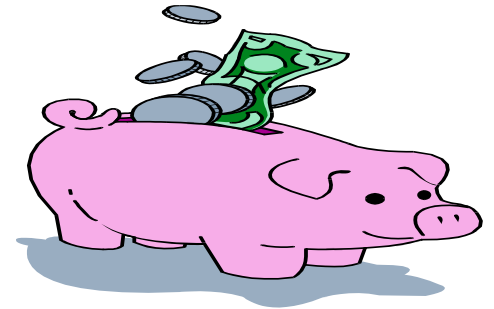


Performance Based Pay.



## Session Objective.

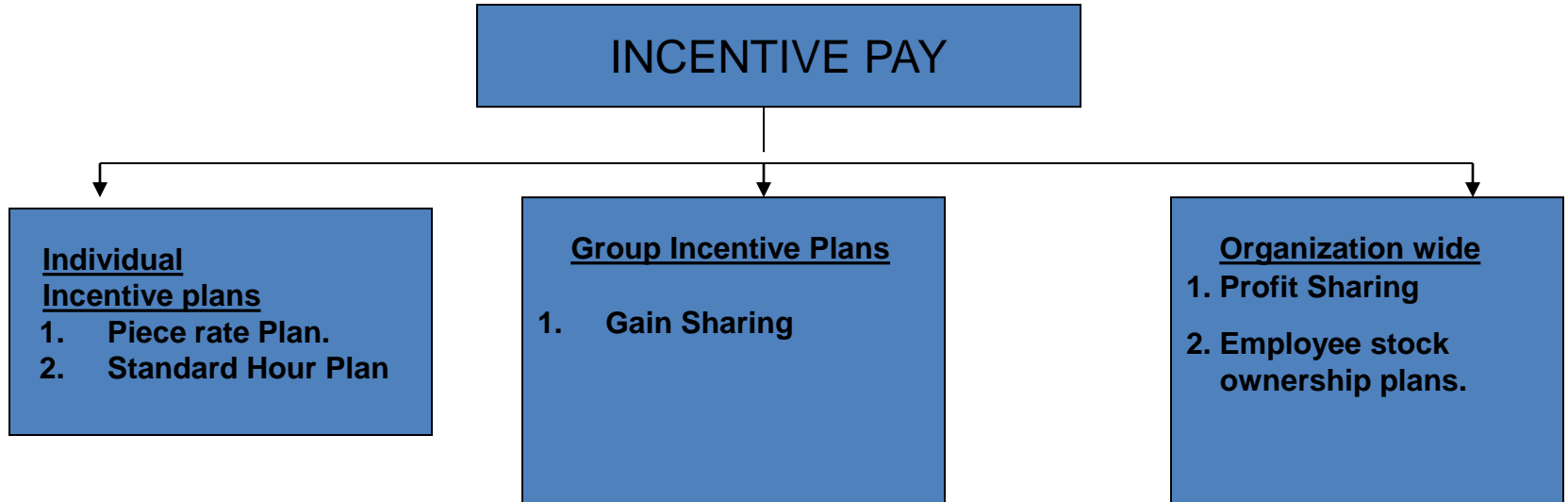
- The student will be understand the assumptions underlying performance based pay.
- The student will be able to compare Performance based pay and traditional pay.
- The student will be able to understand the different plans used for rewarding performance at individual, group.
- The students will be able to outline the steps in developing effective incentive plans.

## Motivation and Pay.

- F.W. Taylor in the late 1800 as a supervisory employee at Midvale steel company scouted for financial Incentives paid to workers whose production exceeds some predetermined standard.
- Fredrick Hertzberg said the best way to avoid dissatisfaction by linking better pay and working condition which he mentioned as (hygienes).
- Edward Deci highlighted the benefits of pay on individual motivation yet insisted too many may backfire.
- In Victor Vroom's theory  $\text{Motivation} = E \times I \times V$  The emphasis was given to the relationship between performance and rewards along with the value of the reward.
- Psychologist BF skinner's finding provide the foundation for much of what we know behavior modification.

Traditional Pay	Performance based Pay
<p>1. Employees receive compensation based on a fixed hourly pay rate linked to factors such as seniority, length of service or past performance.</p>	<p>1. Performance based pay rewards individuals, teams of employees or the company overall for performance.</p>

# Incentive pay classified



## Individual Incentive plans

- ❖ Individual Incentive plans reward employees for meeting work related performance standards.

# Individual Incentive plans

		Method of Rate Determination	
		<i>Unit of Production</i>	<i>Time Period</i>
Relation ship between Producti on level and pay.	<i>Constant</i>	<b>Straight Piecework plan</b>	<b>Standard Hour plan. Bedeaux Plans</b>
	<i>Varies</i>	<b>Taylor and Marrick Differential Piece rate System.</b>	<b>Halsey 50-50 method. Rowan Plan. Gantt Plan.</b>

1	2
3	4

# Individual Incentive Plans

Advantages	Limitations
<ol style="list-style-type: none"><li data-bbox="19 240 946 535">1. Substantial contribution to raise productivity, to lower production costs and to increase earning of workers.</li><li data-bbox="19 567 946 786">2. Less direct supervision is required to maintain reasonable levels of output.</li></ol>	<ol style="list-style-type: none"><li data-bbox="985 240 1912 535">1. Conflict may emerge between employees seeking to maximize output and managers concerned about deteriorating quality levels.</li><li data-bbox="985 567 1912 862">2. Attempts to introduce new technology may be resisted by employees concerned about the impact on production standards.</li></ol>



## Cont...

- In most cases systems of payment by results, if accompanied by improved organizational and work measurement, enable labor cost to be estimated more accurately. This helps in costing and Budgetary Control.
  1. Increased complaints that equipments are poorly maintained hindering employee effort to earn large incentives.
  2. Increased turnover among new employees discouraged by the unwillingness of experienced workers to cooperate in on the job training.

## Group Incentive Plans

- ❖ Group Incentive plans reward employees for their collective performance rather than for each employees individual Performance.

# Group Incentive Plans

- Organizations use two major types of Group Incentive Plans.
  1. Team based or small group incentive plans.
  2. Gain Sharing Plans.

## Team Incentive pay a paradox

- ❖ Size and composition of Teams.
- ❖ Level Problem.
- ❖ Complexity.
- ❖ Control.
- ❖ Communication.

## Gain Sharing Plans

- ❖ Gain sharing describes group incentive systems that provide participating employees with an incentive payment based on improved company performance.

## Types of Gain sharing Plans

- ❖ The Scanlon Gain sharing Plan
- ❖ The Rucker Gain sharing Plan.
- ❖ Improshare.

Features	Scanlon Plan	Rucker Plan	Improshare
<p><b>Goal</b></p> <p><b>Employee Involvement</b></p> <p><b>Type of employee Involvement.</b></p> <p><b>Basis for Saving.</b></p> <p><b>Bonus Payout Frequency</b></p>	<p><b>Increasing Productivity</b></p> <p><b>Required</b></p> <p><b>Screening and Production committee</b></p> <p><b>Labor Cost</b></p> <p><b>Monthly</b></p>	<p><b>Increasing productivity</b></p> <p><b>Required</b></p> <p><b>Screening and Production Committee</b></p> <p><b>Labor cost Raw Material and Service cost</b></p> <p><b>Monthly</b></p>	<p><b>Increasing Productivity</b></p> <p><b>Not Required</b></p> <p><b>N.A</b></p> <p><b>Rate of completion Of work.</b></p> <p><b>Monthly</b></p>

## Designing a Gain sharing Plan

- ❖ Strength of reinforcement.
- ❖ Productivity Standards.
- ❖ Sharing the gains.
- ❖ Scope of the formula.
- ❖ Perceived fairness of the formula.
- ❖ Ease of administration.
- ❖ Production Variability.



# Organization wide Incentives

- Profit Sharing.
- Employee stock option plans. (ESOP)

## Profit sharing Plans

- ❖ A organization wide pay for performance plan that uses a formula to allocate a portion of declared profits to employees.

## Profit sharing plans classified

1. Current profit sharing. (Under these plan cash awards are being given to employees typically on a quarterly or annual basis)
2. Deferred Profit Sharing. ( Under this plan cash awards are placed in trust (deferred share trust) accounts for employees)

# Calculating Profit Sharing

- ❖ A fixed percentage of profits formula.
- ❖ A graduated percentage of profits formula.
- ❖ Profitability thresholds formula.

# Distribution of profits

- ❖ Equal payments to all employees.
- ❖ Proportional payment.
  1. based on employees annual salary.
  2. Based on an employees contribution to profits.

## Pros and Cons

- ❖ Profit sharing plans enable employees to share companies fortunes and in turn enhance employee commitment to organization.
- ❖ Companies use profit sharing program gain greater financial flexibility.
- ❖ Undermine the economic security of employees.
- ❖ Profit sharing plans may fail to motivate employee because they do not see a direct link between their efforts and corporate profits.

## Employee stock option Plans

- These are company wide plans in which right or privilege granted by a corporation to purchase the corporation's stock at a specified price during a specified period.

# ‘ ESOP ’ Typology.

TYPES	Description
<b>Employee Stock Purchase Plan.</b>	Gives employees the chance to buy stock, usually through payroll deductions.
<b>Restricted Stock Plan.</b>	Involves an outright grant of stocks, usually at nominal or no cost. The advantage lies in with the tax deferral that results from the vesting restrictions.
Phantom Stock	It provides employees with a payout usually in cash, based on the increase in the companies stock value.



<b>Advantages</b>	<b>Limitations</b>
<ul style="list-style-type: none"><li data-bbox="85 281 938 423">■ Funded by the market not by the organization.</li><li data-bbox="85 452 948 594">■ Enables in wealth creation for employee.</li><li data-bbox="85 622 933 840">■ Amounts can be sufficiently high to ensure adequate motivation.</li></ul>	<ol style="list-style-type: none"><li data-bbox="1018 281 1765 572">1. The pay out is unpredictable because high dependency on market conditions.</li><li data-bbox="1018 600 1663 749">2. Amount may be insignificantly low.</li></ol>

## Cont...

- Creates a sense of employee ownership in the business.
  - Inculcates a performance driven culture.
1. Lock in periods and other conditions may dilute perceived value.
  2. Employees are subject to the vagaries of the market.