HaRe Group newsletter: **4 October 2012**

Subject: **When pay review outcomes fail expectations**

Most employers would agree that their annual employee pay review is an excruciating process – not only do HR managers struggle with complex worksheet reconciliation and poor budget accountability, but there is often difficulty in managing employees' expectations and dealing with their angst over the outcomes.

With few exceptions, Australian companies are under pressure to be more profitable. Since employment cost is such a significant expense, the money available for each annual pay review is limited. This year, the median budget increase was only 3.5% (*independent HaRe Group research*).

In conjunction with a tight economy (proved by another interest rate reduction by the RBA this week), Australian companies are demanding greater productivity from their employees. It's well known that talented people are critical to building and sustaining competitive advantage, so keeping these people is paramount to business success. The last thing any employer wants is to disengage the people who are the most productive.

A poorly managed and communicated pay review process is certain to disengage talented employees.

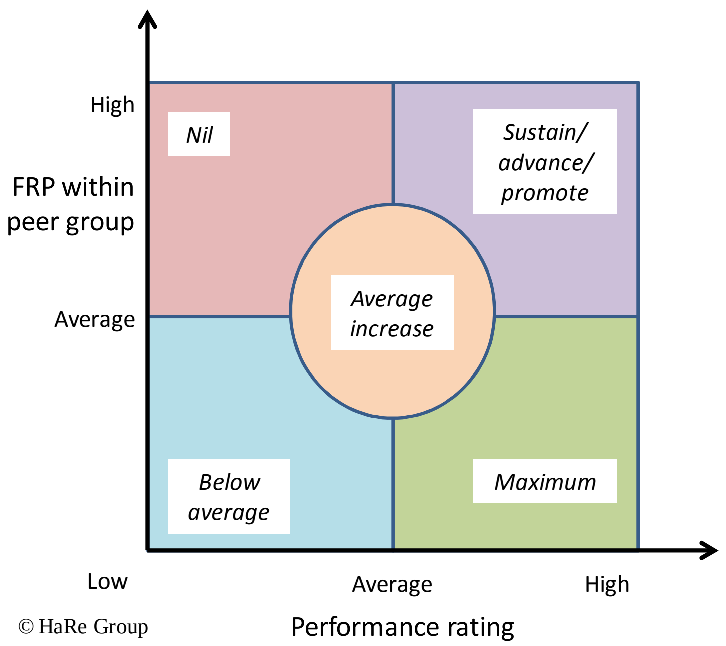
Generally speaking, employees will be happy to know that there is a robust system in place to fairly and impartially review their remuneration. They won't usually expect a detailed explanation of how the system operates, but they'll often want to know the logic behind the decisions that are made. In particular:

- How much money is available for salary increases?
- How is the money "pie" divided between employees?

Of course, an organisation with a "closed" communication culture will be reluctant to reveal any information on this subject – even to their key employees. However, many employers see greater benefits in trusting their people with this information, but only if the communications are effective. In these cases, employees usually learn about:

- Fixed Remuneration Package (not just salary) as the primary measure of base pay
- The available budget for FRP increases for their peer group of employees
- Comparing FRP levels to market rates and their peers within job families
- The impact of individual performance, relative to others in their peer group (which assumes that a reputable performance appraisal process is operating)

This chart will help explain how individual FRP increases can be determined by the intersection of each employee's performance with their FRP, both relative to the employee's peer group:



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FRP increase differentials should favour high performing employees. Lack of performance-based differentiation will often frustrate and disengage the high performers, which cannot be preferable to greater differentiation and disengaging the low performers who may get nothing.

Employees should have a common understanding that there is a limited FRP budget and that it should be divided according to relative pay levels and relative performance. If employees know that they are under/ around/ over average in both FRP and performance, they will usually be more accepting and more satisfied with the FRP review outcome.

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