Collin County Compensation

Total Rewards Philosophy

Compensation is one of the five key components in a successful Total Rewards program.

Objectives of Compensation
and Total Rewards

Compensation programs must be periodically evaluated to maintain a favorable Total Rewards value proposition which will:

1. **Attract** the right talent at the right time.

2. **Motivate/Engage** employees to perform at high levels of effort and commitment.

3. **Retain** employees who are valuable contributors to Collin County’s success.

This presentation will provide information regarding the county compensation program for consideration by Commissioners Court.

Recent Compensation Changes

A general evaluation of our compensation program was conducted by Korn Ferry Hay Group (Summer 2016).

Several changes have already been implemented as a result of their recommendations:

- Increased spot bonus (GEM awards) from $50 to $250*
- Expanded data collection for annual survey and targeting market median instead of average when possible
  - In process of gathering data for 2017 analysis
- Hot jobs process as outlined by consultant may be utilized on an as needed basis
- Increased PFP maximum to 2x average increase
  - i.e. if PFP budget is 3%, maximum possible increase for top performer with a perfect score would be 6% (ability to reach 6% depends on department average and how scores are distributed).

*After tax

Areas of Consideration

- Discussion of a guiding compensation philosophy.
- Policy change to enhance the effectiveness of current compensation programs.
- Options for calculating annual increases.
- Establish a consistent, data-based method of determining changes to compensation.
- Options for distributing pay changes.

Compensation Philosophy

Compensation Philosophy

The following components are being presented as possibilities for including in a guiding compensation philosophy.

1. Collin County utilizes a data-based, market driven compensation philosophy.

2. We will strive to meet the needs of our County's residents by attracting, retaining and motivating talented employees who can provide the best services possible.

3. Compensation policies, pay structure and total rewards decisions will reflect the need to balance our goal of retaining top talent with responsible use of taxpayer funds.

4. It is our objective to establish a strong tie between performance and rewards, and ensure top performers are rewarded for their efforts.

Policy Change

Promotion Policy

A change to our promotion policy was suggested by the Hay Group consultant.

The objective of this change is to provide a salary increase that reflects the significance of a promotion.

- A promotion to a job that is one pay grade up is a smaller change in responsibility than promoting to a job that is three pay grades up.

Detailed below is our current policy and an option.

- **Current policy:** Increase employee's salary by 5% or amount needed to bring them to pay grade minimum, whichever is greater.

- **Change policy:** Calculated by increasing the employee's current salary by 5% for ***each pay grade they move up*** with a maximum increase of 15% (or pay grade minimum, whichever is greater).

		Current		Option	
Grade	**Grade Min**	**$ after promotion**	**%**	**$ after promotion**	**%**
Current grade 530	-	33,000 – current rate		33,000 – current rate	
531	30,297	34,650	5%	34,650	5%
532	32,652	34,650	5%	36,300	10%
533	35,314	35,314	7%	37,950	15%
534	38,276	38,276	16%	38,276	16%

Demotion Policy

A corresponding demotion policy change may be warranted.

Current policy:

- Maintain current policy: Calculated by decreasing the employee's current salary by 5% or to maximum of pay range (whichever decrease % is greater) **OR** decreasing to previous salary if returning to previous pay grade within one year (accounting for any pay increases which have occurred).

Option 1:

- Calculated by decreasing the employee's current salary by 5% or to maximum of pay range (whichever decrease % is greater) **OR** decreasing to previous salary if returning to previous pay grade within **two years** (accounting for any pay increases which have occurred).

Option 2:

- Calculated by decreasing the employee's current salary by 5% ***for each pay grade they move down*** (with a decrease limit of 15%) or to the maximum of new pay range (whichever decrease % is greater) **OR** decreasing to previous salary if returning to previous pay grade within **two years** (accounting for any pay increases which have occurred).

		Current / Option 1		Option 2	
Grade	**Grade Max**	**$ after demotion**	**% change**	**$ after demotion**	**% change**
Current grade 534	-	45,000 – current rate		45,000 – current rate	
533	48,891	42,750	-5%	42,750	-5%
532	45,216	42,750	-5%	40,500	-10%
531	41,975	41,975	-7%	38,250	-15%
530	39,010	39,010	-9%	38,250	-15%

Annual Pay Changes

Annual Pay Change Calculation

Options for consideration:

1. Merit matrix method.
2. Continue current pay calculation.
3. Modification of pay calculation.

Performance Calculation
Option 1 - Merit Matrix

Merit Matrix

	Position in Range (relative to mid-point)		
Rating	**Min - 90%**	**90% - 100%**	**>100%**
Below Expectations	0%	0%	0%
Department Average (+/- 10%)	4%	3%	2%
Above Expectations	6%	5%	4%

- This method combines performance ratings with position-in-range to determine each individual's annual increase.
- Suggested by compensation consultant - intention was to help move employees to midpoint more quickly and reduce the effects of compression, while also taking into account their performance rating.
- Research based on actual Collin County employee data shows that this method does not sufficiently reward performance at varying levels to justify adopting a matrix.
- We have not been able to identify other organizations using a merit matrix.
  - Surveyed other cities and counties.
  - Followed up with consultant who was unable to provide any organizations currently using a matrix similar to the one they recommended.

Merit Matrix Issue 1
Decreased Link to Performance

While a merit matrix offers a link to position-in-range, the tradeoff is a decreased link between employee performance and individual reward.

This occurs in two ways:

1. The message that performance and rewards are linked is diluted when a group of employees with varying levels of performance receive the same percentage increase.

    - A department could have 10 employees who fall into the “Strong Performance” category, while their actual performance scores vary between 8.4 and 9.9.
    - Under a merit matrix, all these employees would receive the same percent increase, despite the clear differences in performance.
    - The current model accounts for all degrees of performance differences and distributes rewards accordingly.

Merit Matrix Issue 1
Decreased Link to Performance

2. Under a merit matrix, those who are above pay grade midpoint receive **significantly** lower increases, even with superior performance.
    - For example, a department whose top performer is above midpoint receives a 5% increase, while the second highest performer (who is below midpoint) receives a 7% increase.

- The decreased link to individual reward for performance is demotivating to high performers.
- It also provides little motivation for lower performers to improve, as they would have to reach a very high level to see any change in their reward.

Merit Matrix Issue 2
Complexity of Program

The consultant's recommended solution is significantly more complex than the current program.

- **Current program** – PFP score correlates to the employee's performance ranking, which translates to annual increase %.
- **Matrix program** – PFP score gets an employee assigned to a rating group.
  - Rating groups are based on scores that are either above, below, or within standard deviation from the department average.
  - Employees are then assigned to a position-in-range group based on their relationship to midpoint. (may be above/below, or may be determined based on % of midpoint).
- The increased complexity will result in decreased employee understanding.
- Significant training and communication would be needed to help employees understand the new method of calculating increases.
- Danger of significant decline in morale and work productivity if employees do not understand the program.

Performance Calculation
Option 2 – Current Pay Calculation

Continue utilizing current pay calculation.

Advantages:

- Established process, would require no additional training or new communications.

Points for consideration:

- Utilization of Self Appraisal in the increase calculation has resulted in significant pushback from employees on all levels. The need to justify their ratings and comments has resulted in a feeling of employees being unable to represent their performance as *they* see it.
- Current calculation limits distribution of funds by department, which means some funds may be unavailable if positions are vacant.

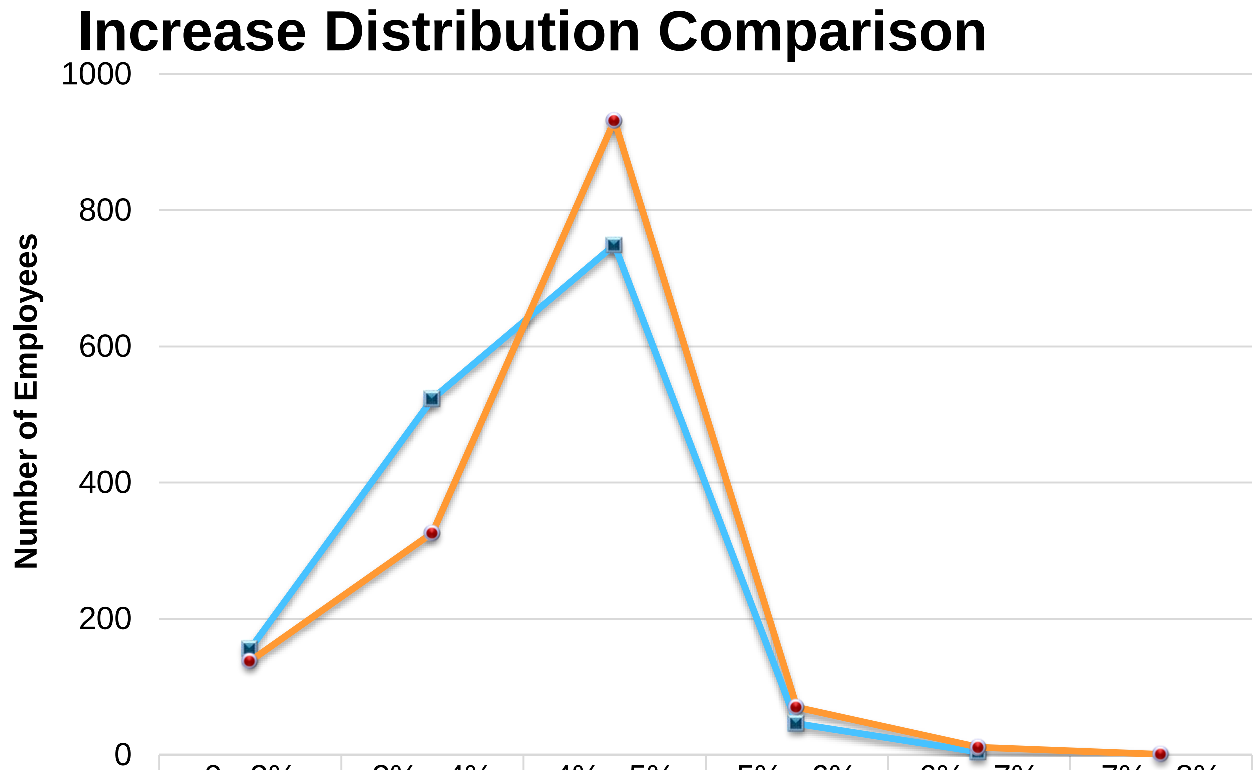
Performance Calculation
Option 3 – Modify Pay Calculation

Options to modify pay calculation include:

1. Remove Self Appraisal from the score and pay calculation.
   - Continue Self Appraisal for use between managers and employees with very little HR intervention in the process.
   - Removing Self Appraisal from calculation allows employees to fully voice their perception of their performance and removes impact on department scoring.
2. Distribute all available funds amongst entire employee population by ranking employees based on entire employee population rather than by department.
   - Merging all departments together provides additional funding for high performers, but increases complexity and may result in reduced employee understanding.

PFP Calculations
Distribution Comparison

The table and graph below compares actual distribution of increase funds (4% total) from performance year 2016 to a simulation of the same year using a modified calculation that distributes all funds in a calculation that merges all departments.



	0 - 3%	3% - 4%	4% - 5%	5% - 6%	6% - 7%	7% - 8%
Current Calculation	156	523	749	46	4	
Modified Calculation	138	326	932	70	11	1

Determining Annual Compensation Funding

Annual Compensation Funding

Historical Methodologies:

1. **Projected average salary increase budget**
   - Provides a general idea of what most organizations will budget for increases.
   - Affects current employees and the degree to which performance is rewarded.
2. **Projected market range movement**
   - Provides a general idea of what most organizations will budget for the change in their pay ranges.
   - When pay ranges move as a result of market wage movement, most organizations apply market adjustments to existing employee salaries.
3. **Available funds not used in previous year.**
   - Provides the amount of funds available for reinvestment in employee salaries.
4. **Aggregate mid-point vs actual pay ratio**
   - Serves as “measuring stick” for County’s objective of compensating at market midpoint.
5. **Individual compa-ratios**
   - Provides insight on individual salary relationships to market midpoint.
6. **Consumer Price Index**
   - Provides changes in the cost of consumer goods and services.

Methodology 1
Projected Salary Increase Budgets

- Salary increase budget projections are useful in ensuring Collin County’s performance increase decisions are aligned with general market conditions.
- Sources for this information include:
  - World at Work Salary Budget Survey – industry “gold standard” for compensation.
  - Annual surveys conducted by HR staff
    - Comparable entities are often working on budget at the same time and may not always be able to provide information.

Methodology 2
Market Range Movement

Collin County has a successful and efficient method of maintaining pay scales by applying market range increases.

- Prior to 2009, we also applied these increases to individual employee pay.
  - When the recession occurred, this was discontinued in an effort by Commissioners' Court to maintain a level budget and display fiscal responsibility during the 2009 financial downturn.

Comparable Public Entities

A recent HR survey asked comparable public entities if they applied market adjustments to employee salaries (in addition to pay ranges).

- 6 out of 7 respondents perform annual market pay adjustments in addition to their annual step, performance, merit or across-the-board increase.

Compensation Industry Survey

World at Work's most recent salary budget survey (largely private sector) asked whether salary increases based on market adjustments had been utilized in the past 12 months.

- 76% of respondents indicated their company had utilized this compensation strategy.

Methodology 2 - Market Range Movement

Market Adjustments Applied to Wages

Why is this strategy so widely used?

- Budgeting for both performance-based increases and market wage movement allows an organization to:
  - Avoid wage compression issues.
  - Ensure employees’ earned performance increases are not diminished by market wage movement.
  - Provides a sense of equity when comparing new hires against longer term employees.

Why is preventing compression and stilted wage growth important?

- Changing job market
  - Unemployment is nearly half the rate it was in 2010.
  - Greater competition for talent.
  - Already seeing a reduced number of applications per position in some areas.
- Millennials have surpassed Baby Boomers in the workforce.
  - By 2030, they will make up 75% of the work force.
  - Average tenure at a company is 2 years.
  - Willing to move on if they do not feel their current job allows them to grow both financially and professionally.

Methodology 2 - Market Range Movement

Performance Adjustments vs. Market Adjustments

What is the Difference?

- Market range movement adjustments have a separate function from pay for performance adjustments.

Performance Adjustments	
<u>Objective:</u> ***Motivate*** employees to perform well by tying the quality of their performance to the size of their PFP increase.	<u>Answers the question:</u> How much of an increase has this employee earned based on their performance?

Market Adjustments	
<u>Objective:</u> **Attract** new employees by keeping pay ranges current with market. ***Retain*** current employees by ensuring their earned performance increases are not diminished by wage compression.	<u>Answers the question:</u> How much of an increase is needed to keep this employee aligned with market?

- Market adjustments are not a step program.
- Performance and market adjustments can be distributed simultaneously through the PFP calculation or separately.

Methodology 2 - Market Range Movement

Relative Increase Amount

- **Relative Increase Amount** is the gain an employee makes on their market pay comparison.
  - Ex: Jane receives a 5% PFP increase. Range movement for her pay grade is 3%.
    - Jane's relative increase is calculated as: 5% - 3% = 2%.
    - While Jane's gross increase was 5%, she only gained 2% against market.

- **Time to Midpoint//Maximum**
  - There is no set industry standard for this number, but in general companies use somewhere between 10 – 20 years to reach pay range maximum.
  - In 2001, a consulting service hired by the County recommended 12 years to reach maximum.
  - The chart below illustrates the number of years it is projected to take an actual **new hire** to reach the midpoint and maximum of their grade when market adjustments are not done with performance adjustments.

Historical Pay Illustration

- The table below shows pay changes of an employee with strong performance ratings (2's) when budgeting for Performance Only increases as compared to a consolidated method. (Uses actual historical pay range movement and performance increase data.)
- In this example, the employee still has not reached midpoint of their pay range after 10 years under a performance only method.
  - Midpoint would have been reached after 7 years under a consolidated method.

Performance Year	Midpoints	Historical Pay Changes	Consolidated Pay Adjustments	Difference
2006 (hired)	$38,001	$31,574	$31,574	-
2007	$38,381	$33,468	$33,784	(316)
2008	$39,343	$34,639	$35,811	(1,171)
2009	$39,737	$35,332	$36,885	(1,553)
2010	$39,737	$36,039	$37,623	(1,584)
2011	$39,737	$37,120	$38,751	(1,631)
2012	$39,737	$37,862	$39,527	(1,664)
2013	$40,928	$38,998	**$41,898**	(2,900)
2014	$40,928	$40,168	$43,155	(2,987)
2015	$42,361	$41,373	$45,960	(4,587)
2016	$43,632	$43,028	$49,177	(6,149)

Historical pay changes are based on approved performance increases and pay range adjustments and their impact on an average employee's pay.

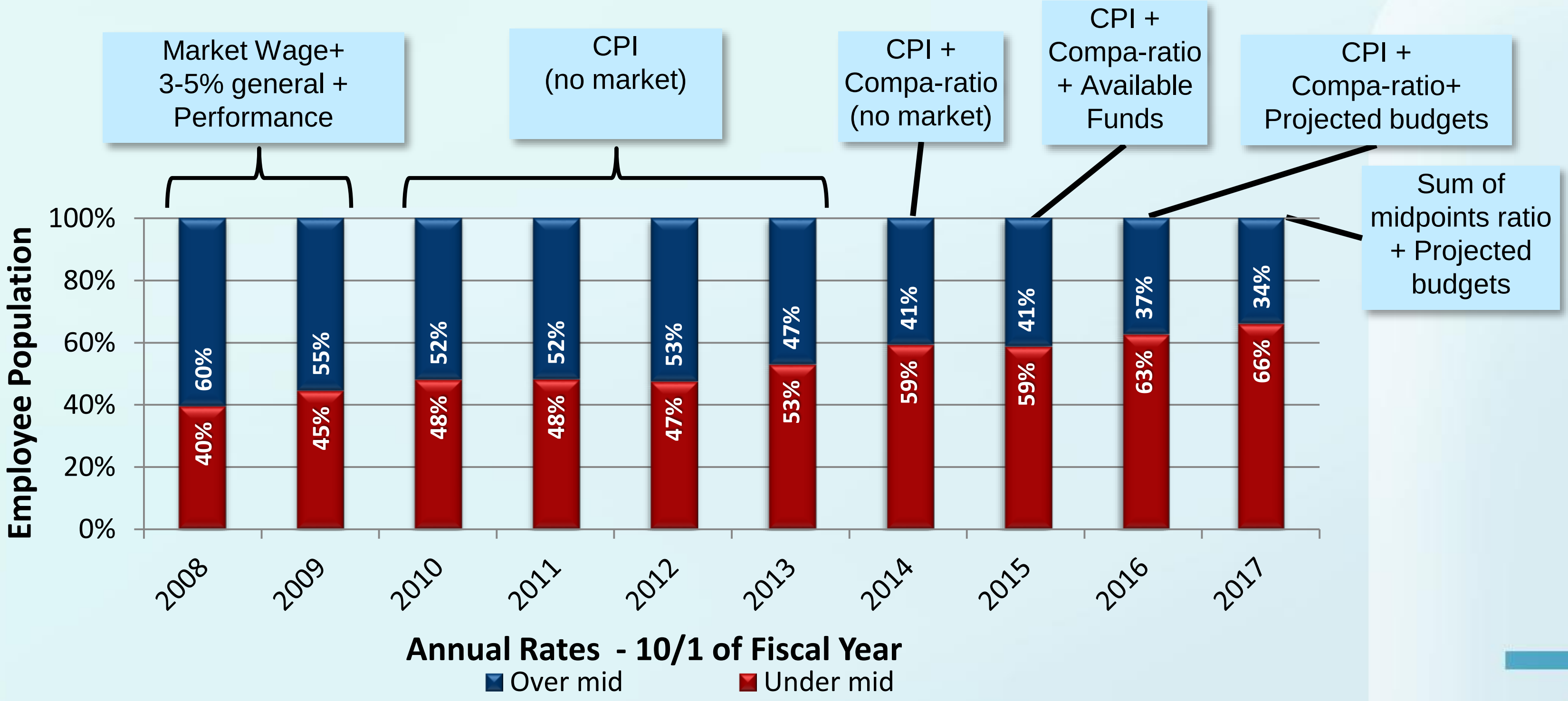
Methodology 3
Available funds not used in previous year

- This calculation provides the amount of funds which were budgeted, but unused in the previous year.
- This would reinvest unused funds into employee pay increases.
- Generally a nominal amount of less than 1%.

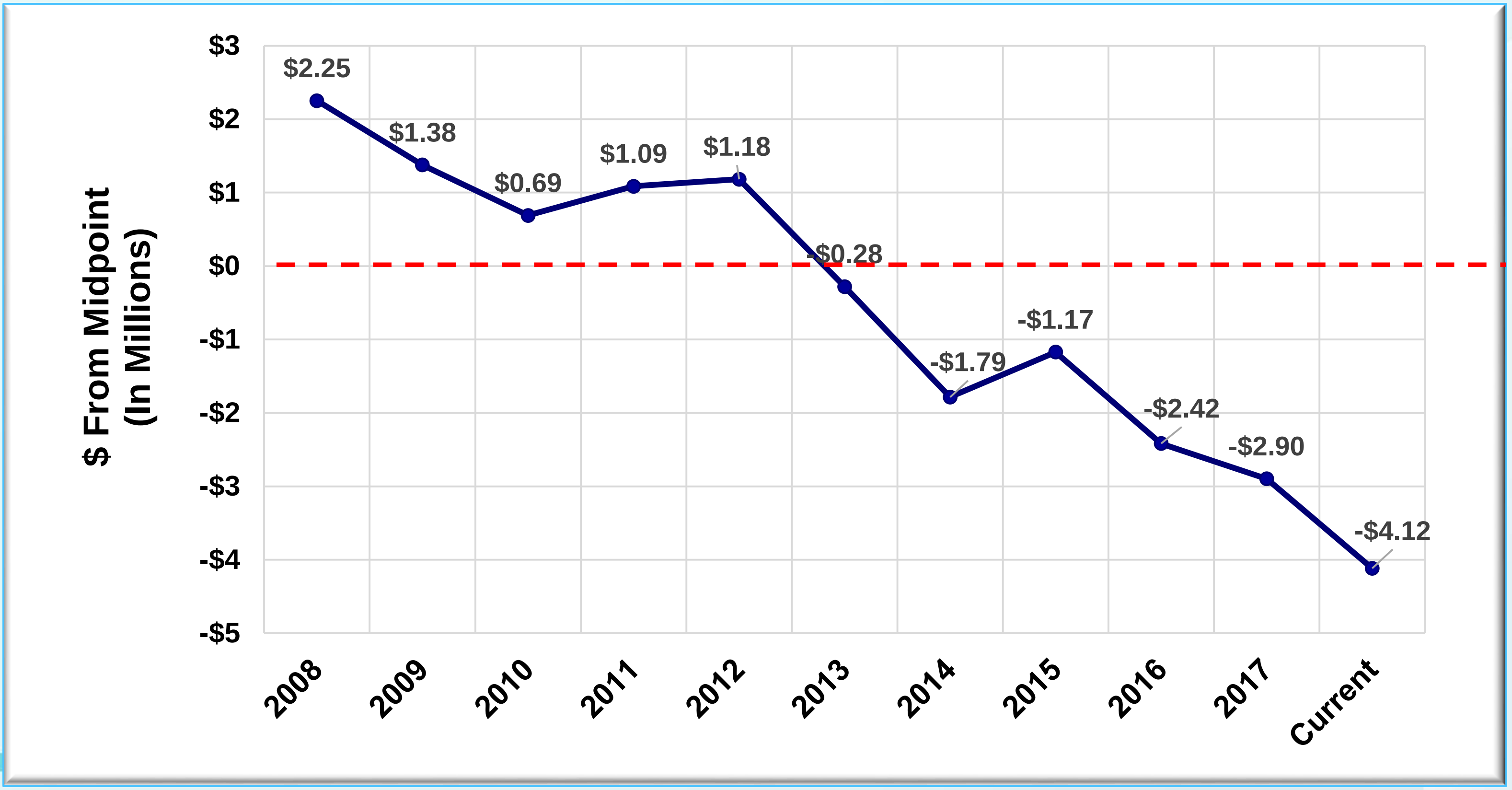
Methodology 4
Sum of Midpoints to Sum of Actuals

This strategy was offered by the Hay Group consultant as a means of seeing how close to market our actual pay is (goal is to be near 0% variance.)

Changes over time can be seen – these correspond to changes in philosophy for evaluating annual increase funding.



Methodology 4
Actuals to Sum of Midpoints



Methodology 4
Sum of Midpoints to Sum of Actuals Ratio

Factors in changes to Midpoints to Actuals ratio (whether favorable of unfavorable) include:

- Wage compression
  - Wage compression occurs when market wage movement outpaces annual increase funding (and/or when there is an absence of market pay adjustment on an individual level).
  - This results in an unfavorable ratio of employees under target pay (midpoint) vs over target pay.
- Changes to employee demographics.
  - In years with more retirements or turnover of long term employees, you may see a lower number, which reflects new hires coming in under midpoint to replace employees who were above midpoint.
- Reclassifications
  - Moving a position to a higher pay grade will cause individuals to be lower in the new pay grade than the previous pay grade, which decreases the Midpoints to Actuals ratio.
  - Conversely, moving a position to a lower pay grade will cause individuals to be higher in the new pay grade, which will inflate the ratio.

Methodology 5
Individual Compa-ratios

- Individual compa-ratios compare midpoint to actual salary on a case by case basis.
- This was utilized in FY 2014, 2015 and 2016.
  - Provides a short-term solution to wage compression.

Methodology 6
Consumer Price Index

- The Consumer Price Index (CPI) reflects changes in the prices paid by consumers for goods and services.
  - Used between 2009 – 2016 as a data point in salary budget discussion.
  - According to the consultant who analyzed our compensation practices last year, using CPI to guide pay increase budgets is the leading cause of wage compression.
  - The market for pricing goods and services does not correlate to the market for pricing jobs. (i.e. goods and services may move by 1%, but wages move by 3%).

Distributing Funds

Distributing Funds

Distribution method options:

1. Distribute both performance and market adjustment funds through the PFP calculation. (all merit based distribution)

2. Distribute performance funds through PFP calculation and market adjustment funds based on a flat percent. (blend of merit based and universal distribution)

Timing options:

1. Apply performance and market adjustments to employee salaries at a single point in the year.
   - (Ex: PFP increases and market adjustments in October)

2. Apply at separate times of the year.
   - (Ex: PFP increases in October and market adjustments in January)

Summary

Compensation Philosophy

Define compensation philosophy

Select each statement to be included.

- ☐ 1. Collin County utilizes a data-based, market driven compensation philosophy.
- ☐ 2. We will strive to meet the needs of our County's residents by attracting, retaining and motivating talented employees who can provide the best services possible.
- ☐ 3. Compensation policies, pay structure and total rewards decisions will reflect the need to balance our goal of retaining top talent with the responsible use of taxpayer funds.
- ☐ 4. It is our objective to establish a strong tie between performance and rewards, and ensure top performers are rewarded for their efforts.
- ☐ 5.

Summary

Promotion & Demotion Policy

Promotion policy

Select one of the options listed below.

- ☐ 1. Continue with current policy - 5% increase***** regardless of pay grades moved. (current policy)
- ☐ 2. Modify policy - 5% per pay grade increase, with a maximum increase of 15%.*****

*or amount needed to reach pay grade minimum

Demotion policy

Select one of the options listed below.

- ☐ 1. Continue with current demotion policy - 5% decrease.** If occurring within 1 year of promotion, return to previous rate (adjusted for PFP/market increases).
- ☐ 2. Modify policy - If occurring within 2 years of a promotion, return to previous rate** (adjusted for PFP/market increases).
- ☐ 3. Modify policy – decrease pay by 5% per pay grade, with a maximum decrease of 15%** OR if occurring within 2 years of a promotion, return to previous rate** (adjusted for PFP/market increases).

**or amount needed to come down to maximum.

Summary

Increase Funding, Distribution and Calculation

<u>Increase funding data</u>

Select each data point to include.

- ☐ 1. Projected average salary increase budgets in market.
- ☐ 2. Projected market wage movement.
- ☐ 3. Available funds not used in previous year.
- ☐ 4. Aggregate midpoint vs actual pay ratio.
- ☐ 5. Individual compa-ratios.
- ☐ 6. Consumer Price Index.

<u>Distributing funds</u>

Method:

Select one of the options listed below.

- ☐ 1. Distribute both performance and market adjustment funds through the PFP calculation.
- ☐ 2. Distribute performance funds through PFP calculation and market adjustment funds based on a flat percent.

Timing:

- ☐ 1. Apply performance and market adjustments to employee salaries at a single point in the year.
- ☐ 2. Apply at separate times of the year.

<u>Increase calculation</u>

Select one of the options listed below.

- ☐ 1. Utilize Merit Matrix (not recommended)
- ☐ 2. Continue with current PFP calculation
- ☐ 3. Utilize modified PFP calculation with one or both of the following:
  - ☐ Eliminate self-appraisal in calculation. Continue for documentation purposes only. (recommended)
  - ☐ Distribute funds among entire county (rather than by department)

Summary of Options

Define compensation philosophy

Select each statement to include.

- ☐ 1. Collin County utilizes a data-based, market driven compensation philosophy.
- ☐ 2. We will strive to meet the needs of our County's residents by attracting, retaining and motivating talented employees who can provide the best services possible.
- ☐ 3. Compensation policies, pay structure and total rewards decisions will reflect the need to balance our goal of retaining top talent with the responsible use of taxpayer funds.
- ☐ 4. It is our objective to establish a strong tie between performance and rewards, and ensure top performers are rewarded for their efforts.
- ☐ 5.

Promotion policy

Select one of the options listed below.

- ☐ 1. Continue with current policy - 5% increase***** regardless of pay grades moved. (current policy)
- ☐ 2. Modify policy - 5% per pay grade increase, with a maximum increase of 15%.*****

*or amount needed to reach pay grade minimum

Demotion policy

Select one of the options listed below.

- ☐ 1. Continue with current demotion policy - 5% decrease.** If occurring within 1 year of promotion, return to previous rate (adjusted for PFP/market increases).
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- ☐ 3. Modify policy – decrease pay by 5% per pay grade, with a maximum decrease of 15%** OR if occurring within 2 years of a promotion, return to previous rate** (adjusted for PFP/market increases).

**or amount needed to come down to maximum.

Increase funding data

Select each data point to include.

- ☐ 1. Projected average salary increase budgets in market.
- ☐ 2. Projected market wage movement.
- ☐ 3. Available funds not used in previous year.
- ☐ 4. Aggregate midpoint vs actual pay ratio.
- ☐ 5. Individual compa-ratios.
- ☐ 6. Consumer Price Index. (not recommended)

Distributing increase funds

Method:

Select one of the options listed below.

- ☐ 1. Distribute both through the PFP calculation.
- ☐ 2. Distribute through separate mechanisms.

Timing:

- ☐ 1. Apply performance and market adjustments to employee salaries at a single point in the year.
- ☐ 2. Apply at separate times of the year.

Increase calculation

Select one of the options listed below.

- ☐ 1. Utilize Merit Matrix (not recommended)
- ☐ 2. Continue with current PFP calculation
- ☐ 3. Utilize modified PFP calculation with one or both of the following:
  - ☐ Eliminate self-appraisal in calculation. Continue for documentation purposes only. (recommended)
  - ☐ Distribute funds among entire county (rather than by department)