point of view

Should you reward staff for five-star service?

Evidence suggests connecting pay with customer experience makes good business sense. Just prepare to manage the pitfalls.

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Summary

Pay that reflects performance makes good business sense. The same follows for linking employee compensation with customer satisfaction metrics. Leaders need only follow a few key methods to incentivize staff, discourage "gaming" the system and ensure the very best results.

Key insight: It's human nature to strive for a reward. It is also in our DNA to do anything and everything we can to reach that payoff—for some, even if it means bending the rules. Executives need to keep that in mind when designing and establishing their customer measurement programs, platforms and processes.

Introduction

Money is a loaded topic for anyone, anywhere. Not surprisingly, there are few practices more central to a company's psyche than pay—and how performance impacts it. Every business strives for outstanding customer service. But should we base employees' compensation on customer satisfaction measurements?

In principle, yes.

Although there's been a backlash against the practice recently and despite that, or perhaps because of it, leaders often question whether they should continue linking customer metrics to staff pay. It's a reasonable query, though evidence supports the yes side. Why? Because using numerical scores summarizing customer feedback to gauge performance reinforces the idea of pay-for-performance. It also creates a material incentive linking the employee-customer-value chain. And, it's in our nature to put forth our best effort when there's a proverbial carrot dangling out front for the taking.

At the same time, concerns about the "gaming" of customer metrics are justifiable. Chances are, as a consumer, you've experienced something like this: an auto dealership salesman asking you to give him a certain customer satisfaction score. Because where incentive exists, there will be some who use questionable means to reach the reward. Fortunately, leaders can address gaming—while also taking advantage of a host of other benefits—by using simple customer experience metrics, setting targets relative to benchmarks and integrating customer data within a balanced framework.

Regardless of the approach, leaders do need to build trust around customer metrics throughout their organizations. The best way is by communicating measures clearly; demonstrating relevance, stability, and objectivity; and using customer metrics to drive employee behavior at the frontline. This approach improves real customer experiences on a daily basis. Essentially, should leaders want to effectively solve the customer satisfaction measurement-related-to-pay equation, they must lead a process that is specific to their company, its needs and its distinctive corporate culture. Compensation is a complex and impactful management area, and one that usually benefits from professional guidance.

These are our learnings about the implications of tying customer metrics to compensation and, more generally, performance management. First, we look at the basics of compensation, methods for addressing gaming and implications of the recent emphasis on closing the loop on customer feedback. Then we bring concepts to life with case studies from famously successful corporations, including Whirlpool, Microsoft and Allstate. Finally, we summarize compelling techniques and give practitioners specific recommendations.

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Compensation 101 – **How do companies pay their people?**

Payment is a deceptively complex matter. We've designed this section for managers considering how best to connect customer experience to compensation. This is an overview decoding the components and intricacies of staff payment. To begin, how does it work? Most businesses compensate their employees in three ways:

1. Base Pay

Companies compensate people with money for their time, expertise, ideas and effort—usually through base pay assigned on an annual or hourly calculation. Base pay reflects the level of perceived value an individual gives the organization.

However, managers are often skeptical of base pay as a tool to influence customer experience because employees tend to view it as an entitlement, with little differentiation between mediocre versus great performance. Once money is in the base, though, it is hard to remove. It is also difficult to demarcate a strategic goal, such as customer experience improvement, and reward that in a way that makes an impact. If companies increase base pay 2% for average performance and 4% for outstanding performance, for instance, it's hard for managers to motivate people toward higher levels of customer experience delivery. Many would argue, too, that the customer experience is part of the employee's core job and doesn't merit increased base pay.

2. Bonuses

Leaders must attract and retain a talented workforce, and base pay alone doesn't always meet that objective. Today, the most popular way to do it is through bonuses, incentives and commissions.

Companies prefer bonuses because they have high up-side potential with low risk and businesses can attach strings to the payout. Employees generally like bonuses, though they are sometimes wary. Several factors can get in the way, including the lack of an objective, non-discretionary, appraisal process, the individual's limited ability to control customer experience improvements and an unclear line of sight to customer impact for many employees, particularly middle managers.

When a company is performing well and making healthy bonus payouts, everyone is usually happy. But when the company restricts the bonus pool and decreases or eliminates payouts, incentive plans can actually de-motivate staff. In that scenario, employees feel that they've worked hard for little return—because even when customer metrics are all on the rise, if the business might be experiencing an economic downturn, the company may not be able to offer a payout. The danger is that this disconnect can linger in employees' minds for years and negatively impact the perceived value of driving customer experience improvements.

3. Long-term incentives

Long-term incentives include stock grants, stock options, deferred compensation and pension considerations. Strategic measures, such as stock price, total shareholder return or even customer satisfaction and loyalty usually drive these tools.

Executives in many markets prefer stock and option grants, especially during the recent talent war of venture capital-backed start-ups. The thinking behind it is that start-up companies can't pay for talent, so they offer stock and options as a way for people to build up capital using "sweat equity." More recently, some companies have tied pension scheme payouts to customer metrics. Leaders can use this new lever to connect pay to customer experience performance.
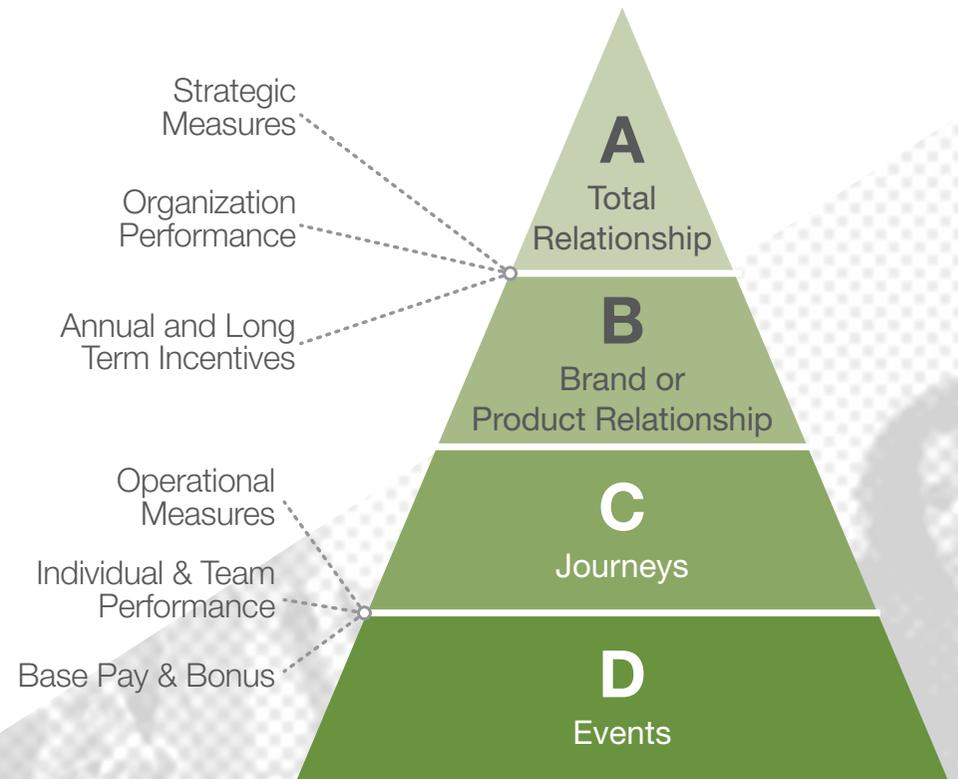
Making metrics work for you

Now the fun begins! How do you determine the best way to use your data to calculate appropriate compensation for your staff? Managers can combine the pay tools to drive staff behaviors, improving the company's overall performance: in areas such as customer experience, satisfaction and loyalty. They can take advantage of specific customer metrics as part of a performance measurement and management system to incentivize their employees' customer relationship-related behaviors. This fosters a customer-centric business, which ultimately helps reach strategic business objectives.

Leaders can use two main points of entry to align compensation with customer metrics (see the figure below). First, at the strategic level: they can capture a measurement of the overall customer relationship.

Managers can use strategic measures—customer experience, satisfaction or loyalty metrics—which reflect overall organization-wide customer relationship health. Strategic metric rewards tend to focus on annual bonus plans and long-term incentives.

Second, managers can measure at the operational level, using operating metrics to set individual and team goals. The payment vehicles of choice are base pay and various bonuses.

Strategic Measures

Organization Performance

Annual and Long Term Incentives

Operational Measures

Individual & Team Performance

Base Pay & Bonus

A Total Relationship

B Brand or Product Relationship

C Journeys

D Events

Combating gaming

"What you measure is what you will get," Dan Ariely, the renowned behavioral economist, is often quoted as saying. Rewards are intrinsically good, but they can also bring out the worst in us. Whether you use strategic, tactical or a combination of customer metrics and fasten those to rewards, expect that your employees will do whatever is necessary to reach goals and get payouts—sometimes even taking inappropriate action. The evidence of this is clear.

The reality is employees engage in gaming customer measurement systems. We've all seen it. Maybe you've had a front desk clerk remind you that his hotel will email you a survey soon and his personal health would benefit from a perfect 10 score. Or perhaps those customer metric program surveys, the ones with low scores, managed to get "lost" before staff could tally them. Surreptitiously stuffing ballet boxes with high scores happens, too.

The good news is: addressing gaming is straightforward. Managers can tackle it using three key steps:

1. Select **simple** customer experience metrics.

2. Set **targets** relative to internal or external benchmarks.

3. Use customer metrics within a **balanced framework.**

Let's explore these in further detail.

Simple metrics win

Leaders must keep customer metrics *simple*. This is critically important. Much has been written about the "one number you need to grow." Regardless of the specific metric calculation, can your employee (at any level) quickly and easily determine whether he's on track for a reward based on customer experience performance? If not, then the system's not working. Most customer feedback programs center on survey responses from a representative population captured at regular time intervals. You can help your employees understand the metric easily—and make your communication about it clear—if you connect compensation to responses to a *single question.*

Simple metrics can't eliminate potential gaming altogether. But, clarity on scores creates two benefits. First, employees who understand how systems work feel they have some control over outcomes, so they'll make an effort to act in-line with system guidelines. In other words, employees tend to play by the rules when they understand them—reasonably so. Second, leaders who use simple metrics find it easier to detect when employees are gaming, and are able to quickly correct missteps.

Setting targets sets the tone

When leaders establish customer experience performance targets, they focus the company on improvement—a must if joining performance to compensation. Clearly identified targets also play a key role in addressing potential gaming. In fact, setting customer experience goals helps leaders address the gaming of other compensation aspects; for example, by balancing the organization's emphasis on customer experience versus short-term financial results and guiding the business to work across functional silos. Target or goal setting also creates an immediate "pull" for customer information and insights, pushing leaders to use customer information in decision-making company-wide.

Benefits of SMART goals (Specific, Measureable, Achievable, Relevant, Timely) aside, best-practice target-setting revolves around three basic concepts:

Top-down: Visionary leadership usually drives these corporate-wide targets dubbed "big hairy audacious goals" (BHAGs). These take the form of Level A / B relationship customer metric improvement over several years.

Bottom-up: Typically measured at higher frequency (monthly or more frequently), these targets are front-line specific Level C / D event and operational metrics.

Outside-in: Leaders base these targets (top-down or bottom-up) off of relative performance within or outside the organization. These require capturing internal and/or external benchmarks targets.

With **Outside-in** targets, relative or benchmarked goals strengthen a measurement system, make gaming more difficult and offer solutions to common target-setting issues, such as challenging top performers to continue progressing. This is well documented. Ipsos authors demonstrate the powerful relationship between relative customer metrics and subsequent financial results in the book, *Wallet Allocation Rule: Winning the Battle for Share.* When leaders set targets using such relative metrics, it drives employee behavior to align directly with how customers spend their money, effectively connecting the employee-customer-value chain.

Clearly identified targets also play a key role in addressing potential gaming.

The balanced framework context

To address gaming, leaders must first understand how customer metrics work within the context of a balanced framework. It must be one that incorporates other financial and operational metrics used within the company for compensation linkage. Experienced managers know that one of the quickest way to reach a customer metric goal is to "fire" customers giving low scores. But this typically leads to immediate revenue loss. Similarly, fast-growing business units often suffer customer score declines as the unit grapples with capacity issues. But penalizing managers for growth doesn't make sense. Instead, leaders can design reward systems to balance the impact of compensation linkages across financial, operational and customer metrics; recognizing inter-relationships, including leading and lagging effects.

Leaders also need to scan for operational, competitive and other factors underlying customer metrics levels and trends. Too often leaders move a successful location manager or unit manager garnering top customer scores to another area, where the manager is then unable to generate the same level of performance. Those managers say that it isn't fair—and they're right!

Customer base make-up, competitive intensity and business mix all impact customer metrics. At one global pizza chain, for instance, the mix of dine-in and take-away drove customer scores because employee-served diners awarded higher scores due to the human contact. At an international hotel chain, customer scores highly correlated to the age of the property: older hotels fared worse than newer ones. How fair is that to the employees? Not very. Unless leaders take a "fair score carding" approach that restates performance metrics making data comparable across measured units, the potential for disgruntled managers gaming the system is high.

Trendy: **Closed Loop Feedback**

Managers nowadays prefer Closed Loop Feedback. Previously, customer measurement systems sent surveys, captured data and reported figures. Even when a customer had a "critical incident," sometimes giving extremely negative feedback, managers didn't follow up with the customer on the individual specific issue. Today, companies let their staff contact a dissatisfied customer and take appropriate action. Typically, this means following up after something goes wrong and attempting to make good (i.e., "closing the loop").

Because closing the loop creates real action at the individual level, most managers believe it can't help but improve the overall customer experience and build a customer-centric culture over time. After all, employees will either learn how to deliver branded experiences consistently well or leave. As a result, managers are interested in key customer metrics related to closing the loop. This includes the number of outstanding hot alerts that need closing, the average time it takes to close the loop and the ratio of the company's and customer's perceived effort to resolve the issue. (Read more in "The Customer: Company Effort Ratio" (Ipsos).)

Integrating customer metrics with broader performance management

Case Studies

Coupling compensation with customer metrics is a complex matter. There are a variety of different options to suit the specific dynamics of an organization, its strategy and culture. As such, solving the compensation equation is very much a company-specific issue. For this reason leaders will find it instructional to review case examples of businesses actively engaged in doing it effectively.

In each case, you can see that the company's success stemmed from incorporating customer metrics not only into the rewards system, but also into performance management within the organization. In addition, the need to weave communication, training, hiring and several other employee engagement processes in and around rewards and performance management systems is clear. These case studies offer a glimpse into how leaders can integrate these elements successfully.

Strategic Linkage – **Whirlpool**

Whirlpool, the world's No. 1 appliance manufacturer, launched a comprehensive global customer loyalty program supported by its chairman and top executives. The team constructed Customer Loyalty Indices (CLIs) based on in-depth customer research for each of its major brands to help measure, model and manage customer relationship strength.

The company's leaders wanted a tough measure to aim for, so they constructed an index requiring top box scores on four of the seven loyalty behaviors. The CEO was looking for significant improvement in the metric over seven years as a way to monitor and drive transformation towards a customer-centric organization. After several waves of data, the CEO's next question was: could they connect the Customer Loyalty Index to the leadership incentive plan? A logical next step.

Whirlpool based its leadership incentive plan on the corporate balanced scorecard. As with most, it combines three service business values to customers, quality products and respect for employees with the need for financial performance (see the chart below).

This diagram is important because it once again demonstrates the inherent limitations of customer metrics—such as the Customer Loyalty Index—in transforming a company. At the strategic level, the metric has to compete with other measures, such as a quality index, an employee commitment index and certainly measures of shareholder value.

As the Whirlpool executive team moved forward, there was good reason for them be cautious about connecting to compensation. The team considered several factors, such as:

- Experience with the Customer Loyalty Index as a metric: Leaders needed enough data to become confident using the measure.

- Control to move the needle: Similarly, the team needed experience to find the right buttons to push in order to make the Customer Loyalty Index move.

- Market dynamics: Merger and acquisition activity (Whirlpool acquired Maytag during this time) made an impact on relationship measures.

The team felt concerned that if leaders thought the metric was erratic, or that they couldn't influence its outcome, they would get cynical about it and the broader customer loyalty strategy. They worried that reaching into staff pocketbooks might create an insurmountable barrier to real change—and that the temptation to game the system might creep into consideration.

The Whirlpool executive team decided to take it slow. They did put the CLI metric on the corporate scorecards, but for the short-term made the payout based on "activity" versus "results." For example, the team might hold leaders accountable for having communication briefings or funding new loyalty initiatives, but not immediately for movement in the Customer Loyalty Index. While this might sound counter to performance pay theory, the leaders felt confident that in the short-term they could align themselves with the customer strategy without fear of a diminished pay check.
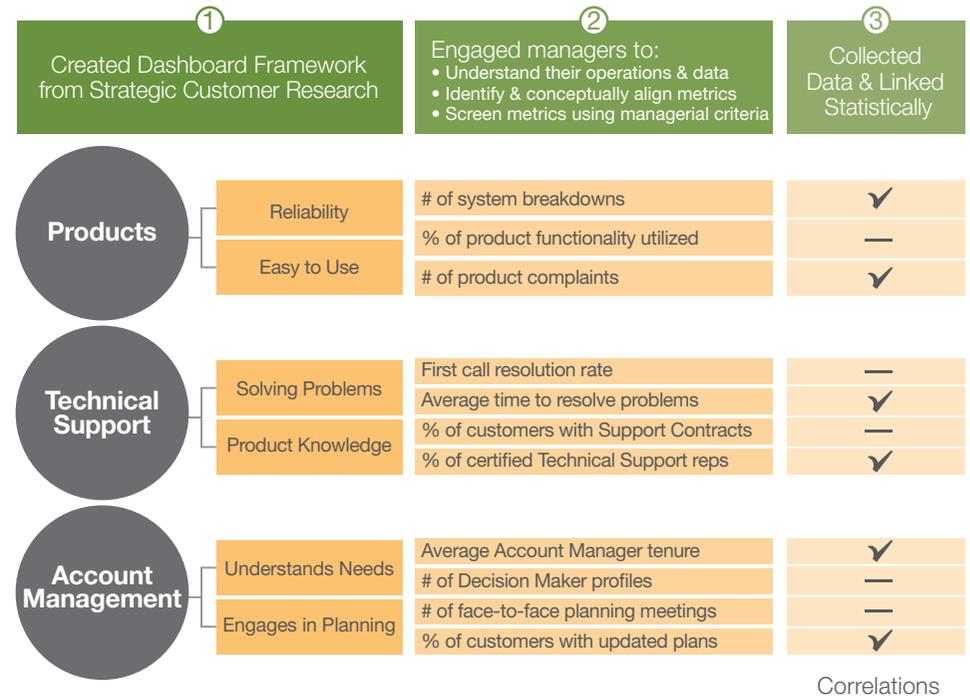
Strategic results can be a long way out
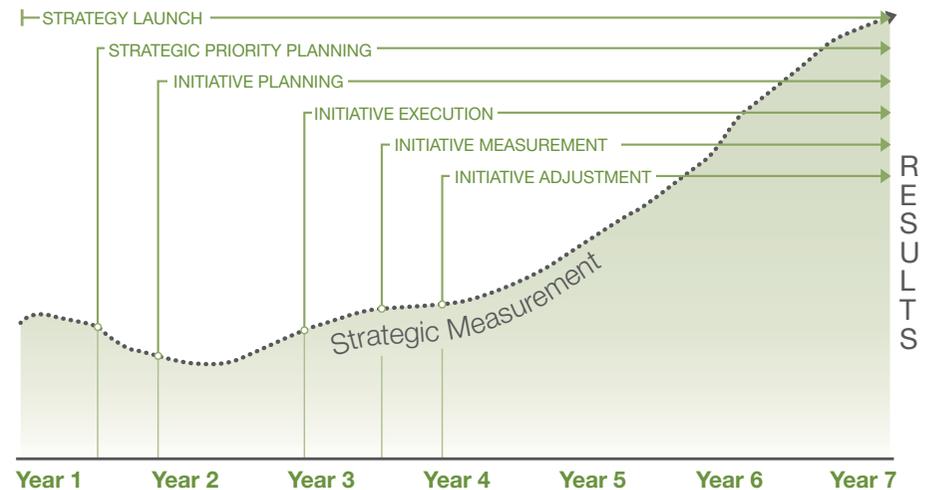
Whirlpool's direction aligned with the reality of getting strategic results measureable by the Customer Loyalty Index. When the company implemented the Customer Loyalty Index in Year 1 (above), it also launched a process planning, resourcing, execution, pilot measurement and adjustment that would take several years to influence the strategic measure. The executives would not expect to see strategic results for another three to four years, justifying the approach to pay for activity in the short-term. Then as time passed, the Whirlpool team tightened the connection between Customer Loyalty Index results and compensation. Patience paid off.

Operational Linkage – **Microsoft**

Microsoft, a multinational technology giant, is a household name, known for its ubiquitous software, personal computers and consumer electronics. The market leader was having difficulty, though, connecting its annual strategic customer satisfaction measure to actions employees could take on the front line.

Each year, the leadership mandated that executives reach new goals of their key customer metric called NSAT to get their bonuses. At the same time, executives felt like they had no operational levers with which to move the strategic needle. They would pass down the goals to their managers, saying, "Do your best. We'll see what results we get next year." Since executives didn't have a line of sight control on action to move NSAT, they disregarded the bonus carrot and took whatever they got—or usually didn't get—at the end of the year.

So the company's leaders made a serious effort to close this gap. The Customer and Partner Experience (CPE) team began by analyzing satisfaction data. They developed a "driver framework" to prioritize what was impacting customer groups' happiness. The team consulted with managers to identify operating measures they used, or would like to use, to make positive progress. Next, the team conducted a variety of driver analyses on the metrics to statistically validate which ones made a difference.

		① Created Dashboard Framework from Strategic Customer Research	② Engaged managers to: • Understand their operations & data • Identify & conceptually align metrics • Screen metrics using managerial criteria	③ Collected Data & Linked Statistically
Products	Reliability	# of system breakdowns		✓
		% of product functionality utilized		—
	Easy to Use	# of product complaints		✓
Technical Support	Solving Problems	First call resolution rate		—
		Average time to resolve problems		✓
	Product Knowledge	% of customers with Support Contracts		—
		% of certified Technical Support reps		✓
Account Management	Understands Needs	Average Account Manager tenure		✓
		# of Decision Maker profiles		—
	Engages in Planning	# of face-to-face planning meetings		—
		% of customers with updated plans		✓

Correlations

The Microsoft executives now had a complete picture showing what priority operating metrics would affect NSAT. At the operating level, actions included more effective communications with clients, recruiting clients to training events and more disciplined account management—related to the priority metrics (illustrated below).

Microsoft could now directly transfer customer-specific goals onto a person's performance management plan. In turn, executives could use the performance management process as the basis for the annual incentive program. *Voilà!* The company could link the NSAT strategic measure to priority operating metrics then convert to personal goals used to payout annual bonuses.

Insight
Customers with latest software are most satisfied

Actions
Deploy latest software through:
- Communications
- Training
- Account Management

Results
Reap the benefits

The framework delivered a wonderful side benefit. To raise NSAT, operational managers could target specific goals for their teams and individual staff members. On a major account, for example, they realized that the client was not enrolling people in training programs. They turned this into a quantified goal for one individual: to "ensure that our major client sends at least five people to each of the three training sessions scheduled for next fiscal year."

Innovative Performance Management – **Allstate**

It isn't easy. Many companies wrestle with connecting customer measures to performance management and compensation to build buy-in, drive commitment and focus staff on customer-centric behavior. Often in the early stages, it is best to measure individual performance and pay for "activity," with the goal of transitioning to performance metrics more closely tied to the customer measurement system.

Allstate Insurance Company, the U.S.'s largest publicly held personal lines insurer, has gradually refined its reward systems—from the executive level through middle management and broadly across frontline employees. The company has aligned staff with Allstate's research results into the drivers of customer experiences, attitudes and behaviors.

Recently, Allstate rolled out an innovative way to match customer metrics with long-term rewards programs: namely, the Allstate corporate 401(k) (a U.S.- based private pension system) match. Allstate tied the variable portion of the company match to improvement in its position on the Customer Loyalty Index. The index is Allstate's metric gauging customer sentiment on three core loyalty drivers: overall satisfaction, likelihood to renew and likelihood to recommend Allstate to others. The company invests all its contributions in the Allstate Stock Fund. This is a clear connection of the employee-customer-value chain in a single mechanism. It immediately captured the attention of a wide range of Allstate staff, signaling the importance of improving Allstate customer metrics.

It's not all about compensation, though. Strengthening corporate cultural attributes related to customer experience management requires that leaders align hiring, promotion, performance and career management processes—from the senior executive level to frontline people.

In this area, Allstate has taken "rising stars" (promising new managers in its Talent Acceleration Program or TAP) and placed them in critical Customer Experience Management roles throughout the company. Not only does this tactic bring key talent to bear on customer-related issues and opportunities, it sends a message to aspiring managers about the importance of customer service at Allstate. In this way, the company is not overly reliant on compensation-based customer satisfaction measurements. Allstate instead integrates broader performance management with customer-centricity.

Summary

Checklist:
Connecting the employee-customer-value chain

Without doubt, playing with pay envelopes is tricky business. How leaders decide to distribute their employees' compensation says a lot about how they manage the business, what their strategy really is, the culture they aim to create and how they value their employees. It is tempting to think that transforming into a customer-centric company is as straightforward as putting customer goals and metrics on every employee's job profile and rewarding five-star service. In principle this is accurate, though implementation is never that simple.

Here's a quick checklist for managing the pitfalls:

▶ Commit to linking customer metrics to compensation

▶ Address potential gaming:
  - Select simple customer experience metrics.
  - Set targets relative to internal or external benchmarks.
  - Use customer metrics within a balanced framework.
  - Investigate closed loop feedback.

▶ Learn from case studies of proven successes:
  - Recognize that the process is organization-specific.
  - Invest in communication, training and support.
  - Seek expert guidance when you need help.

You can transform your company to a customer-centric organization if you approach the task equipped with knowledge, patience, and the right tools and support. In the end, aligning the employee-customer-value chain is well worth the effort.

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About Ipsos Loyalty

Ipsos Loyalty is the global leader in customer experience, satisfaction and loyalty research with over 1,000 dedicated professionals located in over 40 countries around the world.

We collect, integrate, analyze and model a vast amount of both unstructured and structured data on a regular basis. Our modeling & analytical expertise, technological capabilities, and EFM partnerships enable us to offer creative solutions that build strong relationships and lead to better results for our clients.

This has made us the trusted advisor to the world's leading businesses on all matters relating to measuring, modeling, and managing customer and employee relationships.

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