

# **NON-PROFIT TOTAL REWARDS STRATEGY: EARNING YOUR RETURN ON INVESTMENT**

BY MARC KROLL, MANAGING PRINCIPAL  
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As a result of the slow growth economy, non-profit organizations are facing decreased funding due to federal and states' fiscal deficits as well as a significant shift with grant-makers who are increasingly funding awards on a performance/return on investment basis. In addition, the soaring costs of healthcare insurance are adding significant pressure to operating costs. Without new revenue growth, many non-profits are looking for ways to measure and increase the value/return on their social mission and investments. Consistent with these changes, some non-profits are responding by trying to increase the "return" on their services and programs in terms of program execution, utilization, and measurable results. Given this environment, non-profits are being forced to examine the viability of their highest cost centers, most particularly, employee compensation and benefits for value against performance as well as market competitiveness.

Non-profit Boards and senior management are questioning what the appropriate compensation and benefit programs should be, at what levels they should be funded, and how to drive accountability and performance in the employee workforce. While non-profit organizations have predominantly been about social service and charity with their cultures reflecting a "do-good" environment and a concern for employee welfare, present conditions have forced many to consider a culture shift toward performance and accountability as well as changes in their Total Rewards programs. This delicate balancing act between affordability and the ability to attract and retain a stable and talented workforce presents challenges in nonprofits' capacity to assure effective organizational culture, management practices, labor market relevance, and strategic/operational priorities. To help navigate this challenge, the following insights to six key questions provide a prescription for change in Total Rewards:

## **1. *What should your Total Rewards strategy be?***

This is a statement developed by your Board or management committee on how the organization's compensation and benefits programs will support and relate to your operational objectives, culture, management practices, and employee performance. It also describes both the labor market within which the organization wishes to compete and the level at which both compensation and benefit programs will be set and funded.

Until quite recently, typical non-profit Total Rewards strategies have been to set benefits at more competitive levels than pay. Many organizations believe that this has worked as a successful attraction and retention strategy for a more experienced workforce and "fits" with their culture of "giving back" by helping both employees and their families.

However, with significant, steadily increasing benefits costs (healthcare being the leader) and with pay levels now also starting to escalate at a steadier pace since the Great Recession, many non-profits

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are critically assessing what is affordable and more productive for their pay and benefits programs at a time of declining or plateauing funding.

## **2. *What is the present role of pay and benefits in your organization's management practices and culture? Does the Board or management committee want to change that role?***

Any organization contemplating Total Rewards' plan changes should assess their salary, incentive compensation, executive perks, benefits, and recognition programs on two levels.

The first consideration is the work culture needed to support the achievement of your operational strategy.

- Does your organization value team or individually-driven contribution and performance or a combination of the two?
- To what degree and why should it value differentiating performance between individuals or treating employees the same?

Second, how will this shift impact how managers engage and communicate with their staff on various challenges?

- To what degree and how does your organization want to emphasize performance and accountability?
- How can we best tie performance management and career advancement to compensation decision-making?
- How can your Total Rewards strategy fit your strategic mission and goals to move your organization forward amidst your funding and development challenges?

To ensure that any changes in a Total Rewards program will not have an adverse impact on your workforce, it is critical that management and staff have the opportunity to “weigh-in” on the role that culture and performance management play in the design of both the structure and objectives of Total Rewards programs. This can be achieved through interviews, focus groups, and/or surveys.

## **3. *How do you determine the appropriate mix of pay and benefits for a non-profit organization? How do you determine whether it is “affordable?”***

Understanding the factors which determine the right menu of compensation and benefits is imperative to maximize the return on your Total Rewards investment as well as attract and retain a talented workforce.

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The financial, operational, and cultural environment that is particular to non-profit organizations plays a critical role in influencing decisions on the breadth and depth of a Total Rewards program and should be carefully considered.

## Financial

For non-profits, profitability is not a measure of financial success. However, grant-makers and donors (public and private) use administrative cost as a percentage of total revenue to determine potential recipient organizations. This is a measure of efficiency on how non-profit organizations measure their “return” on the dollars they are given. For several organizations we have consulted to, compensation and benefits is the most significant cost in this calculation. An organization needs to either increase its revenue streams or constrain/reduce cost in order to show performance improvement. At present, with declining funding, the review of compensation and benefits programs is just a logical next step in this process.

Second, non-profit compensation and benefits programs can significantly be impacted by the source of their funding. There are many public or private funding opportunities (grants) that frequently contain conditions specifying what specific service the funding will be used for, recommended salary levels, and potential operational requirements. Planning a Total Rewards program and its funding may be a challenge if the organization is trying deliver a consistent message to its workforce.

Although government funding has been a staple of many community organizations, in recent years these sources have proven to be less generous in the delivery of similar levels of funding. The condition of the economy and government budgets being the main determinants. Private funding, although experiencing similar challenges, has one significant difference: several organizations, with the help of donor support have created investment portfolios that generate additional streams of funding. This can create significant financial leeway when determining both grants, services, and a more attractive Total Rewards program.

## Operational (Human Resource Planning)

Depending upon the non-profit’s mission (e.g. community foundation, community services, higher education, healthcare), the nature of jobs within a workforce and their market-competitiveness may dictate how aggressive a Total Rewards program will have to be in attracting and retaining talent. The professional level of the work force and the minimum education and experience levels it requires, will influence both the number and funding levels of compensation and benefit programs.

In addition, key jobs that are needed by an organization may dictate a different Total Rewards strategy based on the labor market and the degree of demand for a certain skill set. A current example would be the importance of information technology (IT) to your organization’s performance. For any two

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organizations (e.g. community foundation vs. higher education vs. healthcare-based community provider) the approach to attraction and retention of IT employees could be quite different.

## Cultural

Desired work culture should influence and shape a Total Rewards strategy. As was previously shared, most non-profits have a team-oriented, collegial, employee-focused culture which is consistent with the organization's work in social services, healthcare services, and education. A Total Rewards program that has supported this culture will typically manifest itself in a richer benefits policy as compared to pay. Many non-profits believe this is the strongest strategy when trying to maximize attraction and retention of a workforce which is both experienced and looking for a "stable" work environment.

## Total Rewards Decision-Making: Strategic Integration of Factors

Designing and designating a Total Rewards Strategy and its associated programs is a "triangulation" of the above three organizational factors. That is, a nuanced balancing based on both external and internal conditions and changes that occur. Some of these changes may include:

- Constrained Funding: Cost pressure (created by decreased funding) on both the amount of spending and structure of Total Reward programs is a current challenge. In response, many organizations are restricting or not giving out an annual salary increase. In addition, the increasing cost of medical and dental programs, has left many organizations having little or no choice but to increase employee contributions to premiums and/or deductibles.
- Labor Market: The current labor market is "scattered." Specific industries and job families have higher salaries than others based on demand for their products and markets. The most significant example is information technology (IT). Attracting and retaining a talented IT workforce is an ongoing challenge in both for profit and non-profit organizations due to the lack of supply and highly competitive salary levels. Many nonprofits, dependent on IT's level of importance in their operations, have been more aggressive in setting IT salary policy in order to obtain the talent they need. These organizations have little to no choice in trying to compete if they need a specific skill set. An example of this is the recent rise of the cybersecurity job market to combat cybercrime.
- Transitioning to an Accountability-Based Culture: Connecting pay and performance is a management challenge for most organizations, let alone for non-profits. As grant funding continues to move toward performance-based awards, non-profits will have to build performance and accountability mindsets in their employees, plus align employee goals to higher organizational performance, and define metrics to elevate performance levels. Consequently, work culture will have to shift to the idea of differentiating pay based upon employee performance.

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Many non-profits are considering this change. However, several are concerned with changing their team-driven culture which is a reflection of the work they do. They continue to look for an “edge” in increasing both financial and operational results.

In setting their menu of compensation and benefit programs, Boards and management are challenged by gauging the program cost against the ability to design a successful attraction and retention policy. At present, it is complicated by decreased funding. This can be done by either reduction of compensation and benefits funding and programs or no increase in the employee workforce. Most times it is the latter. However, we suggest that this decision be weighed in terms of the number of employees needed to accomplish its mission and the cost of delivering services.

#### ***4. Have you defined the appropriate labor market to which your organization wants to compare your current pay and benefits programs?***

Comparing your Total Rewards programs to the relevant labor market is vital to determining how effective you will be in attracting and retaining talent to your organization. Senior managers, along with Human Resources, should define the industry/sector, geography, and the potential “hot jobs” that may be difficult to recruit or retain (e.g. Information Technology). Understanding labor market dynamics that impact your organization will help to choose the most effective survey data sources when it comes to assessing your organization’s position versus the labor market.

#### ***5. What are the financial and practical implications of proposed changes in your Total Rewards programs?***

Any changes in either a pay or benefits program should be financially modeled for its additional costs or savings. The first question from senior management or your Board will be the cost or savings incurred and how the organization will manage it. Second, in what ways and to what degree do these changes conform to the Total Rewards philosophy of your organization and will they make operational sense? Does this change help, hinder, or not change the ability to attract and retain a talented and motivated workforce? What is the compelling “business” rationale for the change?

A timely example might be the approach to fund employees’ retirement. The choices might include an employer-funded pension plan, a contributory plan (403b) where both employees and the organization (% match) fund an employee’s retirement, or both. More recently, several organizations we have advised have been conflicted with this decision over what and how to fund,

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given the labor market trend that most organizations offer only a 403b plan. However, several organizations have both a pension and contributory plan. Question: Is it still financially feasible to fund both? Or, does this conflict with your ability to continue to attract and retain a talented workforce.

## **6. *How will you implement and communicate Total Rewards program changes to employees?***

Clear communication of new programs or changes to programs (compensation and benefits) are essential to their effectiveness and acceptance by the workforce. Consistent messaging to employees from leaders, managers, and Human Resources with a practical (financial and otherwise) rationale for the change is critical in gaining acceptance. The approach and format of how changes are communicated will depend upon how an organization normally communicates with its workforce. Whatever works the best should be used for announcing Total Rewards changes. However, due to the complexity and emotionality of compensation and benefits issues, increased frequency and repetitiveness is advisable, as is face-to-face communication.

The “roll-out” of a new program or changes can be achieved through one or a combination of tools:

- Managerial training that supports managers communicating to staff
- “All Staff” meeting...senior management led
- E-mail communication
- Employee training

Non-Profits are trying to navigate their way through difficult funding constraints, increased demands for accountability, and increased productivity. A different, more strategic approach is needed to set and shift compensation and benefits programs to align with organizational objectives.

Compensation and benefits changes impact employees’ concerns about their jobs and their livelihoods. It is strongly recommended that your organization treat the implementation of these changes just as seriously.

Reviewing and/or setting a Total Rewards strategy and its associated programs will establish both an on-going conversation and a relationship regarding ROI and your organization’s pay and benefits programs. Given the challenges of the current and future economic and funding environment, it is vital that this happen for both financial viability and organizational effectiveness.

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