PERFORMANCE MANAGEMENT SYSTEMS

CHAPTER VI

PAY FOR PERFORMANCE

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- **Objectives:**

  1. Explain different types of non-traditional pay systems.

  2. Understand concept of gain sharing.

  3. Find ways and means of relating pay with competencies & performance

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- **Structure:**

1. Non-traditional pay systems.
2. Gain sharing
3. Organisational reward norms
4. What pay can do
5. Relating pay to competencies
6. Link between Business results & performance

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6.1 Non-traditional compensation systems:

- Traditionally pay is a function of position or status in company, & not performance or contribution to company goals. Market demand & supply play important role.
- **Characteristics of traditional compensation system:**

  1.No relation between performance & pay. Increases come from promotion & not higher performance in present job.

  2. Everyone gets almost same increase annually.

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6.1 Non-traditional compensation systems:

- Non traditional compensation systems intend to provide employee a financial stake in improving company’s maximum performance.
- **Types of Non-traditional pay systems:**

  1. Gain sharing- Bonus is tied to unit wide performance measured by predetermined formula.

  2. Small group incentives: bonus is based on performance of a small group & varies from group to group.

  3. Individual incentives: Started in manufacturing and spread to managerial, professional and service sectors

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6.1 Non-traditional compensation systems:

4. Lump sum payment/ bonus: Onetime performance, not added to basic salary. Some pay it across the board annually as percentage of pay.

5. **Pay for knowledge:** Pay tied to knowledge and skill, rather than to position or job actually performed. Two basic norms are: Increase knowledge-based systems & Multi-skilled-based systems. These systems allow companies to reduce job classifications and encourage a more flexible workforce. Multi-skilled-based systems are a newer, less common and more revolutionary form of pay-for-knowledge.

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6.1 Non-traditional compensation systems:

6. Profit-sharing plans: are based on company-wide performance & are paid in cash or added to retirement benefits.

- In all these plans companies try to slow growth of base pay and make portion of compensation variable and tied to company, group, individual performance. Over a period, base pay will reduce and will be smaller percentage of total pay.

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6.2 Gain-sharing:

- It involves groups of employees in improving productivity through better use of resources. Company shares part of productivity gains with employees in cash bonus. Gain sharing includes a formula for gains and sharing with employees

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6.2 Gain-sharing

- **Gain sharing Vs individual incentives.** Individual incentives become costly to monitor and calculate, as base pay also has to be in line with changes in methods & technology. Moreover there is no incentive for employee to cooperate, work as a tem, help each other, and place company/ group interest over their own. To overcome these problems, gain sharing is an attractive alternative.

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6.2 Gain-sharing

- **Gain sharing Vs Profit sharing or lump sum bonuses:** Both rely upon macro-level measurements and are based on group performance. However profit sharing & lump sum bonuses differ in some ways from gain sharing. They payout once or twice a year, while gain-sharing pays every month. Profit sharing is tied to company’s profits and not to employee performance. Thus no profit means no bonus. Employees have no control over the profits.

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6.2 Gain-sharing

- **Advantages of Gain-sharing over other pay for performance options:**

  1. It is based on group performance.
  2. Encourages teamwork & cooperation.
  3. It is based on macro-measures & easy to administer.
  4. It is based on factors controlled by group.
  5. Does not encourage destructive competition.
  6. Promotes employee-company partnership for improvement.

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6.2 Gain-sharing

- **Criteria for Traditional Gain-sharing formula:**

  1. Fair to the company.
  2. Fair to employees.
  3. Understandable to employees.
  4. Easy to administer.
  5. Flexibility (company goals, objectives and priorities can change)
  6. Useful in isolating problem areas.

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6.2 Gain-sharing

- **Performance appraisals are used for:**

  1. Salary administration.
  2. Performance feedback
  3. Identifying strengths & weaknesses of employees.
  4. Documenting personnel decisions.
  5. Recognition for personal performance.

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6.2 Gain-sharing

- **Performance appraisals are used for (Cont)**

  6 Identifying poor performance.

  7. Assisting in goal identification.

  8. Promotion decisions.

  9. Retention or termination of employees.

  10, evaluating goal achievements

6.3 Organisational Reward norms:

- Employees exchange their time and talent for organizational reward.
- **Four ways to view employee-employer relation:**

1. Company attempts to pay least amount. Employee seeks maximum reward irrespective of company's financial position & leaves for better economic offer.

2. Equity: Rewards should be proportionate to contribution. Compensation procedures include some form of pay-for-performance, competency based or skill-based pay.

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6.3 Organisational Reward norms:

- **Four ways to view employee-employer relation: (cont)**
- 3. Equality: This norm calls for equal reward irrespective of performance or seniority etc.
- 4. Need: This norm requires payment as per employees need. This happens in family business.
- To be effective, reward system at a minimum must be based on clear and consensual norms

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6.3 Organisational Reward norms:

- **Shortcomings of contemporary pay systems are**:

  1. Inability to attract high performers

  2. Perception that people with particular competencies add more value.

  3. With changes occurring fast, job based pay systems are becoming meaningless.

  4. Employees future value is worth significantly more than present one.

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6.3 Organisational Reward norms:

- **Shortcomings of contemporary pay systems are**: (cont)

  5. Need to compensate equitably knowledge workers.

  6. Perception that highly structured compensation systems promotes bureaucracy, reducing flexibility and is incompatible with flat organizations & empowered employees
- Worst frustration with job-based pay systems is that they treat employees as fungible commodities instead of individuals valued for their differences, diversity, initiative, creativity, flexibility and ability to change.

6.4 What pay can do:

- Money has significant impact:

  1. Hiring people-pay attracts good job applicants.

  2. Retaining people, make them reluctant to leave.

  3. Motivating people- an expression of recognition

  4. Avoiding dissatisfaction

When should pay be discussed- If done with appraisal, then appraisals are taken seriously. But then career development, personal growth etc. get less attention.

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6.5 Relating pay to competencies

- People are mostly paid according to their job, job size and external pay market comparisons. Fixing rate for the job ignores performance or capability. Promotion to higher pay job is the only way to pay more. This structuralist view is now challenged. Delayering, team working, project working, flexibility, organizing around business processes, lateral rather than vertical career development- these are all areas of change for most organizations in today’s environment.

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6.5 Relating pay to competencies

- It is reasonable that pay should reflect the skills and competencies which individuals bring and use. It is recognised that pay of individual needs to be related to a number of factors including his role, the skills and competencies, achievements and the market. The real issue is how to achieve the best balance between these factors to meet business requirements and circumstances. If this balance can be achieved then relating pay to competencies can have a powerful and positive impact, by rewarding and encouraging the behavior needed by organization to achieve success in realistic and practical context.

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6.5 Relating pay to competencies

- Overall pay levels will be affected by external markets and organisation’s required relationship with it, given its business performance and its plans and strategies.
- There are two ways in which pay may be related to competencies. First, by building competencies into performance management process and then relating pay movement through a pay range to access performance. Second way is use of role profiling or job family approach. Individuals are evaluated against different criteria. Difference is mainly about presentation. First one is presented as grade structure and the second as a pattern of pay zones.

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6.6 Link between business results and performance:

- Organisations talk a lot but are reluctant to spend time, money and energy on programs which will help people to perform and contribute to their optimum. Failure to see link between people and business results is the cause of this. Whether the issue is one of poor capital equipment, inefficient distribution channels, ineffective marketing or bad resource allocation, it always comes back to people.

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6.6 Link between business results and performance:

- Successful organizations of future will be those that secure a true competitive advantage and understand this link. This requires different type if clarity about external strategic objectives, internal critical success factors, people factors and integrated solution. HR programs must be integrated with orgnisation’s success factors and there must be a clear link with business benefits.

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6.6 Link between business results and performance:

- Today in every company you hear complaints that there are too many initiatives on the go at a time. The problems are- lack of clarity about ho w initiatives relate to strategy and business results and to each other; poor design, lack of integration. All these stem from failure to understand link between business and people.

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End of

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