



Memorandum from the Office of the Inspector General

September 26, 2019

Tina R. Shelton, LP 6C-C

REQUEST FOR MANAGEMENT DECISION – EVALUATION 2019-15626 – INDIVIDUAL PERFORMANCE MULTIPLIER

In 2016, the Tennessee Valley Authority (TVA) implemented an individual performance multiplier (IPM) that allows managers to adjust employees' annual Short-Term Incentive (STI) lump-sum payouts based on performance. This was part of an initiative to (1) strengthen alignment with TVA's compensation philosophy; (2) ensure TVA remains competitive with its peers; (3) enhance the way TVA drives a pay-for-performance culture; and (4) ensure TVA consistently manages pay using a structured, fair, equitable, and market-based approach. Since alignment between the multiplier and performance are important to the success of the initiative, we scheduled an evaluation of TVA's IPM. The objective of this evaluation was to determine if IPMs were in alignment with performance ratings.

We reviewed 5,235 adjustable payouts made in fiscal years (FY) 2017 and 2018, and found most of the IPM adjustments were in alignment with overall performance ratings. However, 59 adjustments made in FYs 2017 and 2018 fell outside the recommended ranges established in the IPM guideline. We determined some of these happened because the IPM process uses rounded overall performance ratings instead of actual calculated performance ratings.

We recommend the Vice President, Total Rewards, Human Resources and Communications, consider revising the IPM process to use employees' actual calculated performance ratings, as opposed to rounded ratings.

In response to our draft evaluation, TVA management stated they would evaluate the benefit of process changes and as appropriate, align with leading practice. See the Appendix for TVA management's complete response.

BACKGROUND

TVA incorporated an IPM component beginning in FY2016 as part of its STI initiative to (1) strengthen alignment with TVA's compensation philosophy; (2) ensure TVA remains competitive with its peers; (3) enhance the way TVA drives a pay-for-performance culture; and (4) ensure TVA consistently manages pay using a structured, fair, equitable, and market-based approach. TVA's STI includes the Executive Annual Incentive Plan (EAIP) that covers executive employees and the Winning Performance Team Incentive Plan

(WPTIP)¹ that covers all other eligible employees.² The IPM can be used to either increase or decrease an employee's annual award based on their performance. TVA's total STI paid for IPM-eligible employees in FYs 2017 and 2018 was approximately \$161.4 million.³

As part of the Performance Management and Compensation process, employees are given performance ratings for several components, which are divided into two categories: individual goals and TVA competencies. The weighted computation of these two categories are used to calculate employees' actual performance ratings, which are rounded to the nearest whole number to get an overall performance rating of 1-5.⁴ Managers are provided a guideline with recommended IPM adjustment ranges based on overall performance ratings, as shown in Figure 1 below. According to TVA, adherence with the guideline is not required and discretion can be exercised based on individual factors (e.g., challenges encountered, overachievement, and/or fulfillment of other duties). TVA's Compensation and Benefits and Talent Management departments, within the Chief Human Resources Office, provides support throughout this process.

Figure 1: Guideline for IPM Adjustments

Performance Rating	IPM-Adjustment Range
1	0.00–0.00
2	0.00–0.75
3	0.90–1.10
4	1.00–1.15
5	1.00–1.25

Since alignment between the multiplier and performance are important to the success of the initiative, we performed an evaluation of TVA's IPM.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of this evaluation was to determine if IPMs were in alignment with performance ratings. The scope of the evaluation included all IPM-eligible STI (WPTIP and EAIP) payouts for FYs 2017 and 2018. To achieve our objective, we:

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- ¹ WPTIP awards are paid as lump-sum amounts based on employees' base salary, incentive opportunity assigned to employee positions, and TVA's balanced scorecard. The balanced scorecard is TVA's primary tool in identifying and communicating the focus of incentives to the workforce. EAIP has the same components as WPTIP.
 - ² In FYs 2017 and 2018, WPTIP eligible employees included supervisors, managers, and specialists (grade 8 or above).
 - ³ This total excludes the EAIP payouts of Chief Executive Officer and his direct reports because they do not receive a performance rating like all other IPM-eligible employees. See the Objective, Scope, and Methodology section.
 - ⁴ Management can make manual adjustments to overall performance ratings.

- Interviewed TVA personnel in Compensation and Benefits, Talent Management, and Chief Human Resources Office, as well as reviewed documentation to gain a better understanding of the IPM.
- Reviewed 5,235 IPM-adjustable payouts⁵ to identify any adjustments not within the recommended ranges established in the IPM guideline for each respective performance rating.
- Contacted responsible managers for 52 of the 59⁶ IPM adjustments outside the guideline ranges (24 for FY2017 and 35 for FY2018), to obtain justification(s) for the deviations.

This evaluation was performed in accordance with the Council of the Inspectors General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation*.

FINDINGS

We reviewed 5,235 adjustable payouts (2,633 in FY2017 and 2,602 in FY2018), and found most of the IPM adjustments were in alignment with overall performance ratings. However, 59 adjustments made during FYs 2017 and 2018 fell outside the recommended ranges established in the IPM guideline as follows:

- Forty-seven adjustments were made that exceeded the guideline range of zero to 75 percent for a 2 performance rating.
- Nine adjustments were made that were either less than (4) or exceeded (5) the guideline range of 90 to 110 percent for a 3 performance rating.
- Three adjustments were made that exceeded the guideline range of 100 to 115 percent for a 4 performance rating.

We contacted responsible managers to obtain explanations for why the IPM adjustments were outside recommended ranges. The explanations included:

- IPM adjustments were based on discretion in consideration of additional factors, such as the employee (1) was new to or no longer in the position, (2) improved in performance over time, (3) performed poorly for the first time, (4) performed very well in some areas, or (5) performed other duties outside their current position when the need arose.
- IPM adjustments were partially driven by and/or made, in conjunction with higher levels of the organization, and/or their respective Human Resources partner.
- Salary adjustments were used instead of, or in addition to, an IPM adjustment.
- IPM adjustments were commensurate with the employee's actual calculated performance rating as opposed to the rounded overall rating. This was reported for 10 of the IPM adjustments that were outside recommended ranges.

⁵ We excluded the Chief Executive Officer and his direct reports from our population review because they do not receive a performance rating like all other IPM-eligible employees.

⁶ We could not obtain justification for 7 of the 59 IPM adjustments because the managers were no longer employed at TVA.

Although the individual IPMs were generally in alignment with overall performance ratings, and the explanations for the exceptions were reasonable, TVA could facilitate supervisors administration of the process by revising the guidelines to use actual calculated performance ratings (instead of rounded ratings) to determine recommended adjustment ranges. For example, if an employee's actual rating was 2.48, the current process rounds the rating to a 2, which suggests an upper limit of 75 percent based on the guideline. A supervisor would then have to go outside the guideline if they determined the 75-percent limit was too low. Revising the guideline to use actual performance ratings would more closely align with the employees' actual performance and limit the need for supervisors to go outside the recommended adjustment ranges.

RECOMMENDATION

To facilitate supervisors' administration of the IPM process, we recommend the Vice President, Total Rewards, Human Resources and Communications, consider revising the IPM process to use employees' actual calculated performance ratings, as opposed to rounded ratings.

TVA Management's Comments – In response to our draft evaluation, TVA management stated they would evaluate the benefit of process changes and, as appropriate, align with leading practice. In addition, TVA management stated they would continue to provide appropriate oversight for reinforcing guidelines and discretionary considerations. See the Appendix for TVA management's complete response.

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This report is for your review and management decision. Please advise us of your management decision within 60 days from the date of this report. If you have any questions or wish to discuss our observations, please contact John Anthony H. Jacosalem, Auditor, Evaluations, at (423) 785-4821 or E. David Willis, Director, Evaluations, at (865) 633-7376. We appreciate the courtesy and cooperation received from your staff during the evaluation.



David P. Wheeler
Assistant Inspector General
(Audits and Evaluations)
WT 2C-K

JAJ:FAJ
cc: See page 5

Tina R. Shelton
Page 5
September 26, 2019

Attachment

cc (Attachment):

TVA Board of Directors
Clifford L. Beach, Jr., WT 7B-K
Susan E. Collins, LP 6A-C
Robertson D. Dickens, WT 9C-K
Megan T. Flynn, LP 3A-C
Jeffrey J. Lyash, WT 7B-K
Justin C. Maierhofer, WT 2C-K
Jill M. Matthews, WT 2C-K
Wilson Taylor III, WT 2D-K
Sherry A. Quirk, WT 7C-K
OIG File No. 2019-15626



Tennessee Valley Authority, 1101 Market Street, Chattanooga, Tennessee 37402

September 25, 2019

David P. Wheeler
Office of Inspector General
400 West Summit Hill Drive
Knoxville, Tennessee 37902

Dear Mr. Wheeler:

RESPONSE TO REQUEST FOR COMMENTS – DRAFT AUDIT 2019-15626 – INDIVIDUAL PERFORMANCE MULTIPLIER

Our response to your August 26, 2019, request for comments regarding the subject draft report is attached. In addition, this response is reflective of a Vice President title change referenced in the report from Compensation & Benefits to Total Rewards.

TVA is committed to a culture of continuous improvement and as such, appreciates the Office of Inspector General helping us to identify opportunities to enhance the way we encourage a pay-for-performance culture.

We would like to thank John A. Jacosalem, E. David Willis, and you for the professionalism and cooperation in conducting this audit. If you have any questions, please contact me at (423) 751-8491.

Sincerely,

A handwritten signature in cursive script that reads 'Tina Shelton'.

Tina Shelton
Vice President, Total Rewards
Human Resources & Communications
LP 6C-C

Attachment

cc (Attachment):

Clifford L. Beach Jr., WT 7B-K
Susan E. Collins, LP 6A-C
Robertson D. Dickens, WT 9C-K
Megan T. Flynn, LP 3A-C
Stephen H. Gaby, WT 8D-K
John A. Jacosalem, SP 1A-C
Sherry A. Quirk, WT 7C-K
E. David Willis, WT 2C-K
OIG File No. 2019-15626

ATTACHMENT
RESPONSE TO REQUEST FOR COMMENTS
DRAFT AUDIT 2019-15626
INDIVIDUAL PERFORMANCE MULTIPLIER

OIG RECOMMENDATION	TVA PLANNED ACTIONS	TVA COMMENTS
To facilitate supervisors administration of the IPM process, we recommend the Vice President (VP), Total Rewards (TR) consider revising the IPM process to use employees' actual calculated performance ratings, as opposed to rounded ratings.	Total Rewards will evaluate the benefit of process changes and as appropriate, align with leading practice.	Total Rewards will continue to provide appropriate oversight for reinforcing guidelines and discretionary considerations.