



**AGENDA ITEM EXECUTIVE SUMMARY**

Agenda Item number: 5b

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| Title:     | Presentation of a Summary Report on Non-union Compensation from Sikich |
| Presenter: | Jennifer McMahon, Director of Human Resources                          |

Meeting: Government Operations Committee                      Date: November 20, 2017

Proposed Cost: \$ 0                      Budgeted Amount: N/A                      Not Budgeted:

**Executive Summary** *(if not budgeted please explain):*

Included in the FY 2017 and FY 2018 budgets is a total of \$30,000 to conduct a compensation analysis and study. The goals of this study include 1) evaluating the City’s current compensation philosophy, 2) evaluating the City’s comparable community criteria, 3) evaluating new comparable communities derived from new criteria, and 4) providing City Council with a final report of findings and recommendations.

Due to a change in staff, Sikich contracted out the last phase of this study to Cowden, a consulting firm with expertise in compensation, health and benefits, and retirement. This final phase included:

- Gauging whether the City’s current system is competitive within the marketplace with recommendations to improve the City’s compensation philosophy.
- Identifying areas that are meeting the goals and objectives of the compensation system as well as those areas that need further review.
- Providing guidance on those areas that would benefit from additional attention; including policy revisions that would assist in addressing those updates to the compensation system.

Included in the backup material is the summary report presentation from Sikich, which is being presented at the meeting, and a list of questions that were posed by City Council members over the course of the study.

**Attachments** *(please list):*

Sikich: Presentation of Power Point Summary Report  
HR Director FAQ: Council Questions RE: Compensation

**Recommendation/Suggested Action** *(briefly explain):*

Recommendation to receive and file Sikich report to utilize as guidance and formally evaluate the City’s compensation plan every three years.



# UPDATE REPORT COMPARABLE DEVELOPMENT RECOMMENDATIONS

City of St. Charles

October 20, 2017



# OVERALL OBJECTIVES

- Assessment will
  - gauge whether the City's current system is competitive within the City's marketplace with recommendations to improve the City's compensation philosophy.
  - allow the City to identify areas in the compensation system that are meeting the goals and objectives of the compensation system as well as those areas that need further review.
  - provide guidance on those areas that would benefit from additional attention, including policy revisions that would assist in addressing those updates to the compensation system.

# EXECUTIVE SUMMARY

- Results of Market Place analysis – St. Charles enjoys a unique competitive position (Value Proposition) compared to similarly situated entities, primarily related to the compensation practice of targeting the 75<sup>th</sup> percentile of pay. This practice permits St. Charles to be in an ideal position to attract and retain the highest performers
- In order to continue this position, we suggest the following:
  - Modifications to Pay philosophy should be considered to clearly articulate priorities
  - Altering merit pay practices should be considered in order to provide greater pay differential adjustments for top performers
  - Collect detailed market data on compensation vs. salary range information

# CURRENT COMPENSATION PHILOSOPHY

- **Compensation Philosophy** - “The compensation philosophy for the City of St. Charles is based on a commitment to hire and retain qualified, motivated employees at all levels within the organization. The City Council has determined that the City will lead the market by establishing ranges at the 75<sup>th</sup> percentile.”
  
- **Market Adjustments** - “Market adjustments involve salary range adjustments, based upon the 75<sup>th</sup> percentile of comparable communities, and are not based upon performance. They are designed to align pay so as to maintain internal and external equity”
  
- **Overview:**
  - Total Compensation Opportunities (base pay, health & welfare benefits, retirement) are extremely attractive
  - St. Charles follows the practice of establishing the maximum salary for each grade at the 75<sup>th</sup> percentile

# ASSESSMENT - COMMENTS ON COMPARISON INFORMATION

- How do employees of comparable communities progress through pay system?
  - More than half the communities indicate hybrid of step and merit
  
- How do employees progress through the St. Charles Pay System?
  - *Step increases* - increases of 3.96% are provided to employees in the first half of their salary range as long as there are no “Needs Improvement” scores on their assessment. The 3.96% increase allows an employee starting at the salary range minimum to reach midpoint in five years. Employees in the step plan are not eligible for merit based increases as described below
  - *Merit based increases* - allow the City to reward employees for both their city-wide impact contribution and their individual contribution, resulting in permitting the City to recognize the employees’ contribution toward the overall success of the organization and for their individual job performance

# RECOMMENDATION TO IMPROVE VALUE PROPOSITION

- Recommendation: In order to highlight the value proposition and reinforce the philosophy, we suggest the following:
  - Communicate the practice of adjusting salary range maximums at the 75<sup>th</sup> percentile
  - Communicate the practice of using performance to set compensation adjustments (if any) once an employee moves beyond the midpoint of the range
  - Prioritize pay-for-performance vs. 75<sup>th</sup> percentile of the market
    - Not possible to mutually exist from a philosophy and practice perspective
    - Philosophy can be a value proposition as follows:
      - Each employee of the City is provided the opportunity to earn compensation at the 75<sup>th</sup> percentile of the market through tenure and performance (city wide and individual)

# RECOMMENDATION REGARDING MERIT PAY

- City-wide impact merit should be more heavily weighted to certain employees who have a potential to make a larger impact
- The current merit system does not create sufficient spread in salary adjustments to reward top performers vs. those performing at “acceptable levels”
  - Top performers (Meritorious service) should receive a larger share of the pool by setting the adjustment at (for example) 120 - 140% of the target level ( $140\% \times 2.5\% = 3.5\%$ )
  - Recognized Service (the next tier) can be set at 80% or 90% ( $80\% \times 2.5\% = 2.0\%$ )
  - Acceptable Service (the next tier) can be set at 50% or 60% ( $50\% \times 2.5\% = 1.25\%$ )
  - The target level of the amounts available would still be in place to be certain that the gross dollar amount to be spent is maintained

# COLLECTION OF MARKET DATA

- In order to continue to maintain the value proposition (75<sup>th</sup> percentile) detailed and specific comparable data must be maintained
  - Targeting pay at the 75<sup>th</sup> percentile for all employees presents challenges in being certain to have accurate and reliable information, especially for higher level employees
  - We have suggested a program for meeting this objective

# ASSESSMENT - SALARY GRADE COMPRESSION

- Public entities that have long-tenured employees (such as St. Charles) often struggle with salary compression that occurs when there is small differences in pay between employees regardless of their skills or experience.
  - Pay compression is the result of the market-rate for a given job outpacing the increases historically given by the organization to high tenure employees.
- Current system is very compressed when comparing maximums between grades, indicating there is little room for movement
  - The average spread between the maximum pay grades for current grades B-M, is 9.05% (Grade A is for the City Administrator and current pay grades N and O relate to hourly employees only)
  - Internal pay equity and related challenges can occur as a direct result of pay compression
- We have provided an alternative grade structure for consideration (see Appendix A)

# Discussions and Questions



ACCOUNTING TECHNOLOGY ADVISORY

LinkedIn: [www.linkedin.com/company/sikich](http://www.linkedin.com/company/sikich)

Facebook: [www.facebook.com/sikichllp](http://www.facebook.com/sikichllp)

Twitter: [www.twitter.com/sikichllp](http://www.twitter.com/sikichllp)

Blog: [www.sikich.com/blog](http://www.sikich.com/blog)

[SIKICH.COM](http://SIKICH.COM)

## COUNCIL QUESTIONS RE: COMPENSATION

**1. What makes up the City's compensation plan?**

*The City's compensation philosophy is to lead the market at the 75<sup>th</sup> percentile to attract and retain top performers. It moves its non-union employees through a pay plan with a hybrid system of both annual market adjustments (i.e. a cost of living adjustment or COLA) and step or merit increases tied to performance.*

**2. What does the 75<sup>th</sup> percentile mean?**

*This is the City's compensation philosophy; to "pay at the 75<sup>th</sup> percentile." The City chooses to lead the market by setting the top of the range for positions at the 75<sup>th</sup> percentile of its comparable communities. Most employees are not at the top and, therefore, are not paid at the 75<sup>th</sup> percentile.*

**3. Where do the City's comparable communities set their philosophy?**

*Most of the City's comparable communities have a philosophy of the 50<sup>th</sup> percentile of their comparable communities.*

**4. What dollar amount does the 75<sup>th</sup> percentile equate to with the City's new comparable communities?**

*HR staff identified six benchmark positions (three exempt and three non-exempt) to compare against the new comparable communities. Other than Battalion Chief, the difference between the City's current top wage rate (at the 75<sup>th</sup> percentile) and the 75<sup>th</sup> percentile top wage rate for the new comparable communities is +/-5.5%, with the average difference being .69%. This is just preliminary work to give a sense of the impact of new comparables. HR staff would require several months to conduct a comprehensive market study to verify the impact.*

**5. How are the City's comparable communities determined?**

*During Phase II of Sikich's study, a new set of comparable communities were established using an empirical method with several criteria and including contiguous communities. Either by scoring or being contiguous, communities were identified as the City's competitors for talent.*

**6. How are pay grades established and positions assigned to those grades?**

*Per the Hay Group's 2007 compensation study, the individual pay ranges established for each position were compressed into fewer pay grades. Like positions were consolidated into one pay grade, resulting in 15 pay grades for all non-union positions. Within the last two years, criteria were established to determine which pay grade a position should be assigned. This criteria includes things like educational requirements, years of experience, decision-making responsibility, the impact those decisions have, etc.*

**7. How does merit work for non-union positions?**

*For the last two years, a hybrid system has been in place. Employees below the mid-point of the range, are given an annual step increase of 3.96% as long as they have no "Needs Improvement" scores. The step system gets the employee to the mid-point in five years.*

*After they've reached the mid-point, the employee will be given an annual merit increase for their individual performance as well as their city-wide impact. The percent increase for city-wide impact is determined by the City Administrator, HR Director, and Finance Director based on available budgeted funds. The individual merit increase is determined by the Department Director. Department Directors are provided a pool of dollars and are to follow guidelines to acknowledge Meritorious service, Recognized service, and Acceptable service. Directors are not obligated to award any merit. The total pool of dollars for merit is established by the City Administrator and Finance Director given existing budget constraints.*

**8. Do the City's comparable communities use a merit-only system?**

*The majority of the City's comparable communities utilizes a hybrid system of both merit and market adjustments.*

**9. How is the market adjustment determined?**

*The market adjustment is designed to have both the position pay range and employee pay keep pace with the market; i.e. maintain the 75<sup>th</sup> percentile. It is determined by looking at the annual adjustment at comparable communities (external) and reviewing the annual adjustments included in the collective bargaining agreements (internal).*

**10. How can the City reward for excellence on specific projects (i.e. new Police Station)?**

*Research by HR staff could identify only one community that utilizes a bonus for high performance. This is not a common practice in the municipal sector.*

**11. Does the City's compensation philosophy and pay plan attract and retain top performers?**

*In their final report, Sikich states that the City's compensation philosophy is a beneficial value proposition in hiring and retaining employees. The City's turnover rate bears this out, which is far below the national average and is related to retirements and relocation. Sikich recommends retaining the step process and the annual market adjustments.*

**12. How is elected official pay determined by the City's comparables?**

*Very few comparables apply their compensation philosophy to elected official pay. Most have established pay historically.*

**13. How often should the City revisit the compensation philosophy and pay plan?**

*A compensation philosophy should be reviewed periodically and modified based on how well it's working and factors affecting the City. For example, during the Recession, public employers had to choose between freezing/cutting wages or layoffs. That was a time when the compensation philosophy may have needed revision to meet the City's ability to pay and because the applicant pool was flush with qualified candidates. In Phase II of the study, Sikich recommended reviewing the compensation philosophy and comparable community criteria every three years. Council approved that recommendation on July 3, 2017. In the final report, Sikich further recommends doing a comprehensive market analysis of rotating benchmark positions every two years. Such analysis includes collecting pay data and job descriptions from comparable communities.*