

Sutton Shareholdings Board

Tuesday, 8 November 2016

6.30 pm at the

Civic Offices, St Nicholas Way, Sutton SM1 1EA



SUPPLEMENTAL AGENDA

To all members of the Sutton Shareholdings Board:-

Please bring the following papers with you to the meeting:-

6. Encompass Pay and Reward Scheme

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Appendix

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Reward Scheme for Encompass Employees

1. Introduction
2. Objectives of Encompass Reward Scheme
3. Encompass Reward Scheme - the framework explained
4. Establishing the Level of Benefits
5. The Appraisal Scheme
6. Conclusion

1. Introduction

A major part of performance management involves managing employees since their performance will have a major effect on the performance of the organisation as a whole.

Modern research indicates that individuals are attracted, retained and engaged by a whole range of financial and non-financial rewards and that this can change over time depending on personal circumstances. In certain situations, individuals may not consider the financial elements of a package particularly important. For instance, people at the beginning of their career may be more interested in gaining access to training and career development. Similarly, individuals may be willing to work for lower pay rates (or even volunteer) if they have a strong attachment to the mission of an organisation, such as a charity.

In creating this reward scheme, Encompass has clearly defined the objectives of the scheme and aligned these to the business strategy. These objectives will be utilised to shape the incentive plan, as well as the expectations and objectives of individual employees.

When designing a performance management process that is linked with pay, it is imperative that employees know what their individual objectives are, how they will be measured, and how they will be compensated when achieved.

Managers must also be careful to ensure that there is adequate differentiation between high and low performers. If mediocre employees are given an average merit increase, they will perceive that their performance is adequate. Conversely, if excellent performers only receive a little more in incentive pay than average performers, they will perceive that the company does not value their performance.

Encompass has defined desired employee behaviour and performance through its Mission Statement, Values and Strategic Businesses Plan and will measure that performance through its appraisal system. This enables the objectives for the individual employee, the business units, and for the company to be connected.

2. Objectives of Encompass Reward Scheme

What does Encompass hope to achieve from a reward scheme?

1. To support the aims of the organisation by aligning the individual objectives of employees with the strategic aims of the organisation.
2. To ensure that the organisation is able to recruit and retain sufficient number of employees with the right skills.
3. To motivate employees.
4. To align the risk preferences of managers and employees with those of the organisation.

5. To comply with legal regulations.

1. ALIGNING THE GOALS OF THE ORGANISATION AND EMPLOYEES

The reward scheme will support the organisation's aims and objectives. At the strategic level, the reward scheme will be consistent with Encompass's Business Strategy.

https://docs.google.com/document/d/1811ff9hxq-il60eICjRUvwj0_pNG0wvV_RN_peAaPQ0/edit#

2. TO RECRUIT AND RETAIN SUFFICIENT EMPLOYEES WITH THE RIGHT SKILLS

If rewards offered are not competitive, it will be difficult to recruit staff since potential employees can obtain better rewards from competitors. Existing staff may also be tempted to leave the organisation if they are aware that their reward system is uncompetitive. High staff turnover can lead to higher costs of recruitment and training of new staff. Losing existing employees may also mean that some of the organisation's accumulated knowledge is lost forever. For many knowledge-based organisations, the human capital may be one of the most valuable assets they have.

3. TO MOTIVATE EMPLOYEES

Motivation of employees is clearly an important factor in the overall performance of an organisation. Organisations would like their employees to work harder, and be flexible. The link between reward schemes and motivation is a complex issue that is hotly debated in human resource-related literature as job security, ability to achieve one's potential, and feeling of being needed become more important. Monetary rewards alone are insufficient to motivate employees. Other factors such as giving greater recognition and greater responsibility may be equally important, for example giving praise at company meetings, promoting staff, and involving staff more in decision making.

4. ALIGNING THE RISK PREFERENCES OF MANAGERS AND EMPLOYEES WITH THOSE OF THE ORGANISATION

Risk appetite is the amount of risk, on a broad level, an organisation is willing to accept in pursuit of value. Each organisation pursues various objectives to add value and should broadly understand the risk it is willing to undertake in doing so.

Managers and senior employees make decisions on behalf of the company, acting as agents of the company. It is desirable that the risk preferences of these employees should match the risk preferences of the organisation and its stakeholders. One problem with many reward schemes is that managers are too risk averse, and will not take actions that may risk their targets not being met.

5. COMPLYING WITH LEGAL REGULATIONS Rewards should comply with legal regulations. Typically, employment laws include areas such as minimum pay, and equal pay legislation to ensure that no groups are prejudiced against.

3. Encompass Reward Scheme - the framework explained

The Encompass Reward Scheme will consist of three elements of pay;

- i) base pay
- ii) bonus scheme consisting of three elements
 - individual performance related pay
 - profit related bonus
 - innovation payments
- iii) employee benefits
 - benefits in kind
 - flexi time
 - flexible working and telecommuting
 - purchase of annual leave

i) Base Pay

The base pay, or basic pay, element is the minimum amount that an employee will receive for working for an Encompass. This will be a fixed annual salary for a 36 hour working week.

ii) Bonus Scheme

Encompass bonus scheme is designed to fulfil a number of key business objectives:

- To improve business performance (e.g. productivity, satisfaction, profits)
- To focus employees' efforts on key objectives such as customer service, quality and service delivery
- To increase employee motivation by establishing a clear link between pay and performance (at an individual and Company level).
- To support stakeholder ideals by allowing employees to share in the success of the business
- To encourage change within the Company.
- To create the desired workplace culture

Encompass bonus scheme will operate at two levels allowing the Company to reward individual efforts and Company success.

- Individual Performance Related Pay

Individual performance-related pay will be a payment made based on the performance, of the individual. In recent decades there has been a move toward performance-related pay schemes in many organisations. The rationale for individual performance-related pay is that it motivates employees to work harder, and rewards those who make a greater contribution to the organisation's aims and objectives.

Advocates of individual performance-related pay schemes state that if performance targets set are based on the aims and objectives of the organisation, then it appears obvious that making part of the rewards of employees' contingent on achieving those

targets will mean that employees are motivated to achieve the goals of the organisation. Individual performance-related schemes also have the advantage over team performance since the employee has control over his/her rewards, as they do not depend on the effort (or lack of) of other members of the team.

The Encompass individual performance-related pay is based on the employee receiving a 'bonus', rather than an annual incremental increase in base pay, where previously agreed objectives contained within an appraisal have been met. A 'bonus pool' is attached to each salary and depending on the outcome of the individual performance a proportion or all of the 'pool' may be paid. Bonuses will be paid in line with the appraisal year.

The performance-related reward scheme will depend on the performance of the employee. As such, the employee's performance will be assessed during the appraisal process (see below). Staff will be assessed twice a year. During the appraisal, targets will be set for the next period, and rewards agreed if the targets are met.

- Profit Related Bonus Scheme

A profit-related bonus is a type of group performance-related pay where a part of the employee's remuneration is linked to the profits of the organisation. If the company's profits hit a predetermined threshold, a bonus will be paid to all members of the scheme.

Advocates of profit-related bonus schemes argue that it motivates employees to become more interested in the overall profitability and therefore, become more motivated to 'do their bit' to improve it. It may also encourage loyalty in cases where staff may lose their bonus if leaving the organisation means that they lose the right to it. The obvious disadvantage with profit bonus schemes is that it does not match the

primary objective of commercial organisations, which is to maximise the wealth of the shareholders.

However, in this instance such a disadvantage is mitigated since that is not the primary purpose of the LATC. The only shareholder is the London Borough of Sutton and the Sutton Shareholdings Board will agree the sum to be retained by Encompass LATC. Therefore, a balance between rewarding company success and benefiting the community can easily be achieved.

Additionally, not all profit retained by Encompass will be distributed as a bonus and a balance between service improvement and profit share is a decision that Encompass' Directors will determine on an annual basis.

- Innovation Fund

Employees will be rewarded where an individual makes an exceptional contribution to the delivery and development of services in a defined way i.e. identifying a business opportunity which generates an income or result in an identified efficiency saving and is over and above what is expected as part of their role within Encompass i.e. the Business Development Team would not be rewarded for identifying a business opportunity.

iii) Employee Benefits Package

- Benefits in Kind

Benefits in kind (or indirect pay) are available to employees in addition to their base salary and performance-related pay. Benefits in kind include items such as health insurance, car parking schemes and restaurant vouchers. They are usually more attractive to junior staff and are an additional incentive at a lower cost. They are often used as a form of recognition, so the employee of the year for example, will be given a

benefit rather than a cash payment. The advantage of benefits in kind is that greater flexibility can be given in designing a reward scheme for an individual. The advantage of this is that employees will select the benefits that they value most.

Encompass are currently considering packages available on the market and consulting staff which benefits they value the greatest. This information, along with costs associated with these benefits, will be used to determine the final benefits in kind package.

- Flextime

Flexi time enable employees to manage work and personal commitment in harmony and therefore the employee has a greater chance of achieving work-life balance.

ii) Flexible Working and Telecommuting

Working from anywhere, at any time, is quickly becoming the norm at many companies, made possible by advances in technology such as cloud-based applications, online video and virtual meeting rooms. Where it fits with the service delivery model, working remotely is one of the best employee benefits that can be offered to help workers maintain work-life balance, In fact, people who telecommute from home are typically are more productive and have greater job satisfaction than in-office workers .

- Annual Leave Purchase Scheme

Buying leave is an employee benefit that allows an employee to make an extra annual leave purchase. The purpose of the annual leave purchase scheme is to provide staff with additional flexibility where possible, subject to operational requirements, in respect of planned time off work. The employee agrees to sacrifice part of their salary in return for extra annual leave entitlement. Encompass Ltd will allow the purchase of up to an additional 10 days annual leave.

All requests for purchasing additional annual leave for the following annual leave year must be submitted to the Team Manager by 31st January preceding the relevant annual leave year. Managers will consider the operational feasibility of granting all the request. This will involve consideration of the fact that no additional cover can be arranged through any means (including overtime, additional hours, or agency) for any additional leave granted. Any additional annual leave must be taken in the employee's leave year, no leave can be carried forward where additional leave has been purchased.

A fully worked up operational policy will be developed to accompany Encompass's new terms and conditions of employment.

4. Establishing the Level of Benefits

i) Base pay

How much should employees be paid? Two factors need to be taken into account here. First, competitiveness, and second internal equity. As already mentioned above, unless the level of pay is competitive, it will be difficult to recruit and retain the right number of skilled employees. If it is too much, the cost to the organisation will be too high.

Encompass has determined its salary structure using the London Borough of Sutton People Plan salary structure. Only recently has the London Borough of Sutton carried out extensive research and analysis on their own pay and reward scheme and therefore, Encompass has benefited from being able to draw on a recently reviewed pay structure.

The pay structure and salary of staff transferred under TUPE to Encompass will remain unchanged and employee's TUPE to Encompass will retain the banding attributed to that job role under the London Borough of Sutton People Plan.

However, for all new employees, the base pay will be determined at point 3 within that band, with a bonus pool attached.

ii) Performance Related Pay

The bonus pool is based on a percentage of the base salary. *Research indicates that most bonus pools are between 5% and 15% and the Encompass scheme has been modelled on 10% for grades 1 to 6 and 15% for grade 7 and above.

The clear benefit of this structures is that the initial starting salary is higher than it would be using an incremental approach. However, new employees will not reach the unconsolidated element of the current pay scale in either model. The unconsolidated element of the current pay scale will only be used where a market supplement is required to attract suitably skilled staff and only after evidence based discussion.

Additionally, the percentage of the bonus pool an employee is awarded will be determined by the outcome of the individual appraisal which, is based on a balanced score system.

Employees will be awarded either 50%, 75% or 100% of the bonus pool depending on the outcome of the appraisal. Employees will need to demonstrate through the appraisal that they have operated above a satisfactory standard to receive a bonus. Employees must demonstrate that they have reach a 'good' standard to receive 50% of the bonus pool, 'very good' to receive 75% and 'exceptional' to receive 100%.

A Team Managers will be given a defined budget that will be used to fund the agreed bonuses for their team members which, will be insufficient to support an award of 100% of the bonus pool for every employee within that team.

It is unlikely that all staff will perform at an exceptional level or even at a very good level and therefore, by allocating a defined budget, managers will be required to examine individual performance and the appropriate reward. Contingency will made for

circumstances where the performance of staff within an individual team does exceed the budgetary provision but, significant evidence will be required to support a requested for a higher budget.

Job evaluation techniques will determine the value of a new job roles in Encompass LATC Ltd organisation.

Example

Job Role - Housing Adviser

Current Salary

Band 7 - Salary Range

Point 1	Point 2	Point 3	Point 4	Point 5	U/C
£27,252	£28,935	£30,555	£31,986	£33,660	£35,655

New Pay Structure.

Base Pay - £30,555

Bonus Pool 15% - £4,583

Possible Total Salary (without any Profit Related Bonus) £30,555 to £35,138

Following the annual appraisal the employee is awarded 50% of the bonus pool

Employee's salary during the following year is £32,846

iii) Profit Related Pay

Most schemes, typically link a profit related bonus to base pay and will be a percentage of the basic pay. Encompass will adopt this methodology for determining the unconsolidated bonus payment.

A profit related bonus will only be available to staff who have completed six months employment with Encompass and will be prorated accordingly. No entitlement to such a

will arise where an employee leaves the company prior to the end of year or during a notice period.

Contract of employments will be constructed to ensure that the profit related bonus is discretionary. All the details of the profit related bonus scheme will be put in writing so the terms are easily understandable. The profit related bonus scheme will be separate to the employee's contract of employment so it can be easily reviewed and amended or updated as necessary.

The bonus scheme will be described in writing as discretionary, non-contractual, reviewable and that it can be withdrawn by the Company at any time.

5) The Appraisal Scheme

(Please note the final details of the balanced scorecard are being developed in conjunction with Encompass's HR advisers)

Traditionally, employee performance, other than Senior Managers, has been assessed by the manager and the employee agreeing upon specific and obtainable goals with a set deadline. Management by objective setting enables the appraiser to easily define success and failure.

However, in a more commercial organisation a more complete measure of organisational performance is required. But by balancing internal and process measures with results and financial measures, managers will have a more complete picture and will know where to make improvements.

A 'balanced scorecard' method of appraising performance give a comprehensive view of the organisation's performance and include both process and results measures. A balanced scorecard or a balanced set of measures provides that valuable information.

Four Perspectives

- The customer's perspective. Managers must know if their organisation is satisfying customer needs. They must determine the answer to the question, how do customers see us?
- The internal business perspective. Managers need to focus on those critical internal operations that enable them to satisfy customer needs. They must answer the question, what must we excel at?
- The innovation and learning perspective. An organisation's ability to innovate, improve, and learn ties directly to its value as an organisation. Managers must answer the question, can we continue to improve and create value for our services?
- The financial perspective. In the private sector, these measures have typically focused on profit and market share. For the public sector, financial measures could include the results oriented measures. Managers must answer the question, how do we look to our stakeholders?

A balanced approach to employee performance appraisal is an effective way of getting a complete look at an employee's work performance, not just a partial view. Using a 'balanced scorecard' method of performance appraisal the employee performance is linked to the organisational objectives. Alternative models of performance appraisal often measure behaviors, actions, or processes without also measuring the results of employees' work. By measuring only behaviors or actions in employee appraisal, an organisation might find that most of its employees are appraised as 'outstanding' when the organisation as a whole has failed to meet its objectives.

By using balanced measures at the organisational level employee performance plans are aligned with organisational objectives.

The balanced scorecard developed for Encompass LATC Ltd views the organisation from four perspectives. Encompass's four quadrants are;

- i) Innovation and Learning
- ii) Business Processes
- iii) Financial
- iv) Customer and Relationships

i) Innovation and Learning Perspective

The customer-based and internal business process measures on the balanced scorecard identify the parameters that the company considers most important for competitive success but, the targets for success keep changing. Intense competition requires that Encompass makes continual improvements to their existing services and processes and have the ability to introduce entirely new services with expanded capabilities.

Encompass's ability to innovate, improve, and learn directly relates to the company's success. Only through the ability to develop and launch new services, create more value for customers, and improve operating efficiencies continually can a Encompass penetrate new markets, increase revenues streams and grow.

In a largely knowledge-based service, employees are the main resource. In the current climate of rapid change, it is becoming necessary for employees to be in a continuous learning mode. Metrics can be put into place to guide managers in focusing training funds where they can help the most. Learning and growth are the essential foundation for success of any knowledge based led organisation.

'Learning' is more than 'training'¹ it also includes things like mentors within the organisation, as well as that ease of communication among workers that allows them to readily get help on a problem when it is needed.

ii) The Business Processes Perspective

This perspective refers to internal business processes.

Customer-based measures are important, but they must be translated into measures of what the company must do internally to meet its customers' expectations. Excellent customer performance derives from processes, decisions, and actions occurring throughout the Company. Managers need to focus on those critical internal operations that enable them to satisfy customer needs. The internal measures for the balanced scorecard should stem from the business processes that have the greatest impact on customer satisfaction—factors that affect cycle time, quality, employee skills, and productivity, for example. Companies should decide what processes and competencies they must excel at and specify measures for each.

Metrics based on this perspective allow the managers to know how well their business is running, and whether its products and services conform to the customer and users requirements.

iii) Financial Perspective

Financial performance measures indicate whether the company's strategy, implementation, and execution are contributing to financial success.

Timely and accurate data will always be a priority, and managers will do whatever necessary to provide it but, there is a need to include additional financial-related data, such as risk assessment and cost-benefit data, in this category.

¹ Kaplan & Norton

Typical financial goals have to do with profitability, growth, financial analysis and financial management. More important, however, is to ensure that improved operating performance and growth is reflected in financial success. Ideally, Encompass should specify how improvements in quality, cycle time, delivery, and new product introduction will lead to higher market share, operating margins, reduced operating expenses or increased profit. The challenge is to learn how to make such linkage between operations and finance explicit in this newly formed commercial entity and some further work will be required to ensure that the metrics are ones that are fully understood and, more significantly, can be applied.

iv) Customer and Relationships Perspective

If customers are not satisfied, they will eventually find other suppliers that will meet their needs. Poor performance from this perspective is thus a leading indicator of future decline, even though the current financial picture may look good.

Encompass focuses on the customer and how the company is performing from the customer's perspective. The balanced scorecard enables managers to translate our strategic priorities for customer service into specific measures that reflect the factors that really matter to customers.

6. Conclusion

A good reward system aims to motivate employees to work harder, and align their goals with those of the organisation they work for. The current trend towards performance-related reward systems is designed to lead to greater rewards and motivation for those who contribute the most.