



*How Variable  
Compensation Programs  
Affect Employee Morale,  
Motivation, and  
Productivity:*

Research-Backed Findings to Help You Craft  
a Highly Effective Variable Pay Program

## Executive Summary

With salary expectations skyrocketing in every role across the workforce, many organizations are determining that the best way to battle pay compression is to offer more variable comp opportunities. In fact, according to a recent WorldatWork survey, 84% of organizations rely on variable pay for employees.

Whether your organization is considering implementing a new variable pay program or expanding a program you already have, it's important that you structure your program properly so you can get the results you want.

### *This white paper helps you:*

- Learn 5 strategies that can prevent potential pitfalls in your variable pay program
- Find out science-backed tips on how to combine variable comp programs with other complementary initiatives, so you can maximize your business gains
- Understand and avoid the top variable pay issue that can demotivate employees
- Overcome the one big drawback that all properly crafted variable pay programs share
- Save time with a handy checklist that speeds up your research if you choose to evaluate variable compensation software solutions

Have questions? We encourage you to contact the EthoTech team. With 20+ years in the industry, you can trust us for knowledgeable, accurate advice that can help you solve any variable comp issue related to Microsoft Dynamics GP. That's all we do, and we do it better than anyone.

We look forward to chatting with you,

*The EthoTech Team*

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## 5 Smart Strategies for Crafting Your Variable Pay Program

*If you're planning to institute or change your variable pay program, you should know that these types of programs can make employees act in surprising ways. It is important to structure your programs appropriately. As in all strategic decisions, forewarned is forearmed.*

One of the biggest potential pitfalls of any variable comp program lies in the fact that **measurable** goals are not always **worthwhile** goals. Sure, tidy measurements can be extremely appealing, but the easiest tasks to measure are not always the most valuable tasks to accomplish.

For example, the length of this white paper is easy to measure (3826 words), but our goal in writing it wasn't to publish a lengthy white paper. The goal was to help you out by providing useful tips for crafting a successful variable pay program. A longer, more informative white paper is more **likely** to achieve that goal of course, but it certainly isn't guaranteed. It took time for us to dig deeper and figure out alternate metrics that better aligned with our objectives.

*Here are our 5 hard-earned tips that can help you ensure success when you're crafting your own variable comp program:*

**1** *Ensure that any KPIs you tie to your variable pay accurately reflect your company's overall goals, and that they are not just measuring what you assume can serve as a proxy to those goals.*

Whatever you do: **don't** make the mistake that Wells Fargo did when they tied employee performance evaluations and pay to account openings.

In that chilling cautionary tale, employees were rewarded based on the number of new accounts they opened. To boost their measurements, some staff members chose to move small amounts of existing customer deposits into new accounts under the customer's name. Then they would close the new account and transfer the money back into the original account later. While this practice helped Wells Fargo team members meet their sales quotas, it annoyed customers and did absolutely nothing to further the bank's underlying strategic goal of increasing new customer accounts.

Yes, the employees engaged in reprehensible, fraudulent behavior to “earn” their incentive-based pay, but the whole issue could have been avoided had Wells Fargo leaders taken the time to identify better ways to measure for their real goals.

Aside from checking that your measurements accurately reflect your goals, you should also:

## **2** *Check that stated incentives are easy to understand and are achievable, so you don't run into any misunderstandings down the road.*

Example: If you are offering higher payouts to salespeople who break into new geographies, make sure to be clear whether those margins apply to new geographies for the salesperson or new geographies **for the company**. Then, make sure the salespeople have the tools they need to accomplish that.

## **3** *Ask good questions, so you can make sure your company goals and variable comp programs align with personal or departmental goals.*

This is specifically important in cases where a long-term company goal may conflict with a department or individual's opportunities for growth. For example, perhaps you offer a sizeable performance bonus to your product management department leader for a new product rollout that will take 4 years to finish, but...

...Unknown to you, the department leader has planned to continue her career trajectory by moving up and out of that department within 2 years. That situation will lead to a conflict, but asking questions can avoid that.

## **4** *Verify that all variable comp programs you put in place, even short-term ones, promote sustainable, long-term behavior among your staff.*

This comes up most often when your variable pay is based on an outcome, such as selling X quantity by Y date (as many quotas are), which can result in ebbs and flows in performance. If salespeople aren't near the goal, or have already surpassed it, they may stop trying.

Alternatively, if your variable compensation program is based on long-term, sustainable behaviors, such as following up on new leads within X number of hours, it will build a habit that should result in more sales consistently over time.

## **5** *Ensure that your programs are fair and equitable.*

One good way to measure this is to use the “printer test.” Ask yourself: “If an unsuspecting employee discovered a copy of the variable compensation program in the office printer, would it pass the fairness test?” If not, make sure you update that program immediately.

# Surprising Ways That Variable Comp Affects Motivation

*We've all heard the aphorism that "employees are your greatest asset," but we all know that employees are also your greatest cost. The upshot of this is that employee productivity gains can directly result in profit gains for you.*

A fascinating [article](#) by **Harvard Business Review**, "The Surprising Economics of a 'People Business'," points out that "if employee costs are five times assets... then it takes only a 5% increase in employee productivity or a 5% reduction in employee costs to increase profits by 25% of assets."

So, can you use variable compensation to increase employee productivity? Let's talk about that.

In an different, highly acclaimed **Harvard Business Review** [article](#), "Employee Motivation: A Powerful New Model," psychologists examined the 4 drivers that impact employee motivation. #1 was "the drive to acquire," and researchers showed that employees are very motivated to acquire a range of common variable pay offerings, including money, travel rewards, and entertainment bonuses.

The article also demonstrated that "when employees report even a slight enhancement of the fulfillment of any of the four drives, their overall motivation shows a corresponding improvement; however, major advances relative to other companies come from the aggregate effect on **all four drives.**" (emphasis ours)

*In other words, your company is likely to increase employee motivation by offering variable compensation programs – but if you want to maximize your business gains, you should consider pairing those programs with initiatives like:*

- *Building team camaraderie and culture*

This satisfies "the drive to bond," and shows the importance of team-building events. Make these events even more impactful by combining them with recognition ceremonies, in which you highlight your most productive salespeople and their corresponding rewards.



**TIP:** Another great way to share recognition is to set up a regular email that showcases which of your salespeople are doing best on their goals. A good variable compensation management software solution can help you automate these emails, so you can effortlessly keep your team motivated.

- *Offering work that is challenging and fulfilling to employees*

This satisfies “the drive to comprehend,” and shows the importance of providing skill-building opportunities for your salespeople. Find out what they’re interested in and help them use their passions to drive their next big project. Perhaps they want to expand into more geographies, or perhaps they want to focus on a new segment. Whatever they want, it’s probably a great opportunity to drive further productivity.

**TIP:** Leverage the power of flexible variable pay management software when you want to fold individualized stretch goals into new variable compensation offerings with very little effort.

- *Maintaining transparent rewards*

This satisfies “the drive to defend,” and shows the impact of transparency and fairness on employee motivation. This drive is what inspires healthy competition quarter after quarter, which is why it’s so important to ensure that your variable pay calculation process is quick and easy, so you can stay up to date.

This is also why it’s important to verify that your variable comp programs are equitable. You can use the “printer test” we mentioned earlier to check this.

**TIP:** Using variable pay management software that's integrated with your ERP can help you make sure that your sales team can easily track their always up-to-date progress toward their individual and team variable pay goals.

### *Warning: Variable Pay May Hinder Employee Motivation and Productivity in the Long Term*

Of course, there's a catch. It's that you can't stick with the same variable pay program long term.

Though many articles online imply that variable payments positively impact motivation long term (here's [one](#) and here's [another](#)), you'll notice that they don't cite sources for their implications or that they misquote those sources. It's a bit strange.

As it turns out, when you track down top sources and quote them accurately, peer-reviewed, published research studies tend to demonstrate inconclusive or very little evidence in support of the idea that variable compensation motivates most people to achieve higher productivity **over the long term**.

Worse, many studies suggest that variable pay can actually demotivate us as time goes on because they transform our intrinsic motivation into extrinsic motivation, and extrinsic motivation exhibits a weaker correlation with exceptional performance.

Sadly, one [study](#) showed that although variable compensation can increase task completion over the short term, it was also associated with the perception that work was more intense. As the researchers behind that study concluded, "performance-related pay may be experienced as a burden that only provides extra pay for workers through an intensification of the work process... [which] raises critical questions regarding the extent to which individual-based incentives can influence employee well-being in a sustainable way."

In other words, it is extremely important that you frame your variable comp programs as short-term goals, rather than long-term ones.

In our experience, the best way to make sure your variable pay goals don't fall into long-term territory is to change goals frequently. We recommend that you aim to have a new goal every month or quarter for each of your employees and teams, so you can maintain strong productivity.

# Using Variable Compensation to Improve Employee Morale

*Assuming a safe working environment with reasonable job security, employee morale usually comes from each employee's personal calculation of salary + benefits + job satisfaction + variable compensation. As it turns out, variable comp can become a surprisingly hefty factor in this equation.*

*When it comes to fine tuning your employee pay structures, it's best to think carefully before you make any concrete moves. As your team discusses the possibility of implementing a new variable comp strategy or updating your existing one, it would be wise to keep these 3 key points in mind.*

## 1 *Performance pay has a widespread positive impact*

In the last chapter, we discussed the research surrounding how performance pay impacts employee productivity and motivation. We determined that performance pay certainly increase productivity over the short term, and the following research shows that it boosts employee morale too.

According to a study in **Human Resources Management Journal**, researchers determined that performance-related pay was “positively associated with job satisfaction, organizational commitment, and trust in management.” Clearly, this form of variable pay pays off with big dividends.

## 2 *Bonuses can increase workplace happiness*

With bonuses down 21% YoY in December 2023, a Q4 2023 survey from BambooHR found that employees are currently wallowing in a 4-year low of unhappiness. Good news though: aggregate data from 57,000 employees across 1,600 companies suggested that bonuses were one of the top measures that would increase workplace happiness.

At your company, you may find that you can double your morale-boosting tactics by combining these approaches. One idea is to offer performance-based pay for some employees and annual or quarterly bonuses for all employees, dependent on company performance.

### **3** *Your variable comp structure must match your culture*

For some companies, bonuses and performance-related pay shouldn't be tied to individual accomplishments. If you worry that incentive-based pay for individual team members could lead to unhealthy competition, gamesmanship, or sandbagging at your company ([this is a legitimate concern](#)), you may want to create group incentives instead. After all, you're trying to improve morale, right?

Keep in mind our advice from Chapter 1: Just as you did with your individual incentives, you should ensure that your group variable compensation awards align with your top-level company strategic goals.

### *How to Improve Employee Morale and Your Bottom Line at the Same Time*

Worried that offering variable pay at your business may simply cost too much in the long run? You'll be relieved to hear that variable comp programs aren't solely beneficial for employees – they can benefit your company's bottom line too.

An article in the **American Business Review** (see appendix in [this source](#)) shows that shifting to more variable compensation can help reduce your organization's breakeven point. This results in your company being able to be profitable faster.

Of course, you will want to make sure you don't accidentally increase labor hours due to administration and management of your new variable comp programs. Variable comp software can help you keep labor hours low and variable pay flexibility high.

# How to Overcome the One Big Drawback to Any Variable Compensation Plan

*Let's talk about the elephant in the room: complex commission calculations usually lead to late or non-transparent data sharing for your commission earners. Fortunately, there's a way you can address this problem head on.*

Okay, so you're ready to begin the strategic process of setting up or adjusting a variable compensation plan at your company. Before you begin, you should know that properly crafted variable comp plans all share one really big drawback:

## You must maintain up-to-date, transparent data.

Why? Because updated, easily accessible data not only promotes better revenues, it also demonstrates that your company is honest. As we've already discussed, it shows that you prioritize your staff's happiness and that you will make sure to promptly reward them for their hard work.

Unfortunately, the double- and triple-checking required to prevent typos in manual variable comp processes take so long that they make transparency nearly impossible.

Let's talk about what makes those processes so complex, and how you can simplify them to achieve greater transparency.

## What Makes a Variable Compensation Plan Hard to Manage?

Since you're reading this white paper, we can safely assume that you have quite a few commissioned salespeople who are spread across different geographies. If you're following best practices for variable compensation plans, we can also assume that each commissioned salesperson has an individualized plan that is tailored to motivate them specifically.

That means that:

- You have multiple plans to manage along with the need for one-off adjustments; and
- You manage multiple regions, each featuring different legislation for cities, counties, states, and countries.

Already, this is complex... **but it gets so much worse.**

*Companies also typically calculate commissions with:*

- Multiple payments for one salesperson, such as if they are the sales rep and the sales manager and therefore will have different rates in a single sales document
- Different variable compensation plan awards based on sale, margin, quantity, quotas (AKA accelerators, milestones, thresholds, or tiers over time), margin quotas, or tier-based sliding scales
- Multiple commissionable and non-commissionable salespeople contributing to a sale, requiring split commissions that each have their own variable rates that apply to different salespeople, customers, or products. These may also have different payment timelines, such as for when an invoice is posted, or when it's paid
- Complications arising from aging invoices, write offs, markdowns, trade or term discounts, varied payment terms, and different incentives for different credit card types

When you have to manually calculate commissions that include some or all of these variables, commissions management can balloon into an exhausting, multi-day task.

Even a single typo can result in a cascade of errors, so commissions processing takes extreme attention to detail and, often, some very late nights. Most reasonable people have no interest in providing timely, transparent insight into a hectic process like that. Would you?

Fortunately, there is a better way.



# A Proven Method to Streamline Your Variable Comp Process

*Many companies have been struggling with commissions calculations and variable comp processing for so long that they cannot envision how easy these processes should be.*

Fortunately, with the right setup, your company can easily achieve a timely, transparent end-to-end process, and you and your staff can experience the stress-free commissions processing you deserve. Really!

*Here's the secret to success:*

*Automate your commissions processes.*

When you automate your commissions processes, you can finally get error-free tracking, calculations, reporting, and payments. Some systems even empower you to automatically notify salespeople and managers about the progress of their variable compensation plan.

*Yes, this will require you to invest in variable compensation management software.*

If you're ready to start the software evaluation process, the following checklist can help you save time on your research and evaluation process.

# 7 Things to Look for in Variable Compensation Management Software

*Don't waste time implementing and training on the wrong variable compensation management software solution. Create your shortlist of solutions to research further by narrowing the list down solely to the options that feature these 7 critical capabilities.*

## 1 *Seamless ERP Integration*

Ensure that your variable comp management software is seamlessly integrated with your ERP or accounting solution, meaning that the two solutions can securely and quickly share data back and forth.

You shouldn't have to jump in and out of various programs, databases, and spreadsheets to find critical commissions data. ALL of your variable compensation management data and tasks should be available in ONE program.

## 2 *Flexibility to Make Changes Anytime*

Your solution should enable you to confidently change any aspect of your variable pay programs or commission structures at any time and give you the ability to run 'what if' recalculation options too.

To save time once you make your preferred changes, ensure that your system will flow your adjustments through to any other commission structures that are impacted by the change.

## 3 *Makes Your Job Easier*

Give yourself the opportunity to enjoy a faster close and on-time, accurate variable pay processing with software that makes it easy for you to auto-run reports and payments with just a few clicks.

During your research or evaluation process, ask to see the exact process it takes to run reports and payments. If it takes more than a few minutes, that software will be a waste of your time.

## 4 *Delivers Empowering Insight*

A good variable comp management solution should provide centralized data lookup, empowering you to access all your commissions data in one place. This helps you quickly and accurately answer questions you or anyone else on your staff may have.

In addition, ensure that the solution you choose offers a comprehensive picture of your commissions liability at any time, so you can always track your payments throughout the month.

## 5 *Streamlines Report Sharing*

Make transparency effortless by looking for automated variable comp software that gives you the power to quickly and regularly email up-to-date commission reports to managers, individual salespeople, or other variable pay recipients.

The best option is to look for a solution that offers flexible email template capabilities, which enable you to set up a commission report email template once and then distribute multiple, fully personalized reports to anyone who needs them.

## 6 *Expert Implementation & Support*

Make sure you **only** purchase your variable compensation management software from a seller who knows the software inside and out. Buying directly from the developer can often be your best bet, but a knowledgeable reseller can be fine too.

To save time and reduce errors, check that your implementation team has extensive experience with both the variable comp solution and your ERP, so you can get your system set up right the first time and count on having expert support over the years.

## 7 *End-to-End Functionality*

A good solution should handle everything that relates to your commissions – and we mean **everything**. Whether you want to change your commission structure rules, enter data, calculate commissions, run reports, distribute reports, or make payments, your variable comp solution should be able to handle all tasks with ease.

And finally, make sure the solution you choose has the ability to handle modifications **after payments have been posted**. You would be surprised at how few solutions have this capability, and you don't want that headache down the road.

## Take the Next Step

Congratulations! Now that you have read this white paper, you understand how to craft your variable compensation plan to maximize employee motivation, productivity, and morale. You also have some great tools in your belt that will help you craft the smartest, most effective variable pay program for your specific needs.

*Now it is time to make your plan.*

*Your Commission Plan, that is.*

Companies that rely on [Microsoft Dynamics GP](#) can [relieve every variable comp headache](#) and complexity listed in this white paper **and** ensure that they provide transparent, on-time variable comp data, every time. All it takes is Commission Plan for Microsoft Dynamics GP.

[Learn More About Commission Plan for Microsoft Dynamics GP.](#)

## About EthoTech

*Since 2002, companies across every sector have relied on EthoTech and our flagship solution, [Commission Plan for Microsoft Dynamics GP](#), as the right tool for tracking, calculating, and paying variable compensation.*

*We provide solutions, integration, and support that is focused solely on integrated variable compensation software for Microsoft Dynamics GP.*

*It's all we do, and we do it better than anyone.*

