

Chain Restaurant Compensation Association

**2004 Survey of Short-Term Incentive
Practices for Corporate Management and
Professional Positions**



Prepared By



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Survey Background

- Purpose: to provide CRCA members with a better understanding of short-term incentive practices for corporate management and professional positions
- Topics covered:
 - ◆ Short-term incentive plan design and administration features
 - ◆ Performance measures
 - ◆ Perceived program effectiveness
- Note: data provided for the plan that covers the greatest number of corporate management and professional employees

32 Survey Participants

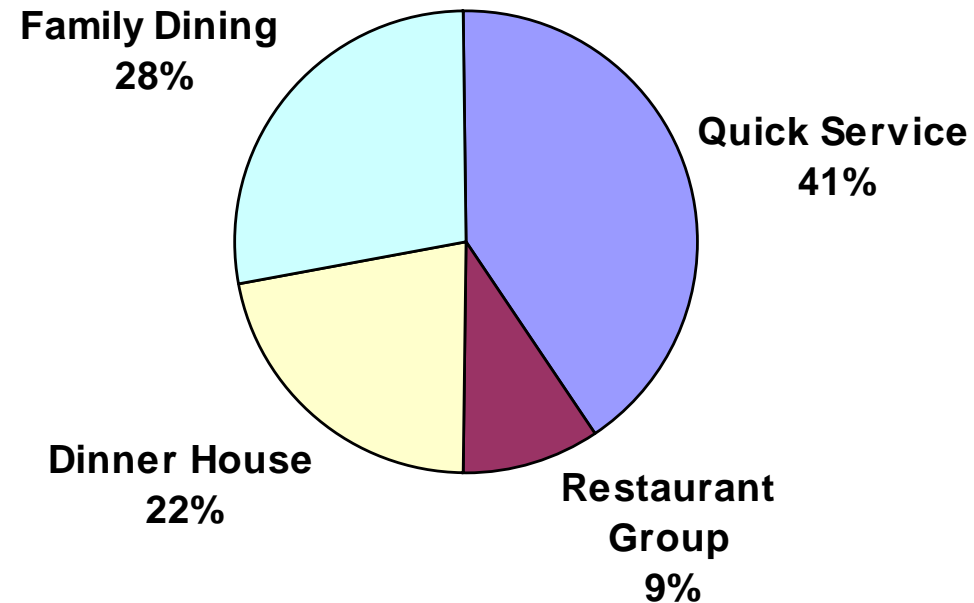


- Applebee's International, Inc.
- Arby's, Inc.
- Bob Evans Farms, Inc.
- Brinker International
- Buffets, Inc.
- Caribou Coffee Company, Inc.
- Carlson Restaurants Worldwide
- Chipotle Mexican Grill, Inc.
- Dave & Buster's, Inc.
- Denny's Corporation
- Domino's Pizza LLC
- El Torito Acapulco Restaurants
- Famous Dave's of America
- Friendly Ice Cream Corporation
- Frisch's Restaurants, Inc.
- Golden Corral Corporation
- HMS Host Corporation
- Jack in the Box, Inc.
- McDonald's Corporation
- O'Charley's, Inc.
- Panda Restaurant Group, Inc.
- Panera Bread
- Rare Hospitality International, Inc.
- Rock Bottom Restaurants, Inc.
- Round Table Pizza
- Starbucks Coffee Company
- Taco John's International, Inc.
- The Cheesecake Factory, Inc.
- The Steak n Shake Company
- Uno Restaurants LLC
- VICORP Restaurants, Inc.
- Wendy's International, Inc.

Participant Demographics

- Median participant profile
 - ◆ # of full time empl.s: 8,522
 - ◆ Revenues: \$500MM

By Dining Concept



Plan Design and Administrative Features

Plan Design Features

- Over 50% of plans were implemented within past 4 years
 - ◆ Approximately 75% of plans implemented within past 8 years
 - ◆ 15% of plans in place for over 10 years

- Primary type of plan design:
 - ◆ Payments based on results vs. pre-defined objectives: 97%
 - ◆ Discretionary payments based on after-the-fact results: 0%
 - ◆ Other type of plan design: 3%

Plan Design Features

- Employee groups covered under plan (check all that apply):
 - ◆ Executives: 69%
 - ◆ Managers: 84%
 - ◆ Professionals: 47%
 - ◆ Nonexempts: 28%

Plan Design Features

- Minimum eligibility requirements (check all that apply):
 - ◆ Job title, level, grade: 78%
 - ◆ Performance based: 28%
 - ◆ Time in job: 22%
 - ◆ Length of service: 13%
 - ◆ No requirements: 6%
 - ◆ Other: 6%

- Typical (median) base salary associated with entry level eligibility in the plan is \$50,000

Plan Design Features

- Approximately 75% of plans have pre-established performance levels.

Relationship Between Threshold and Target	% of Responses
Thresh. payments < 20% of target	22%
Thresh. payments 20%-39% of target	17%
Thresh. payments 40%-59% of target	39%
Thresh. payments 60%-79% of target	9%
Thresh. payments 80%-99% of target	13%

Plan Design Features

- Similarly, approximately 75% of plans have a maximum, cap or upper limit.

Relationship Between Target and Maximum	% of Responses
Max. payments btw. 100%-119% of target	36%
Max. payments btw. 120%-139% of target	0%
Max. payments btw. 140%-159% of target	41%
Max. payments btw. 160%-179% of target	9%
Max. payments btw. 180%-199% of target	5%
Max. payments btw. 200%-249% of target	5%
Other	5%

Aggregate Performance Relative to Target



- Actual organization performance relative to corporate or operating unit financial performance targets:
 - ◆ FY03: 95%
 - ◆ FY02: 102%

Incentive Plan Objectives

Four key objectives of the incentive program.

Incentive Plan Objective	Plan Intent		
	Not Applicable	Intended Objective	High Priority
Noticeably improve individual employee performance/ productivity	10%	72%	17%
Improve overall productivity	23%	67%	10%
Create a more competitive total compensation market position	23%	65%	16%
Noticeably improve organization or team financial performance	10%	61%	32%
Improve employee involvement	45%	48%	3%
Reduce employee turnover	52%	48%	0%
Better recognize employee contributions	32%	45%	23%
Support culture change	63%	33%	7%
Promote a sense of ownership	50%	33%	17%
Move from fixed to variable pay to better manage compensation costs	82%	14%	4%
Other	83%	0%	17%

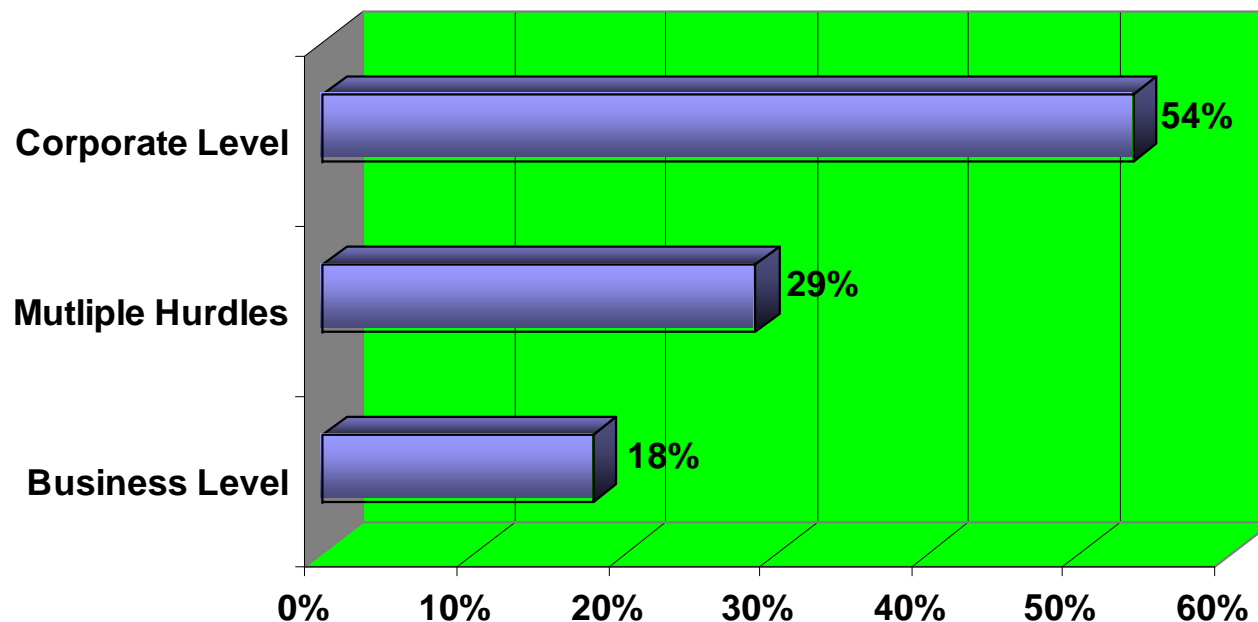
Plan Funding

- Percentage of companies with funded incentive plans:
 - ◆ Yes: 81%
 - ◆ No: 19%

- Criteria for incentive plan funding (of the 81% responding yes):
 - ◆ Budgeted % of payroll: 56%
 - ◆ Plan is self funded: 36%
 - ◆ Criteria are discretionary: 4%
 - ◆ Other: 4%

Plan Payouts

- Percentage of companies with a hurdle or trigger that can prevent payout:
 - ◆ Yes: 88%
 - ◆ No: 12%
- If yes, level in the organization where the hurdle is measured:



■ Method used for incentive determination:

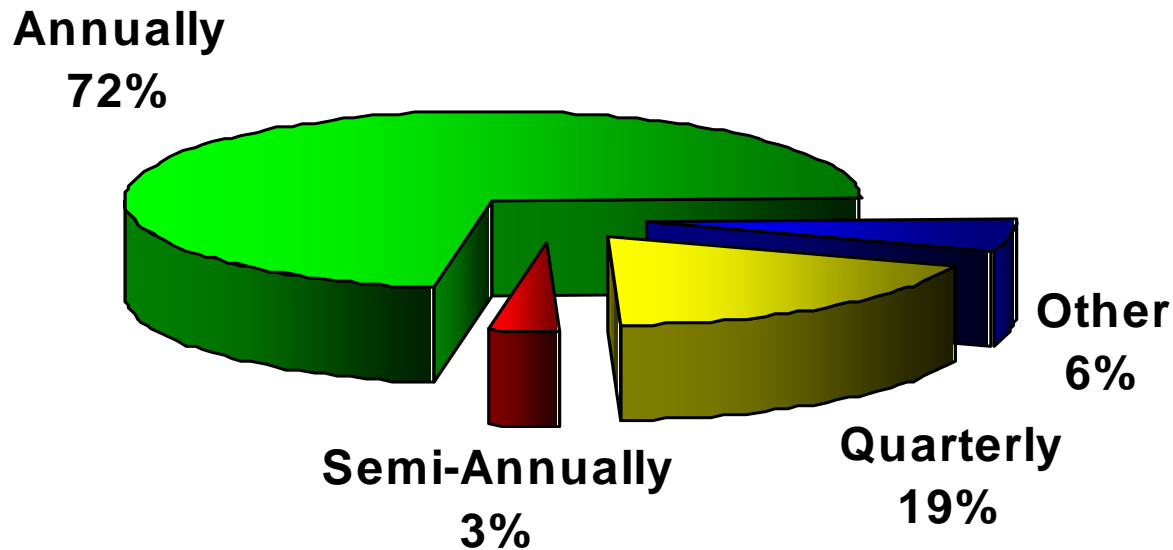
- ◆ % of base pay actual: 69%
- ◆ % of base salary policy: 9%
- ◆ Flat dollar amount: 9%
- ◆ Other: 13%
 - Profit driven pools (e.g, % of profit, % of base pay pro-rated against overall pool)
 - Other: sliding amount based on sales volume

■ Form of plan payout:

- ◆ Cash only, paid immediately: 81%
- ◆ Cash only, all or partially deferred: 13%
- ◆ Cash and/or stock: 3%
- ◆ Other: 3%

Frequency of Payouts

- A substantial majority of the participants provide annual payouts.



Performance Measures

Performance Measures: Types of Measures



- Financial measures (97% of plans)
 - ◆ Profit – operating income, controllable profit vs. plan, EPS, ROA, EBITDA, DOI, PACE, cash flow
 - ◆ Sales -- net sales, comparable restaurant sales, sales growth vs. plan
- Operational measures (19% of plans)
 - ◆ Cost control -- cost of sales, food and paper costs, food costs, food vs. labor costs, crew labor costs, labor cost vs target.
- Customer measures (28% of plans)
 - ◆ Internal customer satisfaction -- quality, service, cleanliness, friendliness, passionate service, QSC scores (score of 85% or better)
- Employee measures (56% of plans)
 - ◆ Commitment survey, individual performance rating, team/department objectives, MBOs for executives and managers

Performance Measures: Combinations of Measures



■ Financial measures only:	41%
◆ Sales only:	0%
◆ Profit only:	54%
◆ Sales and profit:	15%
■ Financial and employee measures only:	28%
■ Financial, operational, customer, employee:	16%
■ Financial, customer, employee measures:	9%
■ Financial, operation, customer measures:	3%
■ Financial and operational measures only:	0%
■ Financial and customer measures only:	0%

Performance Measures:

- Unit measurements (% of plans):
 - ◆ Corporate: 71%
 - ◆ Operating unit: 38%
 - ◆ Team/function: 8%
 - ◆ Individual: 33%

- Median number of total plan measures is 2
 - ◆ Inter-quartile range: 1 to 4 measures.
 - ◆ Low to high: 1 to 10 measures

- Use of discretion in payouts
 - ◆ Strictly predefined: 72%
 - ◆ Judgment may be used: 28%

Program Effectiveness

Incentive Plan Effectiveness

Against key objectives, most plans are viewed as marginally effective to effective.

Incentive Plan Objective	Level of Success				
	Not Effective	Marginally Effective	Effective	Very Effective	Effective + Very Effective
Create a more competitive total compensation market position	0%	23%	52%	3%	55%
Noticeably improve organization or team financial performance	3%	32%	39%	10%	48%
Improve overall productivity	3%	20%	47%	0%	47%
Noticeably improve individual employee performance/ productivity	0%	38%	41%	3%	45%
Better recognize employee contributions	3%	19%	32%	6%	39%
Promote a sense of ownership	3%	20%	23%	3%	27%
Improve employee involvement	6%	23%	26%	0%	26%
Move from fixed to variable pay to better manage compensation costs	4%	0%	14%	7%	21%
Support culture change	3%	13%	20%	0%	20%
Reduce employee turnover	3%	34%	7%	3%	10%
Other	0%	0%	0%	0%	0%

Effectiveness of Plan Policies and Practices



Program Policies and Practices	Effectiveness of Policy or Practice				
	% Not Effective	% Marginally Effective	% Effective	% Very Effective	% Effective + % Very Effective
Overall effectiveness of the short term incentive program	0%	29%	68%	4%	71%
Relationship between incentive program payouts to organization performance	0%	14%	66%	21%	86%
Appropriateness of measures	3%	21%	62%	14%	76%
Funding mechanism	4%	21%	61%	14%	75%
Employee understanding of program	3%	24%	59%	14%	72%
Administrative ease in supporting the program	7%	26%	56%	11%	67%
Appropriate return on investment	3%	34%	52%	10%	62%
Motivational value of program	3%	41%	45%	10%	55%
Relationship between incentive program payouts to group/team performance	14%	38%	41%	7%	48%
Responsiveness to change	14%	41%	34%	10%	45%
Relationship between incentive program payouts to individual performance	17%	45%	31%	7%	38%

Measuring Plan Effectiveness



- Typical measures of annual incentive plan effectiveness:
 - ◆ Informal opinion gathering from senior leaders: 33%
 - ◆ Employee turnover or retention: 33%
 - ◆ Management does not evaluate success: 33%
 - ◆ Employee productivity metrics: 27%
 - ◆ Informal opinion gathering from employees: 27%
 - ◆ Employee satisfaction survey measures: 17%
 - ◆ Labor cost is controlled or lowered: 13%
- Note: up to three most important criteria identified

Plan Improvements

- Areas of potential plan improvement:
 - ◆ Improve linkage btw. payout and performance: 77%
 - ◆ Improve plan line of sight to individual/team: 48%
 - ◆ Improve communication of plan objectives: 39%
 - ◆ Improve ease of administration: 29%
 - ◆ Ensure goals are viewed as more attainable: 29%
 - ◆ Increase participant understanding of plan: 26%
 - ◆ Increase payout opportunities: 23%
- Note: up to three most important criteria identified

Accountability for Plan Design

■ Responsibility for plan design:

- ◆ HR with line management input: 64%
- ◆ Solely HR: 21%
- ◆ Solely line management: 7%
- ◆ Line management with HR input: 4%
- ◆ Other: 4%
 - Executives with HR input

■ Plan participants involvement in plan design:

- ◆ Not involved in design: 87%
- ◆ Opinions solicited: 10%
- ◆ Provided recommendations: 3%

- Level of understanding by plan participants:
 - ◆ Virtually all understand: 23%
 - ◆ Most understand: 55%
 - ◆ About half understand: 13%
 - ◆ Most do not understand: 10%

- Methods of communicating plan details and performance updates:
 - ◆ Written document outlining plan: 61%
 - ◆ Managers verbally discuss: 48%
 - ◆ Plan described at employee meetings: 35%
 - ◆ Plan posted in public place/intranet: 19%
 - ◆ Plan not communicated: 3%

The Good, Bad and Ugly Test

“The Good” -- i.e., Keep Doing



- Focus on key performance measures
 - ◆ “Continue to base measures strictly on pre-tax profits”
 - ◆ “Payout threshold linked to EPS”
 - ◆ “Link to both corporate and individual business unit”
 - ◆ “Focus on overall financial results – 70% of plan design”
 - ◆ “Keep operating unit profit contribution”
 - ◆ “Focus on individual performance measure”

The Good, Bad and Ugly Test

“The Good” -- i.e., Keep Doing



■ Plan design

- ◆ “Straightforward and easy to understand”
- ◆ “Keep link with performance and pay differential between high and low performers”
- ◆ “Continue differentiating rewards based on performance”
- ◆ “All corporate employees are eligible to participate”
- ◆ “Include current levels of participants”
- ◆ “Continue focus on sales building behaviors and sales building as an outcome”
- ◆ “Setting ambitious but attainable performance targets”

■ Administration

- ◆ “Keep it simple and easy to administer”
- ◆ “Quarterly payouts”

The Good, Bad and Ugly Test

“The Bad” -- i.e., Stop Doing



■ Plan design

- ◆ “Focusing on specific earnings and calculations rather than performance”
- ◆ “Setting eligibility based on market base salary vs. level of impact on the organization”

■ Administration

- ◆ “Paying out bonuses at lower performance levels”
- ◆ “Unilaterally setting target bonus levels”
- ◆ “Getting the plan and its measures out late”
- ◆ “Being unaware of incentive payouts in other countries”
- ◆ “Allowing too much variation against company annual plan in the budgeting process”

The Good, Bad and Ugly Test

“The Ugly” -- i.e. Need to Change



- More focus on key performance measures
 - ◆ “Change EPS to another measure since few employees can influence EPS”
 - ◆ “Dilute the number of measures”
 - ◆ “Reduce the number of subjective measures used in some departments”
 - ◆ “Improve customer satisfaction measurement”
 - ◆ “Do not make all targets financially based”
- Design mechanics
 - ◆ “Establish target award percentages instead of flat dollar amounts”
 - ◆ “Build greater emphasis on performance match/comparison to payout”
 - ◆ “View competitiveness as a % of actual pay designated by group”
 - ◆ “Sense of entitlement to maximum payout – not viewed as starting from 0% and building”

The Good, Bad and Ugly Test

“The Ugly” -- i.e. Need to Change



■ Administration

- ◆ “Stop all written communication and have the plan available to eligible employees via the web”
- ◆ “Provide greater understanding of what employees can do to drive financial change to receive payment”
- ◆ “Automate the calculation process”
- ◆ “Make sure all goals are set in a timely manner”
- ◆ “Improve line of sight”
- ◆ “Greater differentiation between good and poor performers”

Conclusions

- Against key objectives, most plans are viewed as marginally effective to effective
- Four key plan objectives:
 - ◆ Improve individual performance
 - ◆ Improve overall productivity
 - ◆ Create a more competitive total compensation market
 - ◆ Improve organization/team performance
- Virtually all plans have financial performance measures and many plans also focus on employee performance measures (primarily individual goal achievement)
- Desire to create a stronger tie between payout and performance
- Important to keep the plan simple and easy to understand
- Most eligible employees understand the plan, but are not involved in the plan design