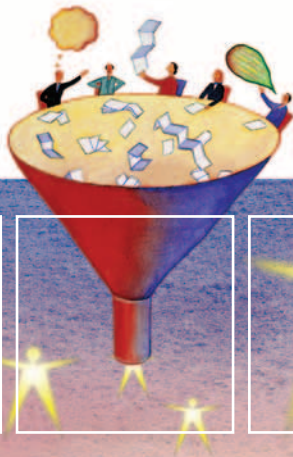


# MERCER

Human Resource Consulting

## 2005/2006 US Compensation Planning Survey Executive Summary



A Study of Pay Increases, Incentive Compensation,  
and Emerging Practices

## **About Mercer**

Mercer Human Resource Consulting helps clients understand, develop, implement and quantify the effectiveness of their human resource programs and policies. Our goal is to help employers create measurable business results through their people.

We work with clients to address a broad array of their most important human resource issues, both domestically and globally. We have specialist expertise in all areas of human resource consulting, including compensation, employee benefits, communication, and human capital strategy. Of equal importance are our investment consulting expertise and the solutions we provide in program administration.

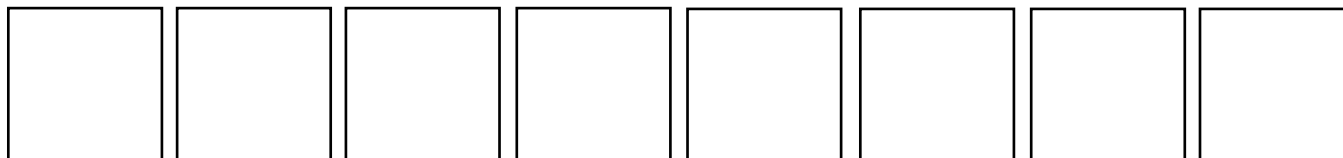
Providing high-quality human resource information has been an integral part of our business for more than 40 years. Around the world, Mercer conducts more than 600 compensation, benefit, total remuneration, and employee mobility surveys. Our software and tools help organizations align compensation and benefit programs with their strategic objectives.

With more than 13,000 employees in some 145 cities and 40 countries, we have the local knowledge and worldwide presence to develop and implement global human resource solutions.

# 2005/2006 US Compensation Planning Survey

A study of pay increases, incentive compensation, and emerging practices

## Executive Summary



Nearly 1,350 organizations provided data for Mercer Human Resource Consulting's 2005/2006 US Compensation Planning Survey. The survey data, which represents the pay practices of close to 13 million workers, supports four key findings:

- Expected pay increase budgets for 2006 will approximate 2005
- The era of salary freezes is being replaced with signing and retention bonuses
- Formal career planning is being considered by 18% of the companies as a means to develop talent
- Pay for performance trend continues with more than half of all non-union employee groups being eligible for variable pay and through greater differentiation of salary increases and incentive awards

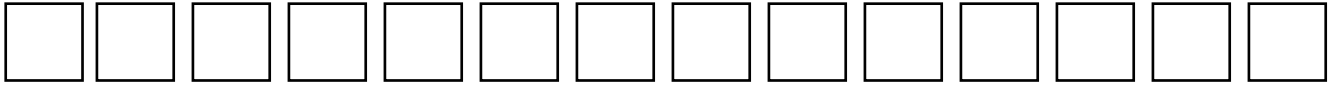
### Base Pay Increases

As the US economy begins to gain traction, organizations continue to remain cautious in their approach to pay increase budgets for 2005. **Pay increases are expected to be 3.6% for 2005 and are projected to remain constant at 3.6% for 2006.** The number of organizations reporting salary freezes for one or more segments of their employee population fell from 5% in 2004 to 2% in 2005. Structure adjustments, reported at 2.8% in 2004, rose slightly to 2.9% in 2005. Actual 2005 and projected 2006 pay increase and structure adjustment budgets follow by employee group.

	Pay Increases		Structure Adjustments	
	2005	2006	2005	2006
All Employees	3.6%	3.6%	2.9%	2.8%
Executive	3.9%	3.8%	3.1%	2.9%
Management	3.6%	3.6%	2.9%	2.9%
Technical/Professional	3.6%	3.6%	2.8%	2.8%
Nonexempt Clerical/Technician	3.5%	3.6%	2.8%	2.8%
Nonunion Hourly	3.4%	3.5%	2.7%	2.8%

Pay increase budgets within the **Energy** and **Mfg - Aerospace** industries are among the highest with 4.2% and 4.2% for 2005 respectively. **Real Estate** organizations had the greatest decrease from 2004, falling from 3.5 percent to 3.0 %.

# Executive Summary

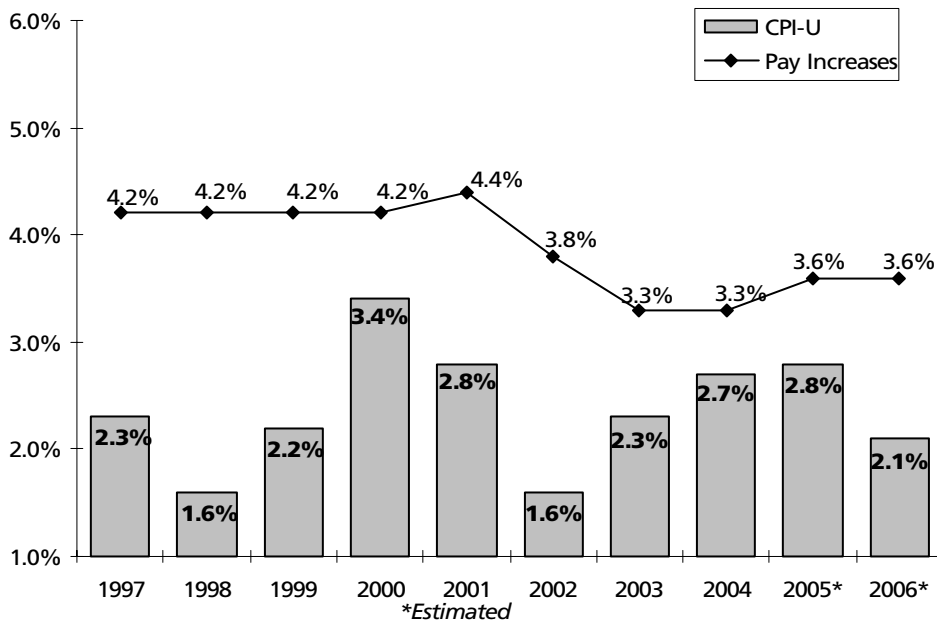


## Base Pay Increases continued

Forty percent of responding organizations indicated that promotional increases are budgeted separately from normal merit budgets. Where organizations budget promotions separately, affected employees are typically awarded approximately five to eight percent.

Projections indicate that the differential between the increase in the Consumer Price Index and employee base pay increase budgets will remain flat in 2005, continuing to reverse a trend of the late 90's where real growth over inflation exceeded 2% per year. With tightening labor markets, we expect the spread to increase reflecting labor supply and demand.

CPI-U estimates provided by Economic Forecasting Center of Georgia State University.



\*2005 and 2006 percentages include 0s and are estimates

# Executive Summary



## Attracting and Retaining Employees

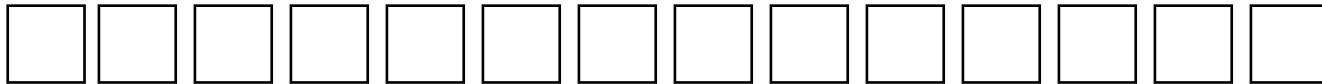
A recovering economy and growing job market are challenging organizations to focus once again on attracting and retaining key talent. Currently within the IT job family, spot cash awards are used by 82% of responding organizations, while 78% provide project milestone bonuses, and 65% offer signing bonuses. Spot cash awards are growing more prevalent in nearly every job family since last year, but seem to be most popular in Accounting & Finance (76%), Human Resources (72%), Sales & Marketing (72%), and Customer Service (70%).

Attraction and retention of top talent will become more important as labor markets become more competitive. Job families already gaining attention include IT, Accounting & Finance, Sales & Marketing, and Engineering.

The table below reflects the programs used to attract and retain employees in several functional areas.

	<b>Signing Bonuses</b>	<b>More Aggressive Pay Increases</b>	<b>Project Milestone Awards</b>	<b>Spot Cash Awards</b>
IT	65%	43%	78%	82%
Sales & Marketing	47%	22%	27%	72%
Accounting & Finance	46%	23%	26%	76%
Engineering	38%	27%	30%	53%
Other	34%	28%	20%	41%
Human Resources	31%	10%	21%	72%
Internal Auditors	29%	17%	21%	60%
E-commerce	23%	10%	16%	42%
Customer Service	18%	7%	18%	70%
Security	16%	7%	12%	46%

# Executive Summary



## Pay For Performance

Organizations continue to look to variable pay as they struggle with their ability to afford and sustain compensation levels. The percentage of companies offering short-term incentives to at least one employee group grew slightly in 2005 to 86% as more companies look to increase the variable portion of their compensation package (14% are considering adding non-management incentives with another 11% looking at adding team/small group programs). Twenty-one percent of responding organizations indicated that the number of employee levels eligible for short-term incentives has increased since 2002.

Actual (median) payouts for 2004 performance remained constant for the nonexempt clerical/technician (5%) employee group, while actual (median) payouts for executive (35%), management (16%), technical/professional (9%), and nonunion hourly (4.5%) employees increased slightly. Executives and nonexempt clerical/technicians received their target awards, management payout slightly exceeded targets, while payouts for technical/professionals and nonunion hourly lagged targets by 0.5%. Payouts for 2005 performance are expected to decrease slightly for management, but remain constant for executives and nonexempt clerical/technicians and increase slightly for technical/professionals and nonunion hourly employees.

Organizations are differentiating pay based upon performance. When asked to identify how individual performance impacts short-term incentive awards, organizations responded that individual performance drives 18% of an executive's award, 22% for management, 27% for professionals, 25% for both nonexempt and nonunion employees. When asked "What compensation investments have been implemented or are being considered", 36% of responding organizations have increased pay differentiation based upon performance with an additional 9% considering.

Participants were asked to identify the measures used to fund and distribute short-term incentive compensation payouts. Financial measures continue to be dominant in funding incentive payouts, but a more balanced scorecard that includes financial measures as well as operational, people, and customer service is used for distribution.

## Emerging Practices

As the economy finds more solid footing, organizations continue to look for ways to effectively identify and reward key contributors. Most key findings around emerging practices fall into the area of *compensation and performance management*:

- For the sixth year in a row, **non-monetary recognition awards** continue to top the chart with 70% of responding organizations offering them, while another 9% are considering doing so.
- As pay increase budgets remain low, 55% of survey participants continue to use **spot cash awards** (up 12% since 1998), and another 9% are considering doing so.
- The use of **broad-based equity (e.g., stock options)** continues to decline from its peak of 37% in 2002 to 31%, with only 1.4% of responding organizations considering implementing such awards.
- As companies look for ways to develop internal talent as a means to grow revenue, 18% are considering adding **formal career planning**, 15% are considering adding **competency-based performance management**, and 14% are considering the use of **multi-rater feedback**.

# Executive Summary



## Emerging Practices

The chart below illustrates the percentages of organizations that have and are considering implementing various programs.

Emerging Practices	Have	Considering	Terminated
Non-monetary Recognition Awards	70%	9%	<1%
Spot Cash Awards	55%	9%	<1%
Enhanced/Increased Choice for Defined Contribution Investment	41%	7%	0%
Individual Non-management Incentives	41%	14%	<1%
Competency-based Performance Management	34%	15%	<1%
Broad-based Equity (e.g., stock options)	31%	1%	2%
Job Sharing Arrangements	30%	5%	0%
Team/small Group Incentives	30%	11%	<1%
Multi-rater Feedback	28%	14%	<1%
Broadbanded Pay Structures	26%	10%	1%
Formal Career Planning	23%	18%	0%
Competency-based Pay	14%	10%	<1%
Cash Profit Sharing	16%	3%	1%
Skill-based Pay	16%	7%	1%
Sabbaticals	13%	1%	<1%
Gainsharing Plans	10%	4%	1%
On-site/subsidized Child Care (other than FSA)	11%	2%	<1%
On-site/subsidized Healthcare	10%	1%	<1%
Concierge/Errand Service	8%	3%	1%
Nonexecutive Employment Contracts	6%	<1%	<1%
Pets at Work	2%	0%	0%

## Additional Information

Additional analysis from Mercer's 2005/2006 US Compensation Planning Survey, including detailed reports by industry and region, is available.

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