

Performance-based compensation must be financially sustainable

There is perhaps no part of performance-based compensation that is more regularly abused than the approaches to long-term financial sustainability. Some districts wait until the close of a pilot before focusing on sustainability. Others claim that long-term financing will result from foundation grants or cost savings in other parts of the organization. There are districts that encounter difficulties in forecasting costs even during the pilot phase. The history of pay-for-performance is replete with projects that have been terminated for lack of funds. These are recurring examples of poor policy and misguided practice.

If performance-based compensation is tied to student achievement and achievement increases over time, it will cost more than current approaches to teacher compensation based on steps and ladders. Moreover, the source for long-term financial sustainability is public dollars. These baseline understandings need to guide planning for the long term.

Scaling up is a function of pilot success and sustainable financing. Consequently, it is important that there is real clarity regarding the benchmarks that will be used to determine that success and, assuming success in meeting the benchmarks, the financial targets that the district will commit to in order to sustain the reform. Absent such clarity and commitment, teachers lose faith that scaling up will actually occur, both teachers and the broader public begin to question the value of the initiative, and the initiative fails to advance beyond the pilot phase. In this regard, financial sustainability is interconnected with financial credibility; people need to believe that the effort will be sustained.

Planning for long-term financing should begin at the start of the initiative and continue throughout subsequent phases of implementation. It should take into account costs above and beyond those that go directly to compensation changes such as the costs of building new data systems, developing or acquiring new assessments, and expanding professional development opportunities. Preparing for financial sustainability involves the use of human resource modeling and financial modeling—distinct departures from current practice in most districts.

Transitioning to a new compensation system

District, union, and board leaders need to make the most informed decisions possible regarding the design and implementation of performance-based compensation for teachers. These leaders require reliable information on the types of costs associated with each strategy *before* making any decisions on components of the compensation plan, the design of a pilot, or larger scale implementation.

Mistaken beliefs and erroneous considerations about cost have been the bane of many failed compensation reforms. It is therefore necessary to identify how costs associated with specific options appear in the short-run, how they are likely to evolve over time, and how they can be affected by associated organizational, transition, and phase-in costs.

Forecasting and analyzing the range of financial exposure for each option and strategy is not a process that can take place behind closed doors or that can be masked by a leader's claims of "the money will be found." It requires transparency and addressing the concerns of a district's diverse publics.

A starting point is to examine the differing costs of salary, stipends, and retirement, and the organizational costs characteristically associated with adjusting old systems or monitoring the effectiveness of new ones. The district should then discuss how changes in one cost area are linked to changes over time and in other cost areas. Taking this approach better positions a district to organize and establish priorities for potential compensation reform strategies.¹⁰

Human resource and financial modeling allows a district to create a staffing picture, which in turn provides a basis for predicting the cost of compensation reform.

An example highlights the critical importance of taking this approach. There is much concern over the repeating pattern of new teachers leaving districts at alarmingly high rates within their first four years of teaching. When they are replaced, the same pattern recurs with another group of incoming teachers. It perpetuates a flow of less experienced teachers within the system who are often assigned to the highest needs schools. It is widely accepted that this dynamic works to the detriment of schools, teachers, and students. Yet it is also how districts in part balance their budgets—new and inexperienced teachers cost less.

These dynamics change dramatically if a district is successfully implementing performance-based compensation. When teachers are supported as professionals and nurtured as instructors, the overall levels of teaching excellence and student achievement increase. Teachers are also more likely to stay in the profession longer. The reduction in turnover cuts induction costs, but this is a one-time gain while the other costs keep increasing. If the compensation system rewards teachers for their contributions to student achievement, and a greater number of more successful teachers stay in a district for longer parts of their careers, it costs more. Pure and simple, performance-based compensation costs more.

The objective is to establish a system of sustainable compensation where teachers develop their professional careers within a stable environment. By using the models to estimate costs, districts have a basis for tracking actual costs during both the pilot and later years of implementation.

Sustaining the compensation system

Cost projections have to be extended into longer timeframes as the elements of the compensation plan begin to involve changes over time or cumulating costs, as with salary and pension. These projections ensure that the district and community are aware of longer-term consequences. Finances in Denver, for example, were projected out over a 50-year district timeframe and a 30-year teacher career timeframe. If these cost projections over time use constant dollars—purchasing power adjusted for inflation—all parties have a realistic understanding of what is involved financially.

These projections also help a district and union understand the different costs associated with specific implementation strategies. For instance, plans that phase in changes—as with a pilot followed by larger-scale implementation—have increased costs over time. Components that require revamping current procedures may have only one-time organizational costs. Components that require new and ongoing monitoring—such as tracking whether incentives are encouraging teachers to attain master’s degrees or pursue professional development that matches their teaching specialty—can have significant continuing organizational costs.

It is particularly important to give attention to choices that involve salary changes. Much of the current wave of compensation reform consists of short-term bonus programs. Yet that is neither the only nor necessarily the best way to craft the compensation reform. For example, paying for achieving student learning objectives or serving in high-needs schools can be offered as bonuses, additions to base compensation, or some combination of these approaches. Here again it is essential to learn, both from teachers and ongoing research, which approach is more likely to incentivize which specific outcomes at the schools. If teachers indicate that eligibility for a smaller addition to base compensation is more of an incentive than eligibility for a larger annual bonus, then that has to be considered in the design and cost analysis. This level of planning is all part of achieving financial sustainability, particularly when retirement and pensions are involved in a total compensation package.

To build a broad base of understanding of the possible impact of a new compensation plan, it is also important to develop a structure for organizing all cost estimates associated with each potential compensation strategy. For teachers, the organization of cost estimates can be by career stage, so that they can compare alternatives in a meaningful way. For schools, the organization can be by grade level and student characteristics, so that the district can compare costs across different categories of schools. For job categories, the organization

can be by level of school and broad job classifications, so that a district can target pay structure changes to specific personnel.

Effective analyses need to delve beyond simple cost assumptions to also identify the nuances underlying the proposed compensation changes. For example, the cost of induction programs varies based on whether they are offered to those without teaching experience, those new to a district, or those who were not classroom teachers in the district the previous year. The analysis should generate estimates of the cost of each option and an estimated range for the overall costs.

By taking this approach and doing so transparently, the use of human resource and financial modeling enables a district to project costs for any of the targeted compensation changes, while building a collaborative understanding of the options with teachers and external publics. When mid-course corrections are considered, the understanding of the financial implications informs the decisions.

As decisions about the components are made and accumulate, the long-term funding picture becomes clearer. As this occurs, a district can prepare to identify funding sources to pursue. If it cannot identify or secure sufficient funding, it will be necessary to revise the proposed reforms. Making cost estimates of revised packages, involving trade-offs among components unrelated except by cost, is part of the process. Particularly in states that have collective bargaining, knowledge about the prospective funding sources has to be shared among the negotiating parties.

If the legislature or electorate needs to make a formal decision, then a district will be prepared with cost estimates to help inform that decision. Such financial analyses and projections become the foundation for the efforts of communication, organizing, and campaign groups. In Denver, for example, extensive briefings on cost information were provided to the media and other interested groups before the public vote to support compensation reform, which significantly lessened the contentiousness and tension of the public discussion.

Districts should also use financial models to match revenue and expense streams over time. District revenues often follow an economic cycle while expenses follow staffing patterns, so a means of adjusting the two is an essential component in any compensation system change.

Doing business differently

The costs of doing business differently—recasting district priorities and reallocating district resources—are an often-ignored part of compensation reform. As discussed in the section on organizational sustainability, aligning and improving the quality of district services to the schools requires management effectiveness in using existing resources, not just on the influx of new finances. These are the costs of real institutional change.

Bottom line

District and union leaders should use human resource and financial modeling to anticipate what the changed teaching force will look like over a period of years and what these changes will cost. All parties need to be well prepared to make decisions based on information related to feasibility, effect on the teaching force, cost consequences, and financing options. Such modeling and decision-making are precursors to identifying and securing long-term financing sources.

When implemented effectively, performance-based compensation costs more than prevailing teacher compensation systems. But improved student achievement can justify the costs.