

What are merit increases, and how to implement them?

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Unscheduled salary rises or incentives for qualified employees can go a long way toward increasing loyalty, keeping top personnel, and boosting morale. However, doing so without a strategy can have the exact opposite effect.

What Is a Merit Increase?

Merit increases are intended to reward the most productive and high-performing employees, incentivizing others to do better as well. However, employees will be confused, upset, and, ultimately, less productive if merit raises are given on the spur of the moment or if there isn't a clear understanding of how to outperform and obtain the rise.

A merit increase is a salary boost given by an employer to a specific employee based on their work performance. People get merit raises based on the value of their capabilities, as the name implies. Some firms award merit raises every year, while others may award merit raises in reaction to outstanding performance. Employers frequently utilize merit increases to raise employee compensation incrementally based on performance, with the highest-performing employees receiving the largest percentage rise.

Why do companies give merit increases?

Companies give merit raises to encourage employees to meet performance goals and foster a strong work ethic. The premise behind merit raises is that providing more opportunities for employees to achieve will drive them to work harder, resulting in increased income for the organization. By rewarding workers for good work, merit hikes can enhance employee retention and loyalty. They link employee conduct to financial performance and, when effectively implemented, drive all employees to improve their skills.

Merit increase vs pay raises

A merit increase is a type of pay raise offered to employees based on their performance at work. It is frequently used to recognize and reward the company's top performers. As a result, employees may be motivated to achieve corporate goals by associating their efforts and ambitions with a raise in pay.

Assume Joanna is a high-performing employee who exceeded the company's targets by 5% that year. As a result, she would get a merit increase in her paycheck due to her efforts. On the other hand, Ashley would only be paid her regular wage if she worked for the same company because she was unable to meet or surpass the firm's goals.

On the other hand, a pay rise is an increase in an employee's income that is unrelated to their success at work. As a result, a pay raise is frequently a compensation rise distributed evenly across the board. So, if Joanna and Ashley have the same job title and work for the same company, they will very certainly both receive a similar boost when it comes to the company's yearly pay boost.

What is the average merit increase?

Merit raises are often a small percentage of your overall income, averaging around 3% on average. However, depending on where an employee's performance ranks within the organization, a corporation may offer a 1% merit raise to one person and a 10% merit increase to another employee. Therefore, when interviewing for a job, inquire about how annual raises are handled and whether high-performing employees receive additional merit increases.

How do cost of living adjustments affect salary increases?

COLAs (cost of living adjustments) are a raise in pay to reflect increases in the cost of consumer goods and services purchased by the average person.

COLAs and merit increases can be perplexing because they have nothing to do with the two elements that drive wage increases: Market Price and Internal Value. COLAs, on the other hand, have an impact your compensation because they are a form of pay boost that is used to reflect inflation in the cost of products and services. As a result, the employee's salary will be affected in the long run.

For example, if annual inflation rises by 2%, it may be prudent to raise your employees' salary by 2% to ensure that they can still cover their basic living expenses. Likewise, if an employee relocates to a new city with a higher cost of living, you can consider making a compensation adjustment to match the market price of what the person would be worth if employed by another company in the new location.

Choosing between COLA and merit increases

Consider using the cost of living adjustment to adjust an employee's wage to account for the rise in basic living expenditures.

If, on the other hand, the person is performing really well, such as exceeding your organization's goals, you may want to consider giving the high-performing employee a merit increase as a reward for their work.

Why do merit increases matter?

This is a step in the right direction in many circumstances (apart from the cost of living adjustments). However, rewarding poor performance can lead to poor results, which can have a negative impact on employee morale. Exceptional colleagues "trump everything else when it comes to employee engagement," as the former Netflix Chief Talent Officer noted in this HBR article.

Salary hikes can also encourage difficult-to-find top performers to stay with the organization for more extended periods. According to Glassdoor data, there is a strong link between pay and retention; thus, wage increases can be utilized to reward and keep employees whose flight risk is also a business risk.

Advantages of Merit Increases

Below are some of the advantages of using merit increase:

a. Emphasizes business objectives

Merit raises are a powerful tool for showcasing the type of performance you expect from your staff. Setting a baseline and rewarding above-average employee performance can assist employees to understand how much the organization values their work?

b. Identifies individual performances

Merit increases assist managers in identifying individual employee performance rather than team performance. Knowing how to spot underperforming employees entails recognising flaws and pointing out areas where each employee may enhance their performance.

c. Improves company standards

Firm management's KPIs determine merit increases. This implies that there is always a standard to adhere to in order to distinguish between good and bad performance. Employees are more likely to follow and exceed fundamental criteria if they are rewarded for good performance.

How can HR Professionals Effectively Implement Merit Pay Systems

A step-by-step guide to creating and implementing merit pay systems;

1. Develop merit pay plans and strategies.

1.1. Calculate merit pay.

You can look at your entire merit budget and which divisions are critical to reaching your company's goals to determine your merit increase. The more essential departments in achieving the company's goals are given bigger merit raises budget under this strategy. Otherwise, you can use each employee's or group's average salary as a benchmark for evaluating merit pay.

Merit pay should not be combined with other pay increases. Merit pay recognizes the accomplishments of individuals or groups, and it should be distinguished from generic raises for all employees or wage modifications due to market fluctuations.

1.2. Determine metrics employees must meet to earn a merit raise.

It's critical to spell out the criteria that employees must achieve to be considered for merit pay. You should include some flexibility in your KPIs, especially if your company operates in a competitive field where it is critical to retain top employees. Companies can give incentives to help keep high-performing staff in this situation.

1.3. Develop a strategic plan for the year.

Companies must have clear, well-planned guidelines for their merit programs to provide fair, unbiased incentives to employees that do not produce irritation or disharmony among them.

Consult with top management, finance, and HR departments to develop a plan that includes goals, timetables and evaluates your merit pay system's overall success.

1.4. Determine departmental and company objectives.

Companies must have clear, well-planned guidelines for their merit programs to provide fair, unbiased incentives to employees that do not produce irritation or disharmony among them.

2. Create merit pay policies.

2.1. Meet with departments to develop policies.

Develop efficient merit pay policies in collaboration with representatives from each of the relevant departments. You'll need to explain these policies to employees once they've been created.

Consider the foundations of your company's strategy and goals, as well as individual and team goals, incentive structure, calculation methods, prospective payouts, and the merit pay system's timetable. Then ensure that each individual understands and agrees to these policies.

2.2. Define employee performance in measurable ways.

Use various information sources to assess all aspects of employee performance and establish accurate and trustworthy performance evaluation methods.

Make a distinction between team performance compensation for meeting project goals and individual performance incentives, such as pay increases, promotions, and bonuses.

2.3. Agree on a compensation plan.

Unless otherwise specified, merit pay should be based on the sustained individual performance of normal duties rather than projects or events. Personal and team goals and assessment procedures must be clearly defined and agreed upon.

3. Implement merit pay systems.

3.1. Communicate employee performance.

When certain efforts are rewarded while others go unappreciated, employees may grow disappointed or discouraged. Managers, supervisors, and team leaders should be trained to convey employee performance clearly and concisely. These individuals should be held accountable for effectively implementing merit pay schemes.

3.2. Use incentive compensation management (ICM) software.

Compensation technologies that are connected with people management and business analytics can help managers with their administrative responsibilities. Managers will be able to make educated pay decisions with the correct technologies.

4. Review your merit plan.

4.1. Get feedback.

Discuss the success of your merit pay system with managers, supervisors, and employees—especially those who are leaving the company—and track the results. Then take the necessary steps.

It's critical to solicit input throughout the year and change your merit pay policy as necessary. For instance, if none or a small number of your employees are achieving the performance criteria for merit pay, it may be time to reconsider your expectations. Unrealistic goals can demotivate personnel, so make adjustments as necessary.

4.2. Amend merit pay policies.

Meet with the appropriate stakeholders to define new goals and develop improved tactics, reward structures, payouts, and timetables if your existing merit pay program isn't working as well as it should.

Keep in mind that a merit pay scheme that works for one department or team might not work for another, so make the appropriate adjustments.

Keep an eye on how the merit pay system you've introduced impacts the workplace culture and relationships between coworkers. If there is too much negative competition, for example, and employees begin to undercut one another, you might want to seek healthier options like group incentive compensation.

4.3. Communicate changes to all stakeholders.

Once a new merit pay policy has been designed, have it approved, and make sure that supervisors, managers, and team leaders inform employees in their departments about the changes. Ensure that a copy of the new policy is sent to all stakeholders.

Encourage employees to voice any issues or questions regarding the new policy as soon as they occur.

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