

## COMPENSATION PUZZLE

I have often seen employers struggle with a right approach to fixing the executive compensation. Whether incentives should be included? Should a variable component added to the annual compensation payable? Is annual performance appraisal system needed?

To further substantiate the above, behavioral research is putting forth the negative impact of explicit compensation like incentives. It is said to be displacing other motivations like altruism, civic duty, and professionalism that humans are known for. This is true when we have forensic audit firms with their crude suggestions ruining the residual and scarce feelings of selflessness and responsibility.

Thinking objectively, I was able to compile below key aspects of compensation that may help employers address the compensation puzzle:

1. 'Performance appraisal' should be 'reasonable' when defined. We have 'transparency' and 'objectivity' achieved but 'reasonableness' goes missing.
2. If there is a variable component linked to annual compensation then the efficacy for annual appraisals is limited.
3. 70% of the performance of an institution is influenced by external factors or 'factors' beyond the control of any single employee.
4. If the average age is less than 30 years, then a good percentage of employed is 'Next gen' who will anyways

change jobs every 2-3 years. In Asia, the average employee turnover is nearing 10% or higher.

5. As humans, reward visible in near future and measurable is more attractive but may produce undesirable behavior.
6. Limit the annual performance appraisal process for promoting or transferring to other functions.
7. The annual inflation-adjusted increase in compensation is not a necessity anymore.



One of the best questions I got to answer recently was "Who compensates you?" I promptly uttered 'Work'.

Then I substantiated my reply stating that when I receive my monthly compensation ('fixed') it's for my eligibility for employ-ability in the coming month rather previous month for which I am contractually eligible. Some may critique this as a too short-term approach to employment highlighting distrust towards one's employer. They will have their opinion refined when they read further.

Compensation is a universal term that not only constitutes the explicit monetary reward but also the intrinsic rewards like belongingness to an institution, recognition, positivity, stability, and security.

Taking the economists assumption of a 'perfect world' with all humans 'rational', the word 'compensation' will be limited to monthly salary one draws for her work. However, we know that's not true. We would not have four decades of empirical research on annual performance appraisals and impact of incentives of employee outcomes. And then quantum of time spent by on designing innovative reward structures.

I have often seen employers struggle with a right approach to fixing the executive compensation. Whether incentives should be included? Should a variable component added to the annual compensation payable? Is annual performance appraisal system needed?

To further substantiate the above, behavioral research is putting forth the negative impact of explicit compensation like incentives. It is said to be displacing other motivations like altruism, civic duty, and professionalism that humans are known for. This is true when we have forensic audit firms with their crude suggestions ruining the residual and scarce feelings of selflessness and responsibility.

Thinking objectively, I was able to compile below key aspects of compensation that may help employers address the compensation puzzle:

1. 'Performance appraisal' should be 'reasonable' when defined. We have 'transparency' and 'objectivity' achieved but 'reasonableness' goes missing.
2. If there is a variable component linked to annual compensation then the efficacy for annual appraisals is limited.
3. 70% of the performance of an institution is influenced by external factors or 'factors' beyond the control of any single employee.
4. If the average age is less than 30 years, then a good percentage of employed is 'Next gen' who will anyways change jobs every 2-3 years. In Asia, the average employee turnover is nearing 10% or higher.
5. As humans, reward visible in near future and measurable is more attractive but may produce undesirable behavior.
6. Limit the annual performance appraisal process for promoting or transferring to other functions.
7. The annual inflation-adjusted increase in compensation is not a necessity anymore.

*-Jaspal Singh Kahlon (Jaspallife.com)*