

PAYING YOUR PEOPLE: IMPORTANT COMPENSATION CONSIDERATIONS

KEY TAKEAWAYS:

- Assess the value of what the people involved in a project are delivering.
- Cash is good, but don't overlook other forms of compensation that can also make sense.
- Revisit compensation methods and be flexible as your company evolves.

Everyone likes to get paid, and paid fairly, for the work they do. As a business owner, your success will likely depend in large part on how motivated the people around you are—and you don't need us to tell you that compensation goes a long way toward how driven they are to help the business grow and thrive.

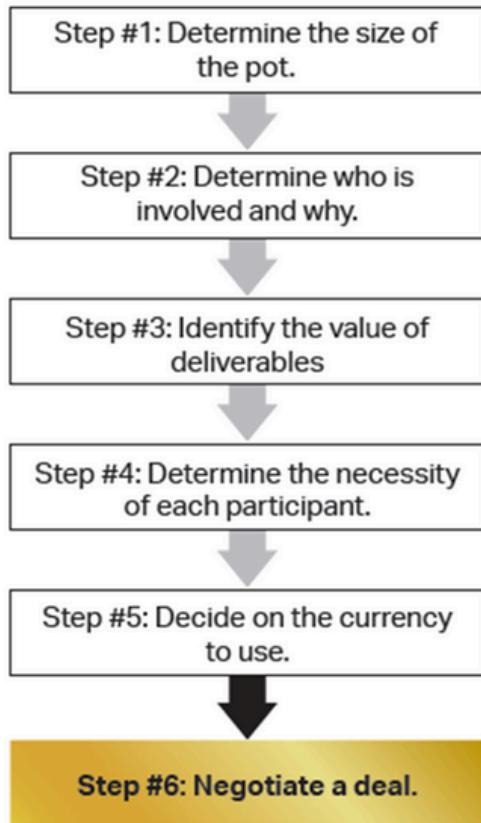
But while you've certainly thought through compensation issues in the past, and will continue to do so going forward, it's possible that you haven't been making the optimal compensation decisions. With that in mind, it's time to examine what we're seeing other top entrepreneurs think about and implement when it comes to paying their people.

A SIX-STEP COMPENSATION PROCESS

Extremely successful business owners are often very good about paying everyone they deem to be important. This is not necessarily because they are “nice” or “fair” (even though they might be both). Rather, they understand that it makes good business sense to properly motivate the people who are vital to helping them achieve their goals and objectives. Of course, money is often not the only driver that's involved in motivating people—but it's very often a big one.

The ability to effectively determine the right compensation levels for the people involved in an enterprise is a top skill set that successful entrepreneurs (or their inner circle executives) tend to master. They employ various ways to value contributions and derive payment programs that work for all involved. The process we see many of them use is highlighted below (see Exhibit 1).

EXHIBIT 1
Setting Compensation



STEP #1: DETERMINE THE SIZE OF THE POT.

In order to pay a worker in a project or business venture, you need to know how much money it's likely to generate. Different initiatives will produce different financial returns, of course. Nevertheless, you will need to do some estimating as to what the results are going to be, which means making formal projections or taking some well-informed guesses.

STEP #2: DETERMINE WHO IS INVOLVED AND WHY.

Specify who is involved in the project. These days, your roster could include employees, contract workers, strategic partners and others. For each of these participants, clearly determine what they bring to the table. In effect, you are asking, "What are the deliverables each participant is responsible for delivering?"

STEP #3: IDENTIFY THE VALUE OF THE DELIVERABLES.

Determine how important each deliverable is to the success of the project or initiative. At the same time, try to calculate the likelihood and value of the synergies that may be generated. Also determine the degree of redundancy in the implementation of the venture. This regularly requires you to address short-, medium-, and long-term consequences.

STEP #4: DETERMINE THE NECESSITY OF EACH PARTICIPANT.

Every single person is fungible, even though they (and perhaps you) don't think so. And yet, as the saying goes, the cemetery is filled with people who thought the world couldn't get along without them. Ultimately, you need to ascertain the extent to which a participant is mission-critical to the venture. As a corollary, you need to be prepared for that participant to no longer work for you.

STEP #5: DECIDE ON THE CURRENCY TO USE.

There are many different ways to compensate people. Cash is good. However, you're likely to have other options to go along with it. Bartering services can be effective. Providing introductions to others who can help the person become more successful can be a very potent form of currency. High-value, thought-leadership content can be a way to compensate certain participants. In our experience, many top business owners employ a variety of payment methodologies.

STEP #6: NEGOTIATE A DEAL.

You will need to develop a working arrangement with the participants that includes how you'll pay them. The more effectively you negotiate, the more fungible the participants are. The greater your leverage (which ties in to your choice of currency), the lower your costs.

YOU WIN, THEY WIN

Paying people a salary (or a fee) is usually the most cost-effective course of action. Generally speaking, that approach will prompt people to work reasonably hard to earn their money. But another powerful way to motivate many people to "give it their all" is to compensate them based on the success of the company and/or the specific endeavor they're involved in.

This approach is all about being paid based on the success of the enterprise rather than on specific activities done. For entrepreneurs, it's a way to share the rewards as well as the risks.

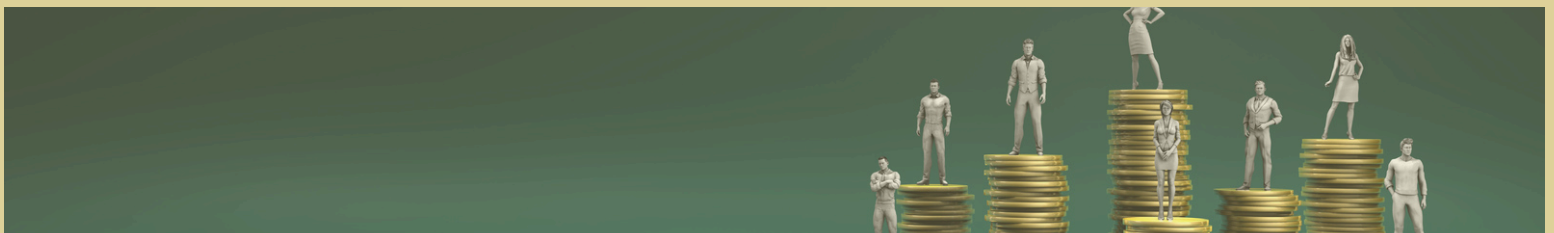
This does not mean giving everyone involved a piece of the action. Instead, you set criteria where basing compensation on achievements will prove most beneficial to you and to the other person/people. Some situations where we see this approach often used include:

- People who are essential to the effective running of the company
- Providers who would otherwise be too expensive to engage
- People who have strategic relationships that you would otherwise be unable to access
- People who are willing to participate in the potential financial upside of an endeavor

This approach to compensating critical, high-potential relationships is used extensively yet carefully by top entrepreneurs. Some of them refer to it as "long-term greedy." It's a way to get substantially more without paying exorbitant sums at the start. Moreover, if things don't work out as projected, the downside can be mitigated.

COMPENSATION CRITERIA TO CONSIDER

In the business world, it's a good bet that paying people well will motivate them. But as noted, money isn't the only form of currency. When thinking about how to pay those individuals working with you, it's essential to know everyone's roles and responsibilities. In setting the compensation of the participants, the following guidelines will likely prove helpful.



STAY FLEXIBLE

As projects and business ventures progress, they have a tendency to evolve. Likewise, the importance of various participants may change along the way. We find that top business owners are generally very efficient at adapting and restructuring the compensation model for any venture. This requires closely monitoring the changing nature of the deliverables and modifying compensation appropriately for participants.

Keep in mind that compensation models are initiative dependent. As the character of an initiative changes, you might need to rework the amount and way you're paying the participants. You must always be prepared to make changes when they are warranted.

REMEMBER THAT MOST PEOPLE THINK THEY ARE MORE IMPORTANT THAN THEY ARE

When working with talented and motivated individuals, you're likely working with egos—some larger than others. While top entrepreneurs certainly want to work with the best, they know to distance themselves from the self-promoting hype of many of these experts.

You need to know what you're paying for. More importantly, know what you want to pay for. To avoid overpaying, you must not unthinkingly buy into the pictures the participants paint of themselves.

PREPARE BACKUP CONTINGENCIES

Sometimes compensation negotiations become intractable—for example, you're able to pay "X" and your prospective participant wants "X + Y." This can be much less of a problem for you if you have alternatives readily available. Highly successful business owners often make conscious efforts to not be dependent on any individual person. This makes them better positioned in any negotiation.

Remember: Anyone can be replaced. Your objective is to be prepared as much as possible to bring in a pinch hitter if a participant becomes too demanding. The more comfortable you are with your backup contingencies, the more you can potentially profit from a business venture.

CONCLUSION

Now could be an excellent time to reexamine your current compensation arrangements with various employees and others you enlist to help you pursue your success. It's possible that a review will uncover ways to make both the amount and the terms of your payment agreements stronger and more effective—for you and the people you count on to deliver great work.



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VFO Inner Circle Special Report
By John J. Bowen Jr.

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