



Going Beyond the Merit Matrix: How Automation Is Changing Compensation Management



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Introduction

Compensation plans should go beyond a simple merit matrix model as the main way we connect pay and performance. You can evolve the way you plan and deliver employee rewards by adopting a holistic outlook on how companies can (and should!) make pay decisions.

We know creating a strong compensation strategy is time-consuming work. And, the outcome of these strategies will definitely impact everyone at your company. Since talking about pay can be a delicate topic, try to keep a fair but competitive mindset when planning your compensation and total rewards programs.

You should also keep in mind a person's position and performance as well as your company's salary budget. To help you do these things successfully, we'll dive into how your organization can:

- Remain compliant by focusing on a fair pay structure for all employees—regardless of age, race, gender, sexuality, and other characteristics
- Take advantage of compensation management software so you can effectively justify pay raises to your stakeholders and executives

Our hope is that the following chapters give you the information you'll need to prepare a pay plan that fits your organization's unique needs.



Why Should You Automate Compensation Management?

In recent years, technology helped us keep up with business as usual while the pandemic raged on. While we've adjusted our work habits in order to remain productive and efficient, there's more work to be done. Consider this: with nearly every industry facing new hiring challenges and a shortage of skilled workers, it's an employee's market. That means you'll need to do more to attract and retain people, starting with more pay and better benefits¹.

In light of "The Great Resignation"², this might be a big ask for HR and comp teams that have been impacted by the empty roles and high turnover. Unsurprisingly, this trend also triggered a rise in automation spending³.

If these aren't good enough reasons to make the switch to automated systems, don't worry. We've got a few more to help you build a business case—one that might just convince stakeholders and compensation committees to evolve the way they make salary and total rewards decisions.

Small Mistakes Can Have a Big Impact

Human errors may not occur as often as we might imagine. However, just one mistake can end up costing a company millions of dollars⁴. In one notorious case of human error, an employee in Australia was paid more than 100 times their normal salary. What's interesting is that an audit revealed that a decimal point in the wrong place led to this overpayment. Such a simple error!

Luckily, the employee returned the money. But this does beg the question: how many instances of human error ended with a negative impact for organizations and employees? And how many of them simply go unnoticed?

¹ Liu, J. (Jan 2022). 'Economists say rapid quitting and hiring will continue in 2022 despite omicron wave'. CNBC. [Available online.](#)

² Bridge. (Sep 2021). 'The Great Resignation: 3 Reasons Your Employees Are Quitting (Plus What to Do About It!)'. [Available online.](#)

³ Andriole, S. (Nov 2021). 'The Great Resignation Will Only Accelerate Automation. Employers Will Retaliate With Machines'. Forbes. [Available online.](#)

⁴ BBC News. (Aug 2018). 'Australian Worker Overpaid by \$500,000'. [Available online.](#)

Small mistake, huge impact!

For a large enterprise employing 18,000 individuals (with an average salary of \$25,000 per year), a 1% error rate would create a loss of \$4.5 million.



Aside from the financial loss, there's also an impact to your organization's most valuable assets: your people. Employee satisfaction is key to a company's success. When people aren't happy, they don't perform at their best. This means you might notice decreased employee engagement—something that leads to low productivity.

A simple mistake—like accidentally underpaying an employee due to human error—could cause someone to lose trust in the company. This in turn might lead them to disengage from their work and ultimately leave.

Reduce the Potential for Human Error

It's safe to say that human error will never disappear completely. Still, it's important for business leaders and executives to provide HR pros with tools that reduce the potential for it. When performed by humans, data entry has an error rate as high as 4%⁵, especially when there are no verification layers included in the process.

Looking at this from a different angle, you might want to think about employee burnout and its influence on human error. When we're tired, it's easier to lose focus on our work and make mistakes. It's an inevitable truth that we've all felt throughout the pandemic. Compensation software can help your HR teams perform simple (yet time-consuming) tasks in a more efficient and effective way.

And, with less risk for human error.

⁵ Hougie, M. (Apr 2019). 'Human Error: 8 Eye-Popping Sets of Stats and Examples'. Oculous. [Available online.](#)

What We Mean By ‘Going Beyond’ the Merit Matrix

The merit matrix is a grid that helps HR compensation professionals and managers calculate salary increases. It was created to help people make data-driven decisions about when (and how) to give pay increases. It’s also a core component of PeopleFluent’s compensation management solution as it helps automate calculations based on criteria that’s entered in by users. However, we do recommend using additional data elements when using an automated compensation tool like ours. More on that later...

A classic merit matrix typically only considers an employee’s performance rating when determining performance-based salary increases. You’ll need more than just that template to make objective, data-driven pay decisions. That’s because the kind of merit matrix outlined above is based solely on the manager’s perception of that employee’s performance. Consider the following:

- 1** Employee performance is based on empirical data—a challenging task for junior managers. Even for seasoned managers, these decisions are tough to make without the ability to [compile performance metrics](#). After all, how can a manager use their discretion on a person’s performance when there are few opportunities for in-person observations?
- 2** It is dependent on knowledge of how competitive an employee’s salary range is compared to the current market rate for a specific role.

If managers don’t fully understand what needs to go into the matrix boxes—and you lack a solution capable of automating calculations—the margin for error can be high.





You'll Need More Than a Merit Matrix

The merit matrix, on its own, won't allow managers to account for the real-life scenarios and variables that exist when making performance-based salary decisions. That's why it should be used alongside an automated compensation solution that offers deeper compensation analytics. These insights can be used to measure an employee's performance, contributions, and business impact. Plus, you can use it to make the rewards planning process much simpler.

Without this kind of data, planning and delivering a large merit pool (with only two factors considered) isn't going to sit right with a Board of Directors. What's more, it isn't fair to the managers responsible for deploying these funds. Ultimately, this exercise should ensure that the money gets to the right employees, at the right time. It's also another way to make sure your organization isn't overspending millions during the salary administration process.

In theory, the merit matrix might be a well-intended starting point as a pay-for-performance model. In reality, you'll need to include some other factors and data points that allow your organization to show the value it places on employee performance—without focusing on merit alone. Those are:

- Loss impact
- Market conditions
- Internal equity

Managers need hard facts and data when approving a salary increase. To be explicit: a compensation committee (and the company's Board of Directors) will expect your compensation plan to be both fair and transparent. If you're going to use the merit matrix, you'll also need to include the other data elements.

Additional Data Elements to Include

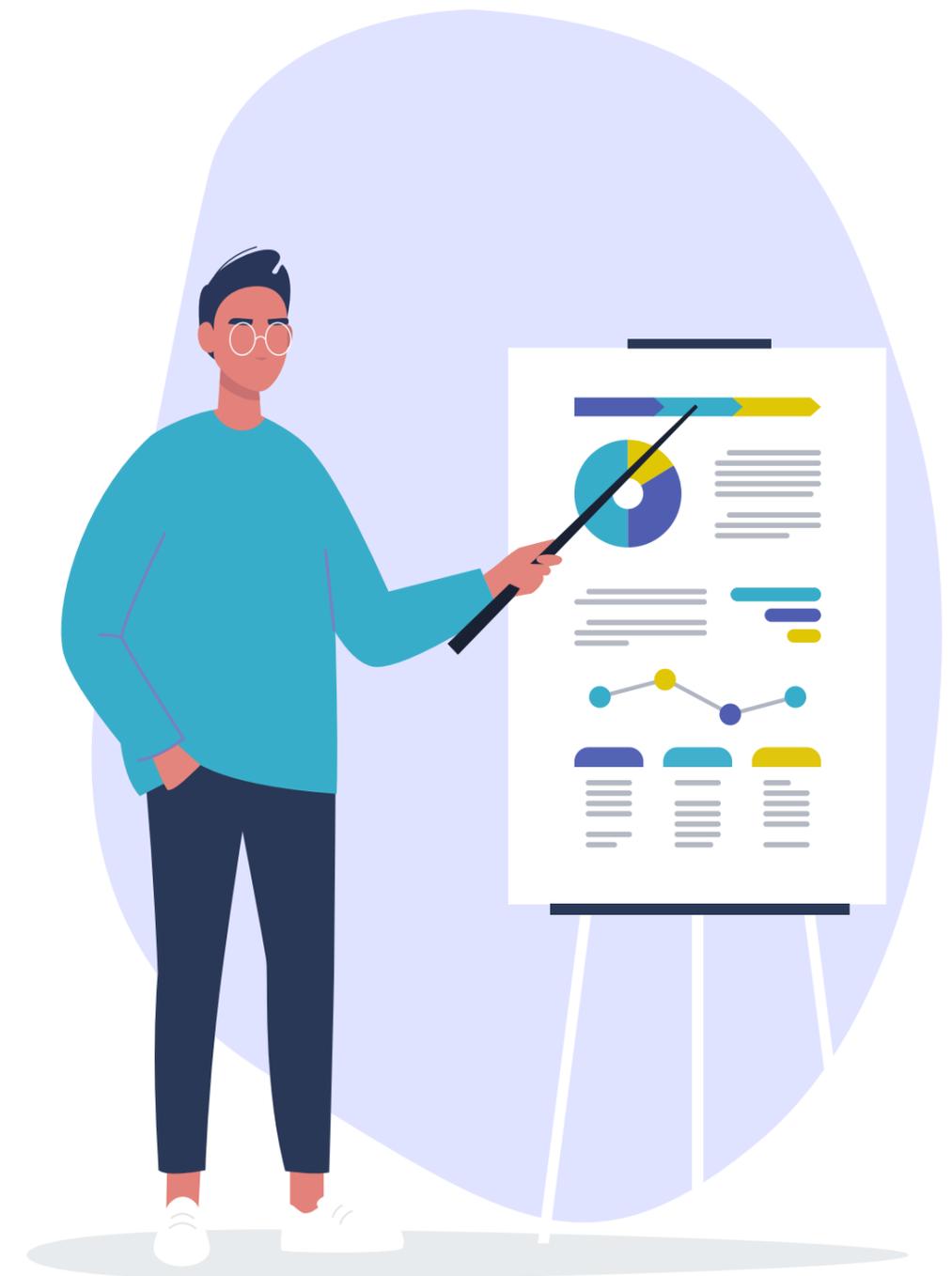
With the right data, you can identify and fix errors or inconsistencies. This gives you the chance to update your approach and train your managers to focus on the data. Keep in mind, a compensation management tool will use the information that users enter in. This could open up a new learning opportunity for managers who aren't entirely sure what elements they need to use.

Overall, the process will be simpler than if you only relied on manual processes. A compensation tool will automate the entire process and make recommended increases based on what it shows on the merit matrix worksheet. In addition to using a merit matrix, you should be using these additional data elements:

- **Loss impact** gives leaders a deeper understanding of how a specific position generates revenue for the business. This includes how productive the individual is within that role and the costs associated with their position. Managers should also understand how difficult it would be to replace an individual and the complexity of their role compared to other positions.
- **Understanding market conditions** will give you an awareness of average salary trends for various roles. In the event your organization's increases are below or above the market rate, you have an opportunity to justify and correct any discrepancies.
- **Internal equity** is another key factor as it helps you make sure salary increases are given to employees whose skill set and level of performance are comparable to others with a similar position in the company.

Our opinion is that the mathematical elements should be the guiding force when designing your pay distribution model, something the merit matrix is great for. Every industry and company will have its own unique culture and values, of course. But the ultimate goal is developing a fair and equitable distribution model that's rooted in data.

Lastly, the model you decide on should be easy to adopt and should make delivering salary increases an easier process for managers.



How to Develop a Structured Compensation Planning Process

As we mentioned earlier, pay increases should be driven by a specific set of data elements. Lean on your compensation managers and/or HR business partners for recommendations on which data elements are necessary. Ideally, this should happen before your managers get involved and start making salary decisions.

Of course, business leaders will need to offer continued training and education for their managers wherever necessary. Otherwise, managers might only rely on guidelines and/or systems to the best of their knowledge and experience. This also creates a great opportunity to identify and explain how an automated tool might help overcome any gaps. And, it gives leaders a better understanding of what training opportunities may be needed.

Once your top-level management has been trained on how to use the distribution model, managers will have more freedom to use their discretion. Of course, this should only happen after the specified datasets are gathered and understood by decision-makers.

Don't Ignore Manager Input

Salary and rewards can't just be based on data and mathematical calculations. Leaders need to gather and consider manager feedback on individual employees. It's impossible for an HR business partner or a compensation committee to know every person in the organization, much less how they perform. Manager input—along

with data compiled from HR systems—can help you develop a comp strategy that is easily tracked, managed, and reported on.

Leaders may also be concerned about the potential for budget misuse. That's to say, interpersonal relationships between employees and their line managers could create biases. This is where managers can lean on data points when evaluating performance. It also lessens the risk of unfair pay practices, perceived or real. Managers should encourage people to develop their own objectives and goals. Performance can then be assessed by how well an individual performed based on the expectations they set for themselves.

If your salary increases are directly tied to performance, your managers should have a central location where they can add feedback on a regular basis. This includes formal and informal feedback as well as quarterly and annual performance reviews.

It's a good practice for many reasons. First, it helps employees understand how ongoing feedback is tied to development. Second, it gives them tangible proof that their annual review is tied to compensation and rewards. When people see where they are in the development process—and how they're performing—they can find opportunities to upskill or reskill themselves.

There's no question that manager input is essential and valuable for making compensation decisions. Even still, you need a consistent and structured approach for identifying the proper data elements.

The Benefits of Automating Compensation Management

As you get closer to making a change and switching to automated tools, you'll need to identify the benefits of doing so. This will help down the road when you're ready to build a business case for change. Here are three benefits we've identified to help you get started.

1 You'll Have Centralized Compensation Data

Onboarding any HR technology system is tough, but it's highly recommended that you encourage user adoption early on. A central system that gives users easy access to the necessary data and makes their job easier will increase the likelihood of user adoption. It'll also help you efficiently move away from manual, legacy processes that are bogging down your HR teams.

Keep in mind, compensation teams are responsible for sending government-mandated reports. They compile these regulatory reports using multiple data sources, increasing risk and leading to decreased efficiency. A central hub that houses your compensation data will help line managers and business leaders gain the real-time visibility they need to be proactive.

2 You Can Make Agile Compensation Decisions

We get it. Creating and sticking to an agile workflow can be tough to get right while everything remains in flux, especially when business decisions require feedback from multiple stakeholders. For example, data points such as compa-ratio and PIR, which are generated from informed market data, can help a manager to decide whether an employee needs an adjustment to minimum or a lump-sum award if the employee is over the maximum range. This can also lead to cost savings for the organization as a whole. Having a more comprehensive understanding of employees' salaries and how they compare to market averages can help you determine where and how to best spend your budget.

An automated compensation tool that sends out alerts and guidance can help remind managers and provide decision-makers with the data they need to finish compensation decisions. HR teams can immediately react to changes that affect compensation—think: organizational structure, data sources, or performance measures—and plan accordingly.

3 You Can Keep Information Secure With Data Integrity

It's more important than ever to keep confidential information secure—a big challenge if you're only managing compensation with spreadsheets. That brings us to the topic of data integrity: the maintenance of, and the assurance of, data accuracy and consistency over its entire lifecycle. Data integrity is a key part of the design, implementation, and use of any systems responsible for storing, processing, and retrieving data⁶.

Recommended reading

Click here to learn how **managing compensation with spreadsheets** can put your business at risk.



Without the proper controls to track and manage your company's compensation data, it's difficult to prove compliance—not a good look when government officials get curious. Things aren't standing still: the list of requirements continues to grow as new mandates are implemented across the US⁷. Managing compensation with spreadsheets can expose your organization to significant compliance risks, such as:

- Errors that go unchecked may not be detected until there's an audit by the Office of Federal Contract Compliance Programs (OFCCP). Human error is especially likely when users are less confident using the templates
- You're more likely to be unable to prove consistency across pay grades because you'll be using multiple data sources across departments and systems

Here's another thing to consider: when you have a large number of spreadsheets moving around the company, it increases the risk of a security breach... especially when a majority of employees are working from home. Now's definitely not the time to neglect data integrity. Make it a focus throughout the compensation planning process.

Start with a deep understanding of how your company's private information is managed and stored. This helps your organization develop the necessary controls (if they don't already exist) and record-keeping capabilities.

⁶ Wikipedia. 'Data integrity'. [Available online.](#)

⁷ Seyfarth. (2020) '50 State Pay Equity Desktop Reference: What Businesses Need to Know About Pay Equity Laws'. [Available online.](#)

Building Your Business Case

Sure, you might have your work cut out for you when it's time to convince leaders that you need new software. Expect (and plan ahead for) pushback. When you're ready to meet with decision-makers, be sure to include and present these benefits of a compensation management tool:

- Cost savings to the organization
- Time and error reduction
- Real-time access to centralized compensation data
- Automating simple tasks, e.g. spreadsheets
- Immediately reacting to changes that affect compensation (e.g. organizational structure, compensation plans, performance measures, and data sources)
- Securing the organization's confidential information

Who Should Facilitate the Change and How?

Your business case should be thoughtful, concise, and fueled by data. Be sure to identify who'll be responsible for auditing the existing compensation planning strategy. Ask your HR leaders to sit down with executive leadership and use this time to outline why the current approach is flawed—and why a better system should be developed.

Once you've audited the current process, get ready to ask for leadership's support. Change management that's supported from the top down is way more impactful. Plus, it helps you build employee trust. You should also consider input

from members of your junior and senior management teams. Don't forget to include feedback from your HR business partner and executive teams.

If you're looking for a link between pay and an employee's promotability—one of the data elements to examine before a salary increase is approved—leaders should ask questions like:

- **Is the individual assigned to critical projects?**
- **What is their track record when working with peers or managers?**
- **How quickly are they developing?**
- **Should there be a program established to help develop them?**

Salary decisions that are based on performance can be a strong motivator for employees. As long as you can justify these decisions when the time comes, you're on the right track. The takeaway for leadership is that an automated compensation tool will give your managers a better way to balance the empirical data with the hard data points they've outlined at the start.

About PeopleFluent

As a market leader in integrated talent management and learning solutions, PeopleFluent helps companies hire, develop, reward, and advance a skilled and motivated workforce. Deployed separately or as a suite, our software spans [recruitment](#), [talent mobility](#), [performance](#), [compensation](#), [succession](#), [org charting](#), and [learning](#)—tailored for either large or mid-enterprise organizations. We deliver unmatched functionality and flexibility, recognized by leading analysts, to develop people, drive performance and deliver results.

Our talent solutions unify talent processes within a collaborative experience that enables HR and L&D teams to guide managers and employees with contextual learning—right in the flow of work.

A part of [Learning Technologies Group plc \(LTG\)](#), PeopleFluent provides world-class service and an unparalleled ecosystem of partners to optimize employee experience, employer brand, and business results.

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