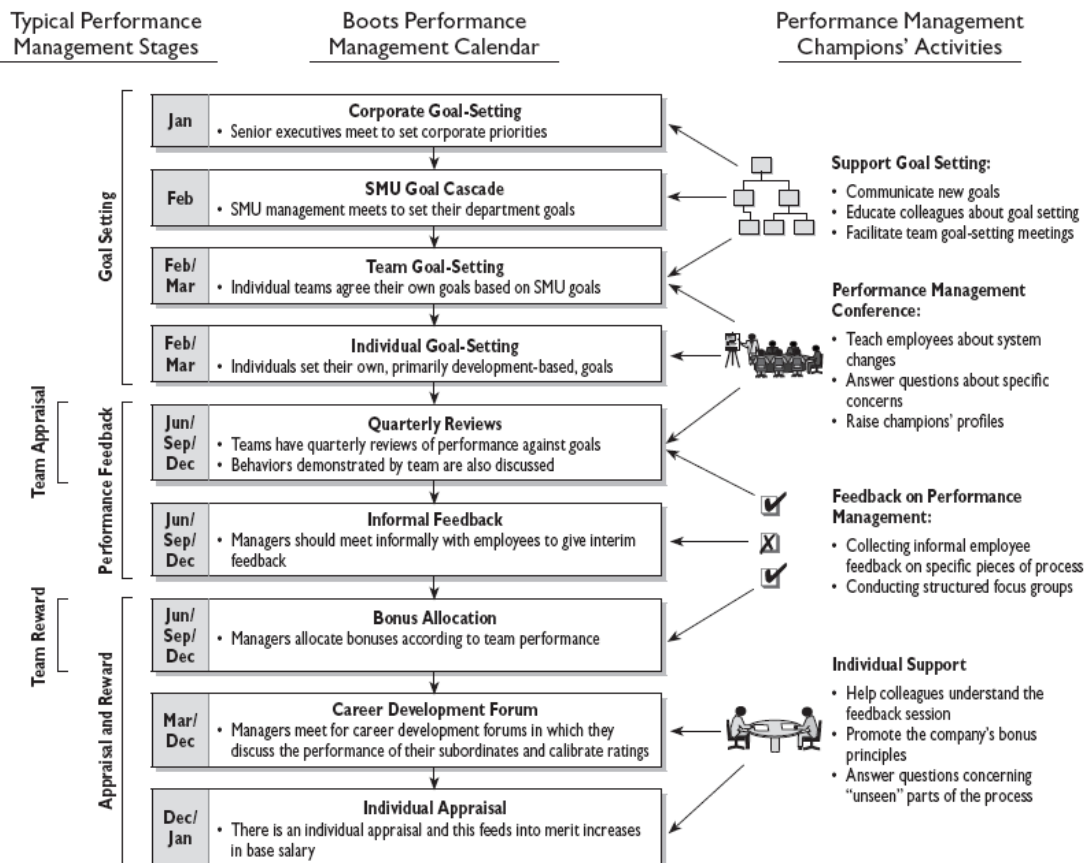


Figure 4: The annual performance cycle for The Boots Company PLC and where reward fits into the cycle (Corporate Leadership Council, 2002, p.21).

While there are steps in the review process that will be common, each organisation will conduct their review in such a manner that makes their review process unique.

Some of these unique features include:

- Conducting the base pay and incentive (bonus) reviews in single (same) review, or as separate reviews.

- Performing the base pay and incentive (bonus) reviews in sequence or in parallel.
- Conducting the performance review (appraisal) and promotions as part of the remuneration review.
- The reviewer and approver workflow.

### 3. Compensation Components

*"A robust performance and remuneration strategy enables alignment of remuneration with employee performance." Debra Lewis, General Manager, HR Operations, Stockland, 9 February 2009*

#### 3.1 Design of Compensation Schemes

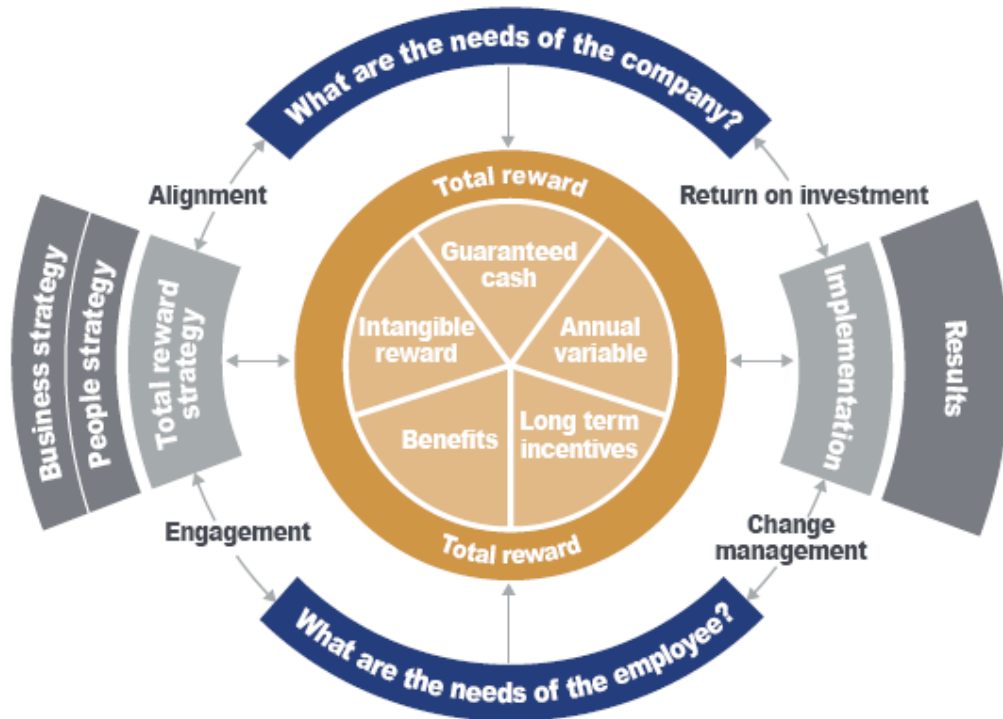


Figure 5: The Hay Group model of total reward management. The intangible rewards are the non financial rewards that employees receive, while benefits are the features such as leave entitlement, flexible working hours, medical insurance, ability to salary sacrifice (McMullen, 2009, p.7).

Like many organisations, Stockland takes a holistic approach to employee compensation package, and frequently refers to it as the total reward process. Figure 5 shows the Hay Group model of for total reward and how it fits into the organisational framework. McMullen (2009) noted that many organisations were redesigning their reward programs to take a more holistic view of reward with greater emphasis upon strategic alignment of compensation (reward) with the organisations goals. HR practitioners such as Neridah MacDonald (2009, pers. comm.8-18 September) have indicated that the base salary must be positioned competitively with

the external market before other elements of the reward package, such as bonuses, or benefits will be viewed positively by the employee.

Figure 6 shows the many components that make up executive remuneration packages, which is consistent with total rewards framework shown previously in Figure 5. Many organisations also make some of these components available to non-executive employees, although the proportions and amount will be significantly different for non-executive employees. The fixed pay is the guaranteed component of the reward package, while the performance based elements are variable and designed encourage and reward employees for superior performance.

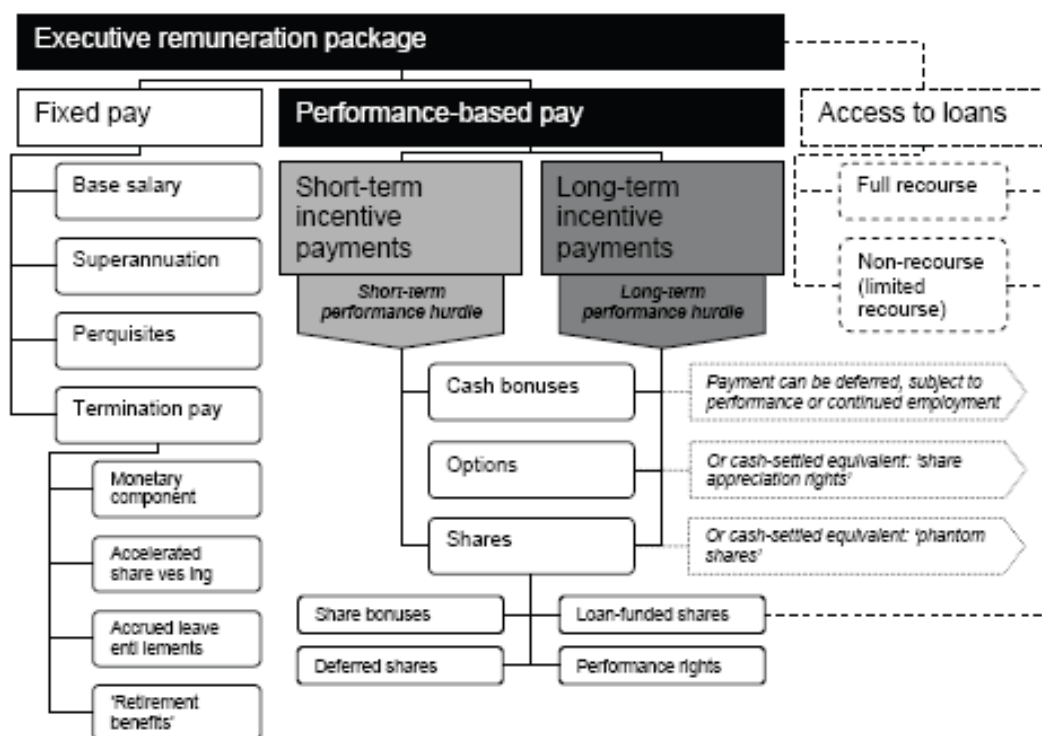


Figure 6: Illustration of the many elements that comprise of executive remuneration packages (Productivity Commission, 2009, p.XXIV). An element that is missing from the figure is the use of allowances as part of fixed pay.

### 3.2 Fixed Pay Components

The many components that make up fixed pay are shown in Figure 6, with the amount being a function of the employee’s experience, ability and role. The Australian Shareholders Association (2009) *Executive Remuneration Policy*

**Statement** stated that fixed pay should be set a level that provides appropriate compensation for adequate performance.

The fixed pay component constitutes the greatest proportion of many organisations total compensation expense. Figure 7 is an illustration of the fixed pay distribution for a *typical* ASX company. As can be seen by the position of the fixed pay median, the greatest proportion of the organisations fixed compensation budget is consumed by the employees in the lower pay bands by virtue of their weight of numbers.

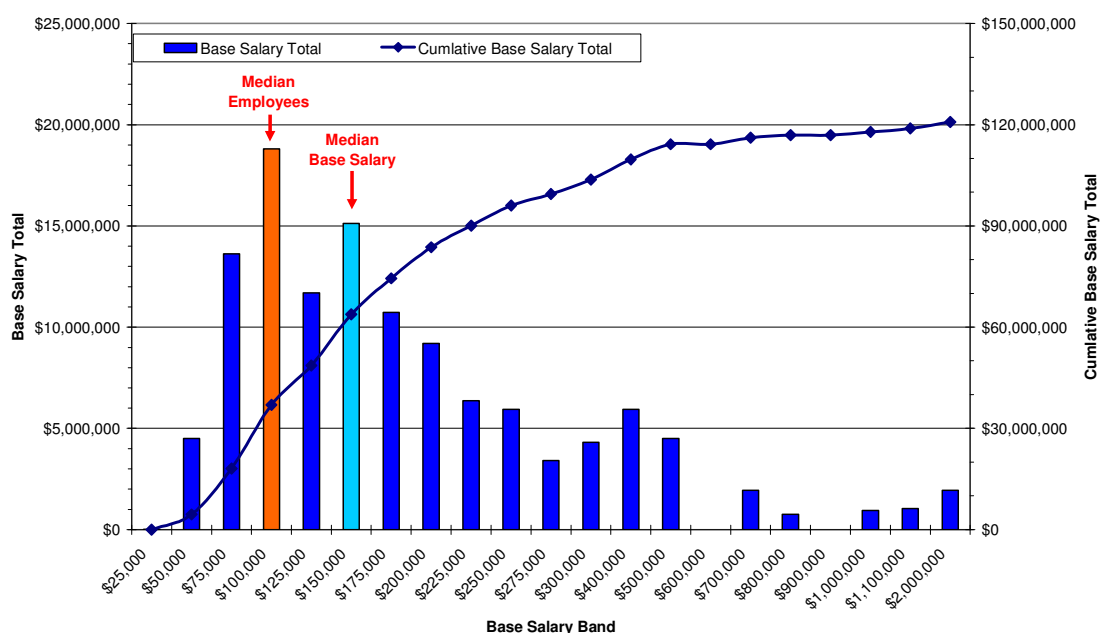


Figure 7: Illustrative example of a typical Base Salary profile for an ASX listed company. Amounts are in Australian dollars (AUD). Note that the salary bands (horizontal axis) are not evenly spaced. Data based upon customers supported by Evanscorp Pty. Ltd and has been normalised to represent an organisation of 1,000 employees. The orange column is the median salary band for employee numbers, while the light blue column is the median base salary band.

### 3.3 Variable Performance Components

The variable or incentive component of compensation is used by organisations to reward employees for individual performance and their contribution to the overall performance of the organisation. The variable components are typically paid as a combination of cash and equity (stocks or shares) allocations with payment dependent upon various individual and organisational performance benchmarks

being achieved. The use of equity is designed to encourage behaviours and results that are consistent with the long term performance of the organisations.

### 3.3.1 SHORT TERM INCENTIVES (STI)

STI's are typically dependent upon performance benchmarks that have a time frame of 12 months or less, and a disproportionate emphasis upon short term results has been implicated as one of the contributing factors to the GFC (section 1.3). While Watson Wyatt Worldwide (2006) found that organisations viewed STI as critical in linking the employee rewards to the organisation's performance, more recently their appropriateness has been questioned by the Australian Shareholders Association, especially in relation to CEO compensation. Guidelines issued by the Australian Shareholders Association (2009) recommend that STI awards should be based on verifiable financial performance metrics at the company level, area of responsibility of the executive, and quantifiable performance indicators that are set at the start of the review period.

Figure 8 is an illustration of the STI distribution for a *typical* ASX company. In comparison to the fixed pay distribution (see Figure 7), the median salary band has risen, and the profile of the cumulative STI is approximating a *linear* trend. All employees are generally eligible for STI payments, with the amount usually set at a percentage of their base salary that increases with seniority or their ability to impact the organisation's performance in the short term. Depending upon the organisations scheme, STI can be paid as cash, equity or combination of both, with thresholds applying to the minimum or maximum amount that may be paid in cash or equity.

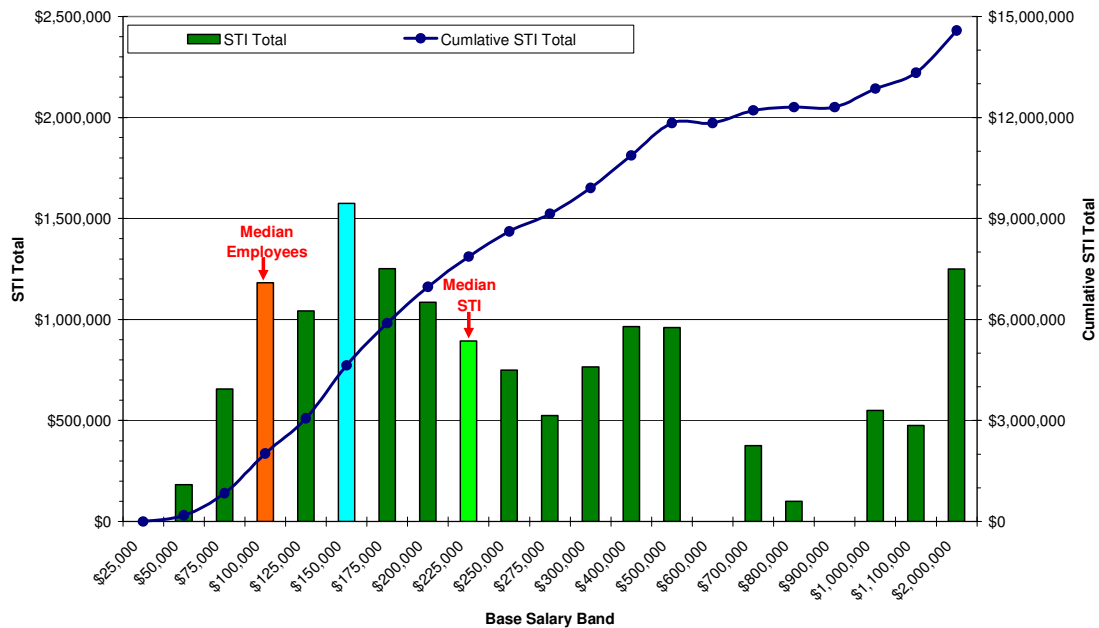


Figure 8: Illustrative example of a typical STI profile for an ASX listed company. Data based upon customers supported by Evanscorp Pty. Ltd and has been normalised to represent an organisation of 1,000 employees, amounts are in Australian dollars (AUD). In this example, the top 100 employees receive approximately half the allocated STI pool. The light green column is the salary band for the median STI.

### 3.3.2 LONG TERM INCENTIVE (LTI)

LTI's are typically dependent upon performance benchmarks that have a time frame greater than 12 months, and a lack of emphasis upon long term performance by organisations has been implicated as one of the contributing factors to the current GFC (section 1.3). The objective of LTI is to encourage behaviours that foster the long term prosperity of the organisation over short term goals, hence LTI's are generally paid in equity rather than cash. The Australian Shareholders Association (2009) views LTI as a important vehicle to reward executives for creating shareholder value and provide incentive to improve the long-term performance of the company.

Figure 9 is an illustration of the LTI distribution for a *typical* ASX company. The median salary band has increased, and the profile of the cumulative LTI is approximately the inverse of the cumulative base salary profile (Figure 7). As with the STI, all employees are usually eligible for LTI allocations, but the amount employees are eligible for will be a function of their ability to impact the organisations

performance at a strategic level in the long term. Hence the top few senior managers and executives receive the bulk of the LTI pool.

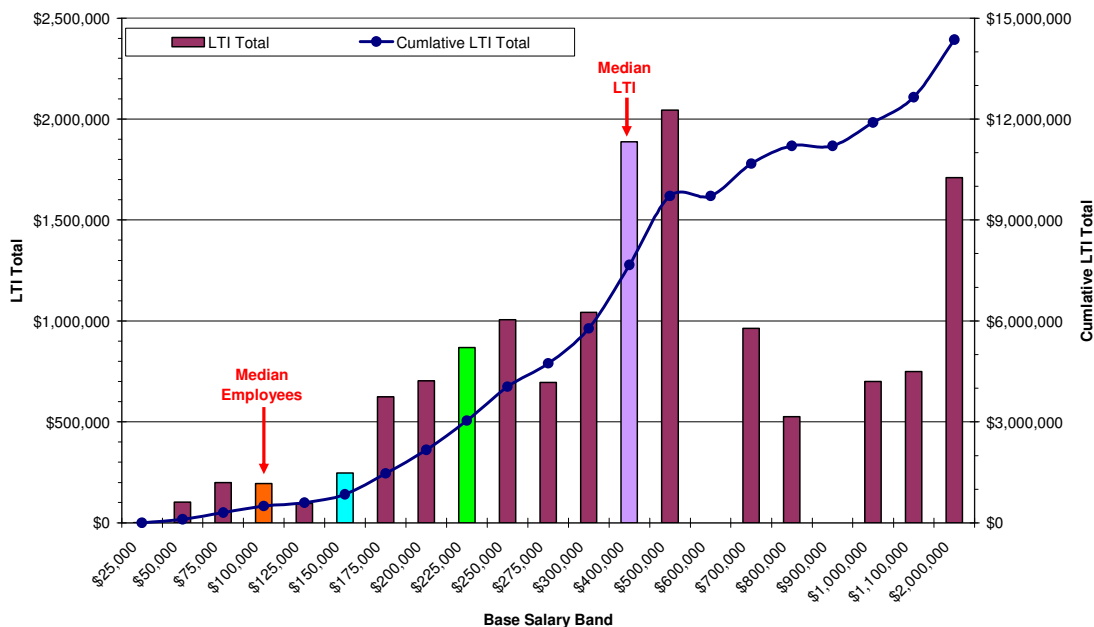


Figure 9: Illustrative example of a typical LTI profile for an ASX listed company. Data based upon customers supported by Evanscorp Pty. Ltd and has been normalised to represent an organisation of 1,000 employees; amounts are in Australian dollars (AUD). The light mauve column is the salary band for median LTI. In this example, the top 20 employees receive approximately half the allocated LTI pool. This figure uses same scale as Figure 8.

### 3.4 Ad-hoc or Lump Sum Components

These are special payments that may be discretionary or mandated which the organisation makes to selected employees. Discretionary payments can be made as recognition for performance beyond normal job requirements, or *topping up* the compensation package of key employees. Mandated payments may be result of a signon guarantee after completion of a probationary period.

### 3.5 Issues with Compensation Schemes

Bates et al. (2003) noted that few organisations manage to get the pay for performance or merit pay schemes right. Ellerman (2001) observed that poorly designed or implemented compensation schemes can produce the opposite effect of the schemes original intent. The role of STI's in precipitating the GFC is an example

of a performance incentive that was meant to improve the organisation's performance, but instead fostered behaviours that ultimately threatened the financial viability of many organisations. Figure 10 illustrates an example of poorly implemented scheme where the employees' performance bonus is dependent upon factors they can not influence, and people that they have no control over. Such schemes can demotivate employees, resulting in them becoming disengaged from the organisation, or leaving the organisation.



Figure 10: Dilbert cartoon regarding compensation (Adams, 2009, 9 July).

The Australian Shareholders Association (2009) position is that performance payments should only be made for superior performance. The perceived failure of organisations to follow this principal, where executive remuneration did not appear to be dependent upon performance was a contributing factor in the Australian Federal Government setting up the current enquiry into executive remuneration.

In an analysis of the use of equity options for incentive pay by US companies, Cahill (2002) found that the use of options had the benefit of instilling a *one organisation* mindset throughout the organisation. However, Cahill (2002) also observed that the simplistic approach of allocating a set number of options to employees regardless of local (country) market conditions which many organisations took meant that they were compensating their non-US executives far more generously than necessary.

A final but critical issue with the compensation reviews is ensuring that line managers are able to effectively manage the pay for performance relationship between

employee and organisation. The line managers must have the necessary training to ensure that they reward top performers appropriately and provide the *tough love* that poor performers require in order to improve performance (McMullen, 2009).

As Foord (2009) observed, the current market volatility presents organisations with a opportunity to redesign their compensation schemes, particularly the incentive components. Performance goals needs to be broadened, and the STI and LTI need to be reviewed both in targets and method of remuneration (i.e. are shares appropriate). The likely outcome of this redesign is that compensation schemes will become increasingly complex, requiring sophisticated ECMS tools that can manage and enforce the link between performance and reward.

## 4. Business Case for Automated ECMS

*“Ironically, companies often lose sight of soft costs, and will invest \$10 or more worth of energy and resources trying to save \$5 in cash.” (Ellerman, 2001, p.27).*

### 4.1 Using Spreadsheets for Compensation Reviews

Spreadsheets have been used by every organisation at some point in the past to perform their compensation reviews, and even today, they remain the most common tool used for compensation reviews. A survey conducted by Varicent (Lan, 2009) found that of 65% of the survey recipients still used spreadsheets, with 90% of those organisations indicating varying levels of dissatisfaction with the review process as a result. If so many organisations are dissatisfied with spreadsheets, it raises the question as to why spreadsheets continue to be used. The answer is highlighted in the above quote, with the internal cost associated with HR resources supporting the existing spreadsheet process not factored into the cost benefit analysis when investigating alternative options.

Organisations such as PwC (C Cook, 2009, pers. comm. 9 February), Stockland (D Lewis, 2009, pers. comm. 9 February) and Lend Lease (C Bingley-Pullin, 2009, pers. comm. 25 February) have reported the following issues when using spreadsheets or similar low tech solutions for managing compensation reviews:

- Ensuring the security of confidential commercial and personnel data.
- Impractical for global organisations needing to review in multiple currencies and report in a corporate base currency.
- Inability to make remuneration changes, promotions and incentive payments at the same time.
- Difficulties in accommodating process or budgetary changes after the spreadsheets have been distributed to managers.
- High administrative overhead for HR to prepare, distribute, collate and analyse spreadsheets, along with following up with managers and monitoring progress.

- Power users who modify the spreadsheet, making the job of merging the completed spreadsheets into a master spreadsheet an extremely difficult and time consuming process.
- Reliance on manual processes to implement multiple levels of workflow authorisation steps, resulting in reviews being conducted over extended periods, and information becoming outdated as a consequence.
- Unable to analyse data during the review to ensure alignment between performance, recommendations and budget until the spreadsheets are returned.
- Difficult to provide management with reports in a timely manner.
- Complexity of generating personalised compensation letters for each employee at the end of the review.
- Support of the review spreadsheet(s) is frequently dependent upon a spreadsheet guru, which represents a significant risk to the organisation if the person were to leave.

While the issues with using spreadsheet are significant, there are circumstances where using spreadsheets for reviews is acceptable. In these circumstances, the previously discussed issues associated with using spreadsheets are manageable, and the organisation will share one or more of the following characteristics.

- Only a few hundred employees.
- Operates in a single or limited number of geographic locations, with employees paid in a single currency.
- Simple compensation scheme, with no requirement for multiple reviewer and approver workflow.
- Organisation has a spreadsheet guru who maintains the spreadsheet and manages the process.

## **4.2 Business Case for an Automated ECMS**

As well as addressing all the previously described issues with using spreadsheets (section 4.1), the business case for automated ECMS must also address the following:

- A) Audit Capability.
- B) Reduce overspend and ensure recommendations (spend) consistent with budget and performance.
- C) Return on investment (ROI).

The following sections will briefly discuss each of these points.

### **4.2.1 AUDIT CAPABILITY**

ECMS must have auditing capability where changes to recommendations are tracked according to who made the changes, when changes occurred, and what changes were made. While this is consistent with general good accounting practices, an audit trail may also be required by regulations such as the US Sarbanes-Oxely Act (2002).

### **4.2.2 RECOMMENDATIONS CONSISTENT WITH BUDGET AND PERFORMANCE**

Many organisations invest significant time and effort into setting review budgets, so an ECMS must be able to provide guidance to managers so that their recommendations are within budget. Similarly a PMS represents a significant investment for an organisation, with the goal of providing incentives for employees to improve performance and reward them for superior performance. Recommendations that are inconsistent with performance can result in budgets being exceeded, the organisation top performers being under paid and poor performers being over paid. The ECMS must be able to provide recommendations to be the managers that are consistent with employee performance, and enforce rules that prevent recommendations that are inconsistent with performance and budgets. Lan (2009) referred to Gartner research that estimated organisation were over paying by around 8% on bonuses and commissions due to manual review processes.

#### 4.2.3 RETURN ON INVESTMENT

As an indication of the potential ROI for a global organisation, White (2005) provided an illustrative example of the costs to an organisation due to ineffective compensation management. White (2005) assumed an organisation of 50,000 employees with average salary of \$50,000 and total annual payroll bill of \$2.5 billion. The estimated annual cost of overpaying employees was \$50 million, while the cost of under paying employees was \$131 million. The cost associated with underpaying employees was principally due to the costs associated with replacing employees who leave the organisation as a result of being under paid.

Apart from the immediate impact of eliminating of calculation errors, reduced overpayment, increase productivity of HR personnel, automated ECMS have a long term benefit in that business rules can be easily modified between review cycles in contrast to spreadsheets that may require significant modification between review cycles (Lan, 2009).

## 5. Automated ECMS

*“... increase in complexity has led to the emergence of a new class of transactional HR tool: enterprise compensation management (ECM) technologies. The aim of such tools is to automate compensation planning and administration.” (Evans, 2009c, p.39)*

ECMS can be broadly categorised as follows:

- A) HR consulting firm solutions.
- B) ERP or HRMIS vendor solutions.
- C) Bespoke solutions.
- D) Best of Breed solutions.

These solutions will be briefly reviewed in the following sections.

### 5.1 HR Consulting Firm Solutions

These are solutions that are provided by firms whose core business is HR consulting rather than software development. These solutions are developed under guidance of HR consultants with a focus on the user interface (presentation) and the current *best practice*. The resultant solution frequently lacks technical sophistication and flexibility to adapt to each organisation's unique requirements without needing to customise the application.

Examples of technical limitations inherent in such applications are the inability to perform reviews in multiple currencies, or dependence upon consultants to perform fundamental tasks such as importing data into the application. Such technical limitations mean that the organisation will be reliant upon the HR consulting firm to perform key steps in the process, or the organisations will need to modify their remuneration process to fit around the applications short comings.

HR consulting firms are typically engaged to assist an organisation to achieve *best HR practices*, and through the process of working with the organisation and improving the organisation's HR practices, the consultants eventually become trusted advisors to the organisation. Once the organisation's HR practices are aligned with

*best HR practice*, the consulting firms ECMS application, which may be a stand alone or part of a *integrated suite* of applications, is offered as *value add* service to the organisation. Once the HR consulting firm becomes a trusted advisor to the organisation, the likelihood that the organisation will conduct an independent review to verify recommendations is reduced.

An example of this was provided during a panel discussion regarding ECMS tools at the IQPC Strategic Remuneration & Reward conference (Sydney 29-30 April 2009). The panel member representing Oz Minerals indicated that they used a HR consulting firm's solution and it was *selected* without having performed a market review of alternative products. While the reasons behind the decision were not given, it was indicated that Oz Minerals had a pre-existing relationship with the consulting firm and it is a reasonable assumption that through this relationship, a level of trust had been established such that Oz Minerals accepted the HR consulting firm's solution without feeling the need to conduct a market comparison. In contrast to this approach, the panel member representing Stockland indicated that their ECMS solution was selected after conducting a evaluation of products that were on the market (A Johnson, 2009, pers. comm. 11 October).

## **5.2 ERP / HRMIS Solutions**

ERP / HRMIS solutions are favoured by IS departments who have already made significant investment in these systems and wish to *leverage* the investment for the organisation. ERP and HRMIS solutions have the following advantages which are outlined in the relevant Oracle (2009) and SAP (2007) product profiles:

- No integration issues, simply *turn on* another module within the existing ERP or HRMIS.
- Solution can be used globally in multiple currencies and converted back to an organisation's base (reporting) currency.
- ERP or HRMIS solutions are backed by global organisations that are continually releasing upgraded versions.

- A large pool of ERP or HRMIS business analysts and programmers available to assist with implementation and support.

However ERP and HRMIS solutions have the following disadvantages which the author has personal experience of:

- Usually only large organisations have the financial resources required for the implementation and the ongoing support.
- Organisations require a large internal IT team for support, or need to outsource the support to a specialist IT business.
- Organisations usually restrict the number and types of users who have access to the ERP or HRMIS. Organisational security or geographical constraints may mean that not all the managers involved in the review process will have access to the system.
- No standard solution exists and every organisation will need to customise the ERP or HRMIS in order to support their organisations unique review processes.
- ERP or HRMIS business analysts and programmers can be expensive resources.
- Upgrading ERP or HRMIS systems are non-trivial and expensive change management projects. With each upgrade all customised code has to be reviewed, rewritten and retested. The cost of the upgrade will be related to the amount of system customisation that has occurred.

The leading ERP vendors are SAP and Oracle, and in comparing the two, Nucleus Research (2005) found that SAP projects were generally larger in scale and scope, and take longer to reach positive ROI. Table 2 shows an analysis of comparative costs of Oracle and SAP's ECMS solutions.

|                           | <b>Oracle Compensation Workbench</b> | <b>SAP Human Capital Management (HCM)</b> |
|---------------------------|--------------------------------------|---|
| <b>Total setup cost</b>   | US\$ 1,563,322                       | US\$ 2,038,333                            |
| <b>Total ongoing cost</b> | US\$ 555,833                         | US\$ 965,833                              |

Table 2: Comparison of Oracle's Compensation Workbench and SAP's Human Capital Management solution based upon Nucleus research (S Goecke, 2009, pers. comm. 26 August).

### 5.3 Bespoke Developments

Bespoke developments can arise due to a variety of reasons, such as *territorial* behavior by IS departments where internal solutions are preferred, or it is more cost effective to develop a bespoke application than modifying the existing ERP or HRMIS. Carefully implemented, bespoke developments have the advantage that they can meet the organisations specific and unique requirements, and the organisation retains full capability to modify the application as required. The disadvantage with bespoke developments is that when review processes or business rules change, the bespoke development has to be modified to accommodate the changes, which may be a non-trivial project.

The Thales Group ([www.thalesgroup.com](http://www.thalesgroup.com)) is an example of an organisation that has chosen to implement a bespoke ECMS application. Previous attempts to customise Thales HRMIS and deliver the functionality to support their remuneration review were unsuccessful. As consequence, Thales performed a cost benefit analysis between the options of further attempting to customise their HRMIS, or developing a bespoke solution. The analysis determined that it would be more cost effective to develop an in-house solution. A second factor in the decision was that Thales is global organisation with a large mobile workforce and not all managers involved in the review process had access (accounts) to the HRMIS, an issue discussed previously in section 5.2. Based upon these factors, Thales commenced development of a bespoke solution by the IS department and driven by the global corporate Compensations & Benefits department (I Bendall, 2009, pers. comm. 9 October).

## 5.4 Best of Breed Solutions

*Best of Breed* solutions are provided by specialist or niche IT firms working in partnership with independent HR professionals and by listening to customer feedback regarding their functionality requirements. This ensures that *Best of Breed* solutions are developed with the underlying architecture that provides the functionality for users to manage the configuration themselves and accommodate changing business processes without the need for customisation of the application or depending upon external consultants to perform key steps.

Organisations such as PwC (C Cook, 2009, pers. comm. 9 February), Stockland (D Lewis, 2009, pers. comm. 9 February), and Lend Lease (C Bingley-Pullin, 2009, pers. comm. 25 February) have implemented a *best of breed* solution and reported the following benefits.

- Ability for users to deploy and configure the system without need for external assistance.
- Ability to support global reviews in multiple currencies.
- Ability to model and implement the organisations desired review and approval workflow process.
- Supports organisations wishing to implement a *performance culture* by ensuring that recommendations are consistent with performance and budgets.
- Intuitive use for system administrators and line managers.
- Web interface accessible to users globally.
- Real time reports allowing HR staff to monitor the progress of each review and ensure that recommendations are consistent with budgets and employee performance.
- Changes to compensation parameters and business rules can be applied mid review without needing to suspend the review to do so.

- HR staff is available to support the users and the process rather than supporting the tools.
- Review managers can easily manage their compensation spend against budget.
- Employee letters can be generated immediately after review is approved.
- Ability to manage multiple reviews concurrently.
- Use of standard security models such as the NIST Role Based Access Control (RBAC) standard for user access.

## 6. Remunerate: Example of a Best of Breed Solution

*"The potential for the software to pay for itself in a very short time, gives Remunerate a compelling edge in the marketplace. The judges commend Evanscorp on developing this elegant solution to a much overlooked problem."*  
Judges citation, 2007 Consensus Software Awards  
<http://www.remunerate.com.au/Consensus2007.html>)

### 6.1 Recognition for Technical Excellence and Innovation

In contrast to other solutions discussed in section 5, the technical excellence and innovation of the Remunerate software has been recognised, being a winner in the 2007 Consensus Software Awards ([www.consensus.com.au](http://www.consensus.com.au)). A key innovation of the Remunerate product is the ability for users to configure the Remunerate application to suit their unique needs. Remunerate does not attempt to replicate any of the *best practice* models may be the current *flavour of the month*. Instead, Remunerate provides the building blocks that allow the user to build, manage and update the solution that fits their organisation. In April 2009, Remunerate was one of a few software products that was included in the Australian Anthill magazine inaugural **Smart 100** list ([anthillonline.com/anthill-magazines-smart-100-2009](http://anthillonline.com/anthill-magazines-smart-100-2009)) of innovative products.

The 2009 HR Technology Conference was held in Chicago (US) on 29<sup>th</sup> September to 2<sup>nd</sup> October and featured key HR technology vendors. A feature of the conference was a technology *shootout*, with SAP, Lawson, Plateau and Salary.com demonstrating their products capability to resolve three HR scenarios, including a compensation distribution scenario. Phillip Evans (2009a, pers. comm. 22 October), attended the conference, advised that in the area of compensation management, the functionality of products featured in the shootout were comparable to the 2004 release of Remunerate.

### 6.2 Remunerate Architecture

The following is summary of the key features of the Remunerate architecture, and the reader is referred to the ***Remunerate Design and Architecture*** (Evans, 2009b) documentation for further details.

### 6.2.1 N-TIER CLIENT / SERVER ARCHITECTURE

Remunerate implements a full n-tier client/server architecture with the client implemented entirely within a browser environment. The client application is a fully functional user interface implemented in JavaScript and Dynamic HTML providing the interactive behaviours more commonly associated with fat-client desktop applications.

All facets of Remunerate have been exposed for easy integration with EAI platforms and other web service technologies through the use of standard web services (SOAP over HTTP/S) for communication between the client and server tiers. Asynchronous JavaScript And Xml (AJAX) has been a recently coined term to describe the architecture that Remunerate has used since its initial release in 2001.

### 6.2.2 PERFORMANCE

From its inception, Remunerate was designed to be used by global organisation and overcome the limitations in network connectivity that is typically present across international boundaries. Remunerate achieves superior performance by caching data extensively in both the server and client tiers to ensure that data is only loaded when it is required. This eliminates unnecessary network interaction, reduces the load on the application server, and eliminates timeout issues that are present in many other applications when user sessions have been inactive.

### 6.2.3 CONFIGURABLE META MODEL

Remunerate unique design allows users to configure Remunerate themselves due to the meta-model and code generation on the server and client. Remunerate uses the following object classes (entities), each of which is end-user extensible using the meta-model definition tools:

**Employee:** Data specific to the employee, such as name, date of birth, hire date, etc.

**Position:** Data specific to the position of the employee, such as position title, current salary details name, supervising manager, work office, etc.

**Hierarchies:** used for structural data, such as the organisations structure, the review hierarchies, office locations (city - state - country – region), etc.

**Position Reviews (or Review Types):** Data related to individual reviews, such as performance rating, recommended salary increases, etc.

**Secondary classes:** Associated with the principal classes are a number of secondary classes which can be attached to the principal classes to create a comprehensive business model.

## 7. Conclusion

The complexity of compensation reviews arises from both the review process (section 2) and the structure of compensation schemes (section 3). Despite the obvious limitations and problems with using spreadsheets and similar low tech solutions (section 4), many organisations continue to do so, while at the same time reporting dissatisfaction with the use of spreadsheets. The continued use of spreadsheets by organisations has a direct financial impact upon the organisation as result of the time that HR resources have to dedicate to the review, and over paying poor performers. More significant though are the indirect costs which are more insidious, since they impact the organisations overall performance through lack of incentive provided to poor performers to improve, previously superior performers becoming disengaged from the organisation and dropping their performance level, or leaving the organisations. When employees leave, the organisations is also faced with the expenses associated with replacing the employee that has left.

As discussed in section 5, there are a range of ECMS solutions that are available to assist organisations improve there review process. HR consulting firm solutions lack the technical sophistication and flexibility that places limitation upon the scenarios that they can address. ERP and HRMIS solutions can usually address the complexity and global issues, however the costs associated with such solutions makes them practical for the large organisations. Bespoke developments can address the organisations unique needs, but they can share some of the costs issues of ERP and HRMIS solutions. *Best of breed* solutions, such as the example discussed in section 6, are an opportunity for HR departments to introduce innovative an ECMS solution and streamline a process that for HR and managers is an extremely labour intensive and error prone process.

## 8. Glossary

| Acronym           | Description  |
|-------------------|--|
| AJAX              | Asynchronous JavaScript And Xml  |
| ASX               | Australian Stock Exchange  |
| CEO               | Chief Executive Officer  |
| EAI               | Enterprise application integration   |
| ECMS              | Enterprise Compensation Management System  |
| ERP               | Enterprise Resource Planning systems such as SAP, PeopleSoft, Oracle or JD Edwards   |
| GFC               | Global Financial Crisis  |
| HR                | Human Resources  |
| HRMIS             | Human resources Information Management Systems, including payroll systems.   |
| HTML              | Hypertext Markup Language  |
| HTTP / HTTPS      | Hypertext Transfer Protocol  |
| IQPC              | International Quality & Productivity Center  |
| IS                | Information Systems  |
| LTI               | Long Term Incentive  |
| NIST              | National Institute of Standards and Technology   |
| PMS               | Performance Management System  |
| ROI               | Return On Investment   |
| Sarbane-Oxley Act | US legalisation enacted in 2002 following corporate collapses (e.g. Enron) as result of questionable accounting practices. |
| SOAP              | Simple Object Access Protocol  |
| STI               | Short Term Incentive   |
| UBS AG            | Union Bank of Switzerland Aktiengesellschaft   |

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