Loop Health

HR Resources

Compensating Employees

Loop HR Guides

Compensation

Three sections included

1. Creating a compensation strategy
2. Rolling out compensation strategy for the first time
3. Structuring incentive based bonuses

Why?

At Loop Health, we've reviewed proprietary data from nearly 3,000 partners and found that the most successful HRs and recruiters are deeply tactical. These leaders track project management, cost analysis and map people management metrics to business outcomes. We've decided to share these insights with the HR community at large in order to help practitioners go from HR *analyst* to HR *strategist*. **These guides will be useful for new HR associates who are learning about the world of organizational management, as well as HR veterans interested in elevating their game.**

At Loop Health, we're fortunate to work with visionary HRs everyday. Our HR partners work across their organizations to optimize not only hiring, compliance, productivity and retention, but employee experience, leadership, learning, development and more. It's not uncommon for HR to be at the centre of organizational restructures and establishing company values – and these areas are more important than ever for modern companies. Setting expectations and prioritizing areas to focus on has never been more challenging. With these challenges come significant opportunities for HR leaders.

Before we get started

At Loop Health, we're building the easiest-to-use health benefit provider in India. We offer free OPD services for all of our partner companies. Learn more at www.loophealth.com or reach out to our Head of Partnerships, Pranaav Marathe, directly at +91 99703 58844

Process: Creating a compensation strategy

This section discusses the following topics related to developing a compensation strategy:

- Why you need a compensation strategy
- Equity-salary calculator
- Compensation process overview
    - Step 1: Get leadership buy-in
    - Step 2: Choose compensation philosophy
    - Step 3: Create a compensation formula
    - Step 4: Roll out plan
    - Step 5: Adjust annually
    - Step 6: Add new levels as needed
- How to determine market salary for each role
- How to set equity-to-salary ratio

Why you need a compensation strategy

Without a compensation strategy…	Time	Motivation	Money
Companies waste time negotiating new hires or comp requests.	✔		
Can end up hiring two people in similar roles for a 2X comp difference, wasting money and demotivating the team.		✔	✔
You don't manage comp expectations, and cause frustration when expectations aren't met.		✔	
You overpay for talent because they undervalue their equity.			✔
Sales teams can underpay great performers and overpay mediocre ones, draining a critical resource for success.		✔	

Equity-salary calculator

Use this salary-equity calculator as you create your compensation plan.

Step 1: Get Leadership buy-in

1. Be ready to make your case for a compensation philosophy. Leadership at startups are usually rookies when it comes to compensation.
   - Identify pain points specific at your company.
   - Review our common pain points in the table below.

2. Propose compensation philosophy goals that maximize value, such as:
   - Align everyone to focus on building the value of their equity.
   - Match market rate salary.
   - Be formulaic rather than discretionary or case-by-case.
   - Make raises with additional equity rather than salary when possible.

3. Create a basic process to follow to make it easy for leadership to buy-in.
   - HR/Name to draft basic philosophy and submit for approval by [DATE].
   - HR/Name to draft compensation plan according to philosophy and submit for approval by [DATE].
   - Feedback and approvals meeting to ensure all stakeholders are aligned
   - Roll out new compensation plan starting on [DATE].

4. Create a communication plan. Get buy-in from all leadership or stakeholders in your process to follow it. Communicating your philosophy before its finalized can lead to false expectations and employee-upset.

5. Conduct kick-off meeting to get leadership buy-in. Simplify the process for leadership as much as possible to get buy-in. For example, an agenda to send to leadership should include:
   - Review needs for a compensation strategy.
   - Discuss high level goals.
   - Agree on process.

Step 2: Choose a compensation philosophy

Compensation philosophy is based on two factors:

- Salary compared to market rate: Do you match, lead, or lag?
- Salary discretion limitations: Do you allow for negotiation at the Hiring Manager's discretion? Or do you use a formulaic method (recommended).

Compensation philosophy for companies: maximize value

- Pay as close to market rate as possible so people aren't worried about cash.
- Focus everyone on equity, and on maximizing their equity value.
- Remove discretion from the process and keep it formulaic.

Why set a philosophy that maximizes value?

- People don't join a startup for the salary. They join to work with great people and build something that matters.
- Focus employees on maximizing their equity value. If the company is successful, employees may earn much more from equity than salary. Provide equity commensurate to experience and risk, and make sure everyone is focused on building the company's value every day through their work.
- Salary discretion rewards the wrong things. The more comp discretion you introduce, the more you reward people for things unrelated to performance — like negotiating ability, or size of previous salary.
- Share the "how" and "why" with employees. Employees value equity only if you explain how it works — its mechanics, its most recent valuation, and how its value changes based on company performance. They won't link their activities to the company's equity value unless you make the connection.

Without an explanation of how their work builds value, you're wasting the motivating power of equity at a startup.

Step 3: Create a compensation formula

A compensation formula sets salary and equity compensation for each role.

1. List out roles in your company by function.
2. Research market compensation for each role. Adjust according to your company's market-rate compensation strategy. Remember, how you adjust to market may vary by role or department.
3. Set an equity-to-salary ratio for each role.
4. For example, equity-to-salary ratio is 33% for a junior engineer earning $150,000 in salary and $50,000 in equity.
5. Apply your formula to all employees and prospective hires.
   - If you vary compensation for the same role based on skill or experience, indicate how each person's comp varies as a percentage of the role. For example, a junior engineer with four years experience may receive 5% higher than one with two years experience.
   - If you allow employees to trade off between salary and equity, create a framework. A common strategy is a dollar-for-dollar offset. For example, an engineer earning $150,000 and receiving $50,000 in equity may decrease salary by 10% to earn $135,000 in salary and $65,000 in equity.
6. Use the recorded valuation at the time an employee joins to determine their equity ownership stake.

Best Practices

1. Skill level shouldn't factor into initial pay. Skill is what gets someone hired in the first place. Plan on recognizing skilled employees over time through performance-based equity and promotion.
2. Assign equity-to-salary ratios by experience level:

- Junior (less than five years of career experience)
- Senior (more than five years of experience)
- VP (leading department)
- You can create a standard ratio for each company-wide level, or within functional areas of similar value to the company like Engineering and Product or Operations and HR.

3. Calculate equity in dollar value (not in percentage of the company) to underscore the importance of growing stock value, not ownership stake.
   - Equity should reflect employee risk. Earlier employees should receive more equity because the company was riskier when they joined. Adjust for risk by dividing current share value by the overall company value at the time when the employee joined.
4. Keep equity-to-salary ratios stable as you scale so you don't have to re-benchmark every time the company raises money.
   - As you grow, salaries increase and equity values increase. Valuation increases even faster, so employees may earn more value in equity while owning an increasingly smaller percentage of the company.

How to determine market salary for each role

Private compensation surveys, such as:

- https://www.advanced-hr.com/
- https://hiringplan.io/ (Free data access!)

Feedback from your VC, recruiter or other HR professionals:

- https://www.linkedin.com/groups/2894430/ You can post comp questions for HR professionals here.

Public compensation surveys:

- AngelList
- Paysa
- Salary.com

- [Indeed]
- [Glassdoor]
- [Payscale]

Best Practices:

1. Start with HiringPlan.io, which provides reputable survey data for free. Then ask your VC for access to their premium comp surveys.
2. Make sure to find true comparables. This means a similar function and responsibility, not just the same title. It also means ensuring companies are at a similar stage and location.
3. If you're blazing a trail in organizational roles or technology, compensation benchmarks will vary widely. You're better off collecting your own data than relying on surveys.
4. Free compensation surveys suffer from selection bias. HR professionals view them skeptically and typically don't use them at all.
5. AngelList provides live data from actual job postings, including both salary and equity so you can see what other startups you know are offering.
6. As part of your research, track both median and range from the 25th to 75th salary percentile. Use this range and your compensation philosophy to set your target salary for a job.
7. If it's your first time benchmarking a job, share your completed compensation rubric with investors or recruiters who can gut-check your numbers.

How to set equity-to-salary ratio

Accel Ventures recommends the following ratios:

	Junior	Senior	VP

Engineering, Product, BD	33%	50%	75%
Marketing, Finance, HR	15%	20%	33%
Sales, Customer Success	5%	10%	33%

Best Practices:

1. Get advice from VCs and recruiters to make sure you're picking the right ratios for your market.
2. Gut-check your ratios by comparing to ratios at large companies, which report equity in dollar amounts. For example, if entry level engineers at Google earn $150,000 in cash and $50,000 in equity, they're using a ratio of 33%.
3. Ratios are higher for technical roles, especially in tech hubs. They are also higher overall in tech hubs.
4. Compare resulting percentage ownership to compensation surveys and AngelList. If your formula says a junior engineer should own $50,000 in equity and your company is worth $10,000,000, how does 0.50% compare with what other companies of your stage in your area are giving junior engineers?

Step 4: Roll out to employees for the first time

Roll out your compensation to existing employees in four steps:

1. Use your internal compensation analysis to identify people who are over- or under-compensated. Plan to raise the salary of those who are underpaid and to schedule a one-on-one with those who are overpaid.
2. Meet with senior leadership and share your target compensation. Explain

your process, and how the target compensation will affect your current burn rate. Also highlight which employees are underpaid to illustrate the risk of losing key team members without a new policy. Get their approval for the plan and the salary adjustment before sharing it more widely.

3. To roll out the changes, schedule an all-hands meeting to explain the changes to the team. Be transparent about the reasons for the change, the process you used, and the data underpinning the results.
4. Follow up with an email explaining the details of the plan. Let employees schedule time with their managers or the HR head to discuss these details. Schedule time with all employees who are overcompensated to explain and discuss their options.

Best Practices:

- In smaller companies, HR can conduct one-on-one question-and-answer meetings, so you don't need to train managers for all kinds of Q&As.
- Managers should have one-on-ones with team members who didn't get an increase. This conversation can be tough, and can go two different ways. Instead of dwelling on the negative, focus on what employees need to do to earn a promotion or performance-based compensation (if your company provides performance-based comp): "You're actually above market rate, so if you want more, let's talk about how we can work together so you can earn a promotion into a new role with a higher pay."
- Don't be cute about communicating compensation to employees. Bethanye McKinney Blount shares how startup founders would deposit random amounts in employee bank accounts in lieu of bonuses. "It was very confusing and not the least bit fun." BuzzFeed employees recall, "I remember when our holiday bonus was a drawing of a cat, and the CEO presented it as an investment."

Step 5: Review annually and adjust salaries

Adjust salaries to market rate once a year.

1. Don’t review salaries more than once a year. The process takes time. Annual review is enough to ensure fairness and employee satisfaction.
2. After you raise a large round, increase all salaries slightly to help retain employees against competing companies at your new funding level. No need to roll out changes immediately, but don’t put off adjustments for longer than the annual pay review cycle.
3. In communication, emphasize that salary adjustments have nothing to do with performance. They’re just keeping up with the market. Instead, for a promotion or exceptional performance, employees can earn additional equity.

Email template: Communicate Annual Salary Increase

Note: This should only be sent out as a confirmation after managers discuss with team members during recurring one-on-ones. We strongly advise against discussing compensation over email.

Hi [NAME],
We’re pleased to share the results from our annual salary review process.
Our goal is to make sure we're keeping up with market pay for your role. We’re targeting [MEDIAN] salary for [SEED] companies in [SAN FRANCISCO]. [Because of our recent Series B raise, we’re benchmarking against a set of bigger

companies. As a result, we expect to see a slight increase in pay across the board.]
For a [ENGINEERING VP] like you, this means [an increase] from [$200,000] last year to [$212,000] this year. [You'll see that adjustment on your next paycheck.]
Regards,

[YOUR NAME]

Step 6: Add new levels as needed

If successful, your company will eventually outgrow a three-level system, especially if you're offering each level the same pay without any discretion. When this happens, you have options to reflect your greater number and variety of roles:

Approach	Pros	Cons
Add more levels.	It's simple. This is particularly helpful if you're not negotiating salaries — to differentiate between "entry" and "junior" developers, for example.	If you grow large enough, having different rules for every function will be more complex than mapping all roles onto company-wide levels.
Add salary ranges within levels.	You can push three levels quite far if each has a range to account for experience and performance.	This introduces more discretion into the process, sacrificing the benefits of a formulaic comp plan by allowing salary advocacy.

Create steps within roles.	Each “step” can represent one or two years of experience, and can have clear criteria for different kinds of roles. This allows a “no-negotiation” approach that can account for variation of experience within levels.	Steps still allow discretion and negotiation — even when steps are formulaically defined. Steps are also complicated if your company isn’t very large.
Develop company-wide job levels.	Instead of having separate tracks for each function, you map each role onto an overarching job level, and pay these roles the same across the company. It’s transparent and systematic. Combined with steps and clear criteria, it can remove ambiguity from compensation.	This allows all employees to compare their worth, which will inevitably demoralize some — especially when first introduced. It’s complex and takes a lot of time to roll out and maintain, so it only makes sense for large companies. You cannot escape discretion in assigning people to levels.

How to roll out a compensation plan for the first time

Rolling out a compensation strategy for the first time is the fifth stage of creating a compensation plan:

This article details the steps necessary for compensation roll out:

- **Step 1:** Finalize your comp plan and proposal
- **Step 2:** Get leadership approval
- **Step 3:** Run all-hands meeting
- **Step 4:** Share comp plan

Step 1: Finalize your comp plan and proposal

Plan to raise salary for those who are underpaid versus your plan and to schedule a one-on-one with those who are overpaid. You won't be decreasing salaries for anyone, but you need to let overpaid employees know not to expect increased pay, and to share what they can do to increase compensation by earning a promotion or performance bonus.

Name	Function	Title	Level	#	Salary $	Target $	Adjust $
Sookie	Eng / Prod		VP		$180	$200	$20
Bill	Eng / Prod		Senior		$160	$140	Overpaid
Tara	Eng / Prod		Junior		$70	$100	$30
Eric	Eng / Prod		Junior		$95	$100	$5
Jason	Ops / Mkt		VP		$220	$200	Overpaid
Lafayette	Ops / Mkt		Senior		$130	$140	$10
Alcide	Ops / Mkt		Junior		$75	$80	$5
Jessica	Ops / Mkt		Junior		$70	$80	$10
Sam	Ops / Mkt		Junior		$79	$80	$1

Step 2: Get leadership approval

Get leadership approval to roll out comp plan
To successfully conduct 1-5 below, use our tool.

1. **Meet with senior leadership** and share the results of your compensation planning.
2. **Start by reprising your planning process** that the leadership team charged you to undertake.
3. **Share the benefits of the compensation plan** through specific examples from analysis at your company – especially if you expect resistance to the plan.
4. **Share how the plan will impact the company**.
5. **Get leadership's approval for the plan** going forward and the salary adjustment before sharing.

Step 3: Run all-hands meeting

Run all-hands meeting to share comp plan: To roll out the changes, schedule an all-hands meeting to explain changes to the team. Be transparent with the reasons for the change, your process, and the data you used to implement this process by using this tool.

Compensation Plan Presentation Template to entire company:

Today we want to explain and roll out a new compensation plan.

- In this meeting you'll learn the what, why, and how – and some of the details – behind the plan.

The "What"

- Simply put, a compensation plan is a formula that standardizes what employees make.
- We want to pay everyone a reasonable salary, but everyone's biggest opportunity is to make company equity as valuable as possible.
- Done right, a compensation plan will clearly explain how compensation works, and help focus everyone on building the company and increasing the value of equity.

The "Why": Without a plan, the company faces many problems.

- Compensating employees too little or unfairly means we'll lose great people.
- Leadership spends tons of extra time in hiring and dealing with one-off comp requests.
- We reward people for how good they are at negotiating, not for how good they are at their job.

- A more discretionary system means there's more room for bias.
- We're missing out on a way of systematically rewarding and focusing people on making equity as valuable as possible.

The "How"

- We started with our philosophy:
  - We don't want to pay people the most cash of any company, but we need to take care of people and want you all to earn a lot when we sell or IPO.
  - For us, this means paying everyone a market rate salary (for tech jobs in the Bay Area) plus significant equity upside, for your roles.
- For each function, we researched comparable salaries, and set a target at [median] for startups in our area at our same stage.
  - We used [INCLUDE DATA SOURCE].
  - We'll share more later, but here's what it looks like for a few roles.
- Then, we created an equity rubric that translates what value equity employees should get as a % of salary.
  - For example, if someone earns $100K in cash and gets $50K in equity, the ratio is 50%.
  - [Explain process. We first started with recommendations from VCs, then researched comparables on AngelList and adjusted for our area and philosophy, then verified it with our investors and HR advisors.]
  - [Share the rubric.]
- We calculate your actual ownership stake based on the company valuation around the time you join.
  - [Explain how and when you recalculate the valuation -- e.g. every financing, every year, every quarter].
- We also plan on letting people sacrifice up to [XX%] of their salary for increased equity.

- As a result, salary is set based on your role, while equity is based on your salary, your roles equity/salary ratio, your choice, and the company's risk (valuation).

At this point, you're probably wondering, "What about raises?" For now, there are two ways to get more salary and three ways to get more equity.

- Salary
  - Market increases. Every [DECEMBER] we will review market pay for our jobs and adjust everyone to keep up with the market.
- Promotion
  - We're growing fast, so so a job, get promoted, and you earn market pay for your new role.
  - When you're promoted, you'll also get more equity. All employees will be brought up to the level required for that role today. For early employees who already have more than that level, they'll receive the the difference between the new and old position (e.g. if new has $100K and old has $40K, they get $60K).
- Equity
  - Retention. All employees will receive additional equity each year, starting at 2.5 years. This will be proportional to what you would earn if hired at that time. So if you'd get $40K vesting over four years for being hired, each year you'd get $10K vesting over four years.
- Performance.
  - Every [DECEMBER] we'll review group and team performance for the entire company. People who've made a truly exceptional contribution -- typically around 5-10%, but we hope it's much more -- will receive bonuses worth the equivalent of [1-2X] their retention grant. Employees are eligible for these performance bonuses after two full

years at [the company].

- **For everyone, the best way to increase compensation is to make the company as valuable as possible.**
    - As of our last formal valuation, the company was worth [X].
    - Since then, we've accomplished [insert movement in KPIs linked to company value], an average improvement of [XX%] across valuation metrics, suggesting a value of [YY].
    - Each of you is working on something that ties directly back to these core metrics and the company value [List examples: building the product, acquiring customers, increasing retention, improving support, etc.].
    - So, while everyone is paid well, the way to earn a lot is to do all you can to help us succeed.
    - If we all keep working smart and hard, equity will increase by [4X] every four years.
- **What next.**
    - For people currently below market, we'll be adjusting you upwards.
    - [For the few people above market, we won't be adjusting you down, but we also won't be providing a market adjustment right now; your manager can discuss ways for you to grow your responsibility and earn more in the future].
    - Expect an email sharing the overall plan, your updated salary information, and the ability to schedule time to discuss with [HR] if you have any concerns.
- **Questions?**

Process: Structuring incentive-based bonuses

Bonus Plan Type Cheat Sheet

Use this email template to share bonuses.

Discretionary Bonus Plan	• One-time bonus based on most flexible criteria. • Best for early stage companies.
Spot Bonus Plan	• Ad-hoc bonus given based on pre-set bonus tiers. • Best for early stage companies.
Milestone/Project Payout Bonus Plan	• One-time bonus for milestone achievement. • Best for early to growth-stage companies.
Profit Sharing/Gainsharing Bonus Plan	• Annual bonus plan based on revenue growth. • Best for later growth stage companies.
Annual Incentive Bonus Plan	• Annual plan for all employees. • Best for mature-stage companies.

Overview

This article outlines the following steps for selecting and structuring incentive-based bonus plans:

1. Select bonus plan structure
2. Set budget
3. Determine who is eligible
4. Select goals, metrics, and timeframes
5. Determine payouts above/below target goals
6. Communicate bonus plans to participants
7. Tie bonus plans back to the bigger picture

Step 1: Select a bonus plan structure in accordance with your company needs

	Bonus Plan	Overview
Early stage	Discretionary Bonus	• One-time bonus based on most flexible criteria • Suitable for early stage companies who need to incentivize employees while budget is in flux. • Biggest compliance risk. • Not recommended for long term use.

	Spot Bonus	• Ad-hoc bonus given retrospectively. • Based on pre-set bonus tiers. • Slightly more structured than discretionary bonus. • Requires minimal budgeting.
Early to growth company	Milestone/ Project Plan	• One-time bonus rewarding milestone achievement • Suitable for early to growth-stage companies with available budget to reward select high-performers and teams based on immediate results.
Growth company	Profit Sharing/ Gainsharing Plan	• Bonus pool is % of total yearly profit. • Payout based on salary level. • Ideal for growth-stage companies seeking to align employees with revenue goals.
Mature company	Annual Incentive Plan	• Pre-set goals. • Pay out is % of salary. • Ideal for late growth-mature companies looking to create collaborative, inclusive environment.

Step 2: Set bonus plan budget

Use this bonus plan calculator for each type of bonus plan alongside these best practices below.

Best practices

1. Ensure that money invested in bonuses is within budget and with realistic expectations. First consult with your leadership or finance team for budget approval, then consult with managers of team members on the bonus plan to ensure payout amounts will actually motivate employees.
2. Set aside the bonus plan budget in a designated bank account during the start of the bonus period. There are two ways of incurring revenue for bonus plans: either a) amassing revenue from a pool you hold in reserve or b) structuring bonuses around goals that drive enough revenue to fund the bonus payouts.
3. Determine whether payout amounts will motivate employees once you've set your budget and established payout amounts. See table below for payout guidance per plan:

Bonus Type	Payout Guide
Discretionary Bonus Plan	• Payout set entirely by discretion of company.

Spot Bonus Plan	• Plan may be entirely discretionary, or utilize a plan framework that outlines tiers of spot bonus payouts with more impactful projects earning larger spot bonuses. • Usually funded from preset spot bonus pool; company will need to set target amount of utilization and manage use (e.g. inform managers who are under/over utilizing the program). • Reward amounts typically remain the same for all employees, although tier framework may scale payout, for example:Tier 1 rewards work impacting team level: $500Tier 2 rewards work impacting department: $1,000Tier 3 rewards work impacting company: $2,000Reward sizes can range from $50-$10,000 although commonly set between $250-$5,000
Milestone/Project Payout Plan	• Plan typically specifies set payment amount (e.g., $X) tied to completion of project. Possible to vary payout depending on speed/quality of project completion. • Reward amount varies based on impact of project and compensation level of eligible employee(s); typically ranges around one month’s salary.

Profit Sharing/Gainsharing Plan	• Profit-sharing. Bonus payout commonly aligns to salary level in the organization. • Gainsharing. Bonus payout commonly set as the same % of salary for all employees. • Comp-to-comp method. Calculate percentage of employee's salary as a % of total base salary spend in the company; payout this same % of the total bonus pool to the employee.
Annual Incentive Plan	• Target bonus payout commonly set as a percentage of salary. • Typical to vary percentages based on level in the organization:Lower-level roles commonly start around 5-10% of base salary target bonus.Mid-level roles commonly earn around 10-20% of base salary target bonus.Senior-level roles may earn 20-30% of base salary target bonus.Executive roles may earn 30-100% of base salary target bonus.

4. If target rewards are too small to be effective, increase the budget or narrow eligibility to reserve funds for a smaller number of employees most critical to the goals you've established.

5. Choose a strategy for determining how to allocate the bonus budget according to desired distribution. Determine whether to use Top-Down or Bottom-Up by consulting the table below.

Top-down	Bottom-up
Set a budget, then work out how to split the pool.	Decide who will participate, target payouts, and then add up the projected cost.
• Company budgets $100,000 for bonus pool. Sets eligibility as all employees participating, eligible for 10-20% of salary target bonus depending on level. • This calculates to $150,000 target spend, so company re-evaluates and decides to compromise. • Increases bonus pool to $125,000 and reduces eligibility to mid-level employees only.	• Company designs spot bonus program with target for 30% of employee population receiving an award averaging $1,500 per year. • This calculates to $45,000 target spend. • Company decreases target population to 25% of employees receiving spot bonus annually and lowers average award amount to $1,000 for a target bonus pool of only $25,000 needed.

Step 3: Determine who is eligible

Bonus eligibility depends on use-case of the incentive program and the budget.

- Limit eligibility to employees that have an impact on a goal you've established.
- Broaden eligibility if you are incentivizing and rewarding overall company performance.

The broader the eligibility, the more it will tie into an inclusive company culture that rewards shared success.

Avoid the “peanut butter” mistake. This happens when budget is spread too thin across a wide group, making the incentive less effective. Be sure your budget/eligibility pool allows for the target bonus amounts to be meaningful, especially if you are incentivizing outstanding performance for a select group of employees.

Step 4: Select metrics, goals, and timeframes

Isolate which type of metric, or broader goal, you want to incentivize.

- Financial goals (e.g., grow revenue).Operational goals (e.g., reduce operational costs, product defects).Qualitative goals (e.g., improve environmental/social sustainability).

Select three metrics to focus behavior on top priorities.

- Too many metrics dilutes the incentive for top priorities. Too few metrics may overly incentivize one area. For example, if your plan only rewards revenue growth, employees may not have enough incentive to invest in R&D for future products.

Pinpoint the specific goals and timeframes for eligible employees.

- Most broad-based plans use an annual cycle, but if goals are difficult to set one year out or there’s a need for more frequent payouts, choose quarterly or biannual.

Use your metrics to build out specific goals tied exclusively to the timeframe for the current bonus cycle.

- For example, if your metric is revenue growth, then the goal for the current bonus cycle may specify growing revenue by X% by the end of the fiscal year.

Step 5: Bonus payouts below/above target

Some bonus plans can be all-or-nothing: either the bonus pays out in full if the target is reached or nothing at all if the target is missed.

- All or nothing. Situations where this approach is applicable is to win/loss goals (e.g., when your company either wins or loses a bid to work with X).
- Threshold payouts. Performance goals (e.g., goals where the performance is separable from a binary win/loss) allow leverage for threshold payout. These options include:

Option 1: Plan leverage	• For situations where performance outcomes may vary. Plan leverage will allow for partial bonus payouts for performance falling short of the full goal and/or providing additional compensation for performance exceeding the goal. • This helps to keep employees motivated near the end of the performance period if it is clear they are either falling short of the target and can still be eligible for a partial bonus *or* if they have already met the target goal they have an incentive to keep working for additional payout.

Option 2: Minimum performance threshold	• For situations where partial performance is rewarded (e.g., performance must hit 50% of full goal for any partial bonus payout). Typically, these range around 50% to 80% of the target goal and use a linear scale for payout between the threshold and target (i.e., meeting 50% of target goal pays out 50% of target bonus, 51% of target goal pays out 51% of target bonus, etc.). • You can decide to include a minimum threshold or a maximum cap to reduce budget liability (e.g., payouts cannot exceed 150% of the target bonus).
Option 3: Maximum performance threshold	• For situations where there is a need to cap liability on bonus spending for the company. • Less common than minimum thresholds, but typically range from 125% to 200% of target.
Option 4: Linear scale for payout	• Also typically used (e.g., 101% percent of target performance pays out 101% of target bonus).

Step 6: Communicate the bonus to participants

The best-crafted incentive plan will never be successful unless plan participants understand and are invested in it. This step requires you to communicate with employees expected to receive bonuses:

- Goals the employees need to achieve?

- Expected bonus payouts?
- Timeframe?

If you have a broad-based annual incentive plan, you will need to create a formal plan document that puts in writing the details of the document with plan participants. This plan document should include:

- Plan participant eligibility.
- Metrics and goals.
- Performance period.
- Target bonus amounts.
- Leverage/payout ranges (if applicable).

Download the template for sharing bonus plans with employees. Paste and edit plan details from the bonus calculator template as needed. For more individualized or discretionary bonus plans, there is no need for a formal bonus plan document. However, it is a best practice to put into writing the understanding of any preset goals and payout expectations and share with the bonus plan participants.

Step 7: Tie bonus plans back to the big picture

Use the opportunity of communicating bonus plans to remind employees:

- Where is the company heading.
- What is their role in making this happen.
- How do the goals in the incentive plan align to the overall long-term company strategy.

A good bonus plan will reward performance that drives company success. Use your bonus plan to motivate employees and reward them for their impact on the company's success.

Annual incentive

What it is	• Structured bonus plan that sets goals at the start of the performance period (e.g., one year) and usually pays out as a percentage of salary based on the performance of the preset goals.
Advantages	• Incentivizes employees to achieve preset goals. • Creates a sense of teamwork with shared incentive goals. • Consistent plan used for multiple employees. • May be consistent plan for long-term use. • Formulaic payout (with option for discretionary component). • Easy to communicate payout expectations to employees.
Disadvantages	• Requires pre-set goals; less flexibility for change during performance period. • Formulaic payout may not account for unforeseen situations.
When to use	• Company is able to set goals in advance with low probability of those goals significantly changing during performance period. • Multiple employees participating. • Seeking structured plan with less discretionary reward.

Examples	- Plan offers a target bonus of 15% of salary based on revenue growth goals; target revenue growth is 10% by year-end and plan will pay out 100% of the target bonus if that number is met or exceeded. - Plan offers a target bonus of 10% of salary based 50% on net profit growth and 50% individual performance; 50% of the target bonus will pay out if net profit goal is met or exceeded and the other 50% target bonus payout will be subject to manager discretion at the year end determining individual performance for the employee.
Payout guidance	- Target bonus payout as a percentage of salary. - Vary percentages based on the employee's level in the organization:Lower-level roles commonly start around 5-10% of base salary target bonus.Mid-level roles commonly earn around 10-20% of base salary target bonus.Senior-level roles may earn 20-30% of base salary target bonus.Executive roles may earn 30-100% of base salary target bonus.
Other notes	- Possible to do shorter / longer timeframe (e.g., 6-month). - Typically based on company-wide performance goals but possible to incorporate department/team/individual goals. - Common to have some component of individual performance in addition to company-wide goals. Higher level employees will have bonus payout weighted more heavily to company-wide goals as

	they have more influence on company-wide performance. Best practice is to calibrate individual performance payout by having managers meet together to discuss scores for individual performance and agree on final outcomes as a group.

Profit sharing/gainsharing

What it is	• Direct sharing of company profits or other operational improvements with employees; creates a payout pool based on a predetermined formula.
Advantages	• Self-funded plan as payout only occurs if company earns enough profit and/or operational gains. • Direct incentive to reward company profit/gains. • Creates a sense of ownership and impact for eligible employees. • Creates a sense of teamwork with shared incentive goals. • Consistent plan used for multiple employees. • May be consistent plan for long-term use. • Formulaic payout easy to communicate payout expectations to employees.
Disadvantages	• No discretionary component. • Formulaic payout may not account for unforeseen situations. • No reward for individual performance.

When to use	• Company is profitable and/or able to reasonably predict effect on profit with operational gains. • Multiple employees participating. • Seeking structured plan with no discretionary reward.
Examples	• Plan reserves 20% of annual net profit for the profit sharing plan pool; that pool is paid out at year end to employees. • Plan reserves 20% of the savings from operational cost-reduction initiative; pool is paid out at year end to employees.
Payout guidance	• Pool typically shares 10-50% of profit/gain with employees. • Profit sharing: Bonus payout commonly aligns to salary level in the organization.Comp-to-comp method: calculate percentage of employee’s salary as a % of total base salary spend in the company; payout this same % of the total bonus pool to the employee. • Gainsharing: Bonus payout commonly set as the same % of salary for all employees.
Other notes	• Profit sharing typically uses a one-year period; gainsharing typically uses quarterly periods; possible to do shorter / longer timeframes. • Able to add goals and/or performance thresholds (i.e., no payout unless a minimum threshold goal is met/exceeded).

	• Profit sharing plan may be used as employer contribution to employee 401k plans.

Milestone/project payout

What it is	• One-time bonus rewarding milestone achievement or project completion.
Advantages	• Directly rewards successful completion of high-level projects. • Highly customizable; often used for one-time payouts. • Preset payout plan easy to communicate payout expectations to employees; may have a discretionary component.
Disadvantages	• Not appropriate for long-term use. • Not appropriate for broad use; plan eligibility often limited to employees with direct impact on project completion.
When to use	• Not appropriate for an ongoing bonus plan; typically used as a one-time/supplemental plan compared to an ongoing company-wide bonus plan. • Commonly applied to single department/team/individual with direct responsibility for a critical project. • Direct reward for support functions (e.g., Legal, IT) that may not necessarily have a direct link to

	company financial/operational performance goals common in company-wide bonus plans.
Examples	• Plan offers one-time bonus payment of $20k to company's General Counsel for successful resolution of litigation case (payout date dependent on case closing). • Plan offers milestone payouts to small product team to reward new product launch; each employee receives $5k for successful beta launch and $10k for successful launch (payout dates dependent on launch dates).
Payout guidance	• Plan typically specifies set payment amount (e.g., $X) tied to completion of project. • Reward amount varies based on impact of project and compensation level of eligible employee(s); typically ranges around one months' salary. • Possible to vary payout depending on speed/quality of project completion.
Other notes	• Usually set for timeframes around 3-6 months; payout date usually dependent on milestone/project completion (may also incentivize faster completion of project). • May be used to incentivize meeting a tight deadline (e.g., payout occurs if project is completed before X date). • May serve as a retention bonus to incentivize staying with a project through completion.

Spot bonus

What it is	• Ad-hoc bonus usually given retrospectively to an individual or small group to reward recent performance for a specific project.
Advantages	• Directly rewards successful completion of high-level projects or other work performance. • Usually given retrospectively without preset goals.
Disadvantages	• Not appropriate for broad use; plan eligibility often limited to employees with direct impact on project completion. • Highly discretionary; no preset expectations.
When to use	• Not appropriate for an ongoing bonus plan; typically used as an ad-hoc/supplemental plan compared to an ongoing company-wide bonus plan. • Commonly applied to individual or small group with direct responsibility for a critical project. • Direct reward for support functions (e.g., Legal, IT) that may not necessarily have direct link to company financial/operational performance goals common in company-wide bonus plans.

Examples	• Plan offers spot bonus plan to employees with rewards ranging from \$100 to \$1,000; approximately 25% of employees receive a spot bonus during the year averaging \$500 each; company leadership team approves spot bonus payments each month for select individuals and uses discretion to determine reward amount. • Plan offers spot bonuses at two tiers with Tier 1 offering \$250 for work impacting the team/department and Tier 2 offering \$500 for work impacting the company. Approximately 30% of employees receive a Tier 1 award and 10% receive a Tier 2 award each year.
Payout guidance	• Plan may be entirely discretionary, or utilize a plan framework that outlines tiers of spot bonus payouts with more impactful projects earning larger spot bonuses. • Reward amounts typically remain the same for all employees, although tier framework may scale payout, for example:Tier 1 rewards work impacting team level - \$500Tier 2 rewards work impacting department - \$1,000Tier 3 rewards work impacting company - \$2,000 • Reward sizes can range from \$50 - \$10,000 although commonly set between \$250-\$5,000. • Usually funded from preset spot bonus pool; company will need to set target amount of utilization and manage use (e.g., inform managers who are

	under/over utilizing the program).
Other notes	• Awards typically subject to manager discretion with appropriate leadership approval; may also include peer nomination component. • Best used as an immediate reward for the employee(s) upon project completion.

Discretionary bonus

What it is	• One-time bonus for an individual or small group; company has complete discretion over when, for what, how much, and whether the bonus is paid.
Advantages	• Highly customizable/discretionary. • May reward specific or unexpected situations. • Directly rewards successful completion of high-level projects.
Disadvantages	• Not appropriate for broad use; plan eligibility often limited to individual or small group. • Highly discretionary; no preset expectations.
When to use	• More appropriate for lean start-ups to take advantage of plan flexibility. • Not appropriate for an ongoing bonus plan; typically used as an ad-hoc/supplemental plan compared to an ongoing company-wide bonus plan. • Commonly applied to individual or small group for

	one-time use. ● Direct reward for support functions (e.g. Legal, IT) that may not necessarily have direct link to company financial/operational performance goals common in company-wide bonus plans.
Examples	● Company offers one-time bonus to small cross-team of employees on acquisition project to incentivize/reward a successful acquisition of target organization. ● Company retroactively rewards customer service team for going beyond expectations to effectively resolve a major unexpected customer issue.
Payout guidance	● Payout set entirely by discretion of company.
Other notes	● Company may offer discretionary bonuses for select individuals (usually leadership roles) if no company-wide annual incentive plan is established yet. ● May be difficult to manage/administer if a significant amount of employees are on different discretionary bonus plans with different goals, time periods, payout expectations, etc. ● When possible, keep awards consistent between employees. You can vary payout if performance/impact differs but it is a discrimination risk if you pay two employees different bonus amount for the exact same contribution without any clear rationale for the

	difference.