

Reward & Compensation & Incentives: Pay-for-Performance

Human Capital Center Toolbox Series



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What is the PCPS Human Capital Center Toolbox Series?

The Toolbox Series is designed to highlight the learning and tools available in the Human Capital Center (HCC), including templates, action plans, checklists and more. The HCC serves PCPS members by focusing on staffing best practices and providing the resources to master and implement those recommendations. Contributions to the Toolbox Series were made by the AICPA's Specialized Communities, including the Personal Financial Planning, Information Technology, Forensic and Valuation Services and PCPS sections. Visit the 11 segments of the Human Capital Center at pcps.aicpa.org/Resources/Human+Capital+Center/ to discover more.



This tool icon refers to Tools that are available in the PCPS Human Capital Center.

Reward & Compensation & Incentives: Pay-for-Performance

Original content for the Reward, Compensation & Incentives section of the PCPS Human Capital Center was provided by August Aquila and Coral Rice, who are highly regarded consultants to the CPA profession, especially in the area of owner and staff compensation.

Set the Firm's Mission, Vision and Core Values

The first step in designing a compensation plan is to determine your firm's purpose, future and key ideals. Firms that have not completed this step prior to addressing a new compensation model can refer to the Strategy and Planning section of the PCPS Human Capital Center. The firm should also develop a core value evaluation on which to measure adherence to the firm's core values. Refer to the **Core Values Survey Tool** to learn more.

Create the Firm's Strategic Plan

The Strategic Plan document helps all stakeholders understand how the firm will accomplish its mission and vision and who will be responsible for each goal. From here, you can learn how to best pay team members based on performance. For firms that do not have a Strategic Plan, please refer to the Strategy and Planning section.

Develop and Communicate a Firm-Wide Compensation Philosophy

Next it's imperative that the firm's mission, vision and values are reflected in its compensation philosophy. Furthermore, this philosophy must be made available to team members and referred to regularly. The **Sample Compensation Philosophy** will help get you started with this step.

Determine Desired Outcomes of a New Compensation System

An effective compensation plan outlines the newly implemented changes and benefits in the revised compensation system/plan. The following are some of the questions that must be answered affirmatively to ensure a good plan – how does your firm score?

- *Is the system fair?*
- *Have you involved those most affected by the plan?*
- *Does everyone understand how it works?*
- *Does it encourage everyone to do what's best for the clients?*
- *Does it reward for current production as well as future capacity?*
- *Is the compensation system tied to the firm's strategic goals?*
- *Does the system usually provide for predictability in total compensation year-over-year?*
- *Will the system keep the firm alive after the retirement of senior owners?*

In addition, what other outcomes does the firm want from a new or re-designed compensation plan? Review the **Desired Outcomes of New Comp System Template** to help you address these questions and consider outcomes that are important to your firm. Every compensation plan should be constructed to help the firm achieve its strategic goals and to attract, reward and retain the right people. If the plan does not accomplish these two objectives, it needs to be restructured.



Design New Compensation Systems/Plans



Once you have a solid foundation, you're ready to build the actual compensation plan. Remember, today's workers are generally loyal to themselves first and the firm second. Your father's compensation plan won't work today. The present workforce requires a very different kind of compensation plan. While firms will design different plans, there are fundamental principles to which every plan should align. Consider the following:

Establish fundamentals, like who will administer the plan, eligibility requirements, tracking results, etc.

Ensure the plan is win-win-win for each of the three critical stakeholders: clients, employees and shareholders.

Use satisfiers (which attract and retain) and motivators (which drive people to improve performance).

Get owners, employees, or both, involved in the design.

Balance rewards for results and effort.

Identify measures, define targets and track performance. Check out the **Firm Competency Model** and **Core Values Survey Tool** to help measure success.

Create high trust between owners and employees. Low trust can kill a compensation plan.

Avoid side or one-off agreements to prevent different classes of citizens in your firm.

Recommit and re-engage everyone in the first year. If there are problems with the initial design, explore them and make the necessary modifications.

Budget for bonuses. A modest budget for bonuses is advisable. If all owners and staff in a firm achieve their goals, the financial results should be there to support more significant bonuses.

Communicate. Be sure to allocate sufficient time to explain the program, answer questions and allow individuals to see the differences between the current and past plans.

A best practice is to provide team members with a list of Frequently Asked Questions in an effort to address questions, concerns and transparency. Employ the **Sample Frequently Asked Questions Tool** as the foundation for your firm's list of FAQs.

Develop Win-Win Agreements

There is no single compensation plan that works for all firms; therefore, it is necessary to develop an individual firm-based list of compensation criteria. We suggest a list that includes activities that produce results today, as well as activities that will build capacity for producing results tomorrow.

At the beginning of each fiscal year, each staff member, together with his or her manager or owner, should develop agreed-upon individual performance goals that align with the firm's strategic goals – using some type of goal-setting form or template. Not only are goals defined at the beginning of the year, but also measures and targets for success for each goal are defined. The Performance Management section of the PCPS Human Capital Center offers tools and guidance on establishing goals based on a **Firm Competency Model**.

See the **Goal Category Checklists** for sample goals (including measures) and goal categories. Category weightings for the purpose of computing year-end performance ratings vary among firms and

individual people. At the end of the year, use these measures to determine the degree to which the employee or owner has achieved each goal.

There are sample win-win agreements outlining goal categories, goals and measures in the Tools sub section. These agreements can be as simple or complex as desired. We strongly recommend starting with a simple agreement, but note that each firm must develop unique and dynamic win-win agreements based on its firm's vision and strategic initiatives.

The **Sample Partner Win-Win Agreement** includes the following five sections:

Base Compensation

Over time, base compensation should become a lower percentage of total compensation so that more compensation (at least 25% or more) is "at risk" and based on current-year performance.

Core Values

All partners are evaluated by peers and a number of employees on how well they uphold the firm's core values using the **Core Values Survey Tool**.

Objective Performance Criteria

There are hundreds of objective production criteria on which a firm can evaluate individuals and could include personal production, book realization and business development.

Balanced Scorecard

Use this to measure goals that may not have immediate ties to production, like developing new services, mentoring team members, transferring business to another partner, etc.

Discretionary Bonus Allocation

Because not all people contribute equally, this bonus should ideally be allocated based on extraordinary performance and/or a special and unique contribution(s).

Develop and Implement a Transition Plan

Team members must trust the measures and the measurement tools to feel comfortable with the new compensation plan. It is advisable to pay the people based on the old plan, but show them what they would have earned under the new plan. By using this method, you ensure:

- *The new plan creates alignment.*
- *You are able to track measures and provide quarterly reports.*
- *Communication is timely and on target.*
- *You are able to debug any problems.*

After introducing the new plan, meet regularly and often with employees and owners to confirm people understand the system, as well as the actions they must take to meet the stated goals. As you gain experience with the new plan, ask yourself the following questions:

- *Are we seeing the right behaviors from all our team members?*
- *Is our overall productivity improving?*
- *Is owner and employee morale improving?*
- *Are we on track to achieve our goals?*
- *Are we gaining alignment with key stakeholders – employees, clients and owners?*

To assist in communicating the timetable for implementation and to answer questions employees naturally have about the new plan, we have included the **Sample PFP Calendar of Events** and the **Sample Frequently Asked Question** documents, respectively.

Manage Performance

Managing performance is not something done only at year end; workers must know they are being held accountable. They also must hold each other accountable for their performance throughout the year.

Bruce Tulgan, author of *FAST Feedback*, suggests that often the difference between a low-performing team and a high-performing team lies in a coaching-style manager who knows how to keep individual performers focused and motivated day after day. Tulgan believes employees should receive FAST feedback: *Frequent, Accurate, Specific* and *Timely*. These are the four qualities employees most often ascribe to evaluations from “the best manager they ever had,” but also to responses they need but don’t get from most managers. Employees should receive both positive and constructive feedback.

The PCPS Human Capital Center’s Performance Management section offers additional guidance on managing performance. Refer to the *Feedback and Effectively Managing Performance Guide* for specific tips and direction for your team members.

Review the Compensation System/Plan Annually

After implementing a pay-for-performance compensation system, the firm should assess its plan annually to determine whether it is helping the firm meet strategic objectives.

This means analyzing if the firm accomplished the desired outcomes, if people are engaged in necessary behaviors for accomplishing the goals, and if there were flaws in the system/plan that prevented people from doing what needed to be done. Accomplish this analysis by surveying employee satisfaction with the new plan, benchmarking and updating, as necessary.

The **PCPS/TSCPA National MAP Survey** and the **2006 CPA Owner Compensation Survey** can assist you with the benchmarking analysis.



Sample Win-Win Agreement tools are provided to demonstrate examples of how firms can develop their own unique and dynamic individual compensation contracts.

Other Rewards and Recognition

Non-Financial Rewards

Human beings like being recognized and acknowledged for a job well done. Studies show that non-monetary awards can be as meaningful as monetary ones. Consider doing the following:

- *Providing lunch for meeting short-term goals*
- *Closing early on Friday*
- *Sharing gift cards*
- *Awarding “firm dollars” for firm products and/or logo wear*
- *Spotlighting the employee of the month in an internal and/or external newsletter*
- *Providing special parking privileges*
- *Allowing extra paid time off*
- *Hosting firm and/or department outings*



Recognizing Tenure

While pay should not be tied to tenure, recognition should be. Long-term, productive employees are key to every successful business, but especially for accounting firms where client relationships are paramount. A service award based on tenure is a way of saying “thanks” to people who have contributed to the firm’s success. Some examples include a firm pin, gift certificates and individual time with the managing partner at specific intervals.

Remember to make a big deal out of any and all promotions and service awards. These milestones present great opportunities to remind team members that they are part of a family and that the firm is interested in everyone’s personal growth. Building a sense of family and appreciation is an invaluable retention tool for any size firm.

Speaking of retention, visit the **PCPS Top Talent Study** booklet and the **Employee Retention Guide** to gather additional incentive ideas and best practices.

Following the above ten steps can lead you and your firm to a successful pay-for-performance program that will better enable you to attract and retain the best and brightest in the profession.

NOTE: The book *Compensation as a Strategic Asset: A New Paradigm* was also written by August Aquila and Coral Rice. It is an impressive guidebook to navigating the tricky subject of partner compensation. As your firm progresses through the journey of implementing a pay-for-performance program, you might want to refer to this valuable tool. PCPS members can receive a discount when purchasing *Compensation as a Strategic Asset*.

Visit aicpa.org/PCPS and become a member today. You’ll enjoy access to an array of tools and resources related to staffing and compensation issues. To find out if your firm is already a member, email pcps@aicpa.org.

Access These Tools At aicpa.org/PCPS

Core Values Survey Tool

Sample Compensation Philosophy

Desired Outcomes of New Comp System Template

Sample Frequently Asked Questions

Goal Category Checklists

Sample Partner Win-Win Agreement

Sample Manager Win-Win Agreement

Sample PFP Calendar of Events

2006 Owner Compensation Survey



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