THE GLOBE AND MAIL

March 23, 2011

Pay-for-performance can be a minefield

By RASHA MOURTADA
Globe and Mail Update

When done right, these schemes are a win-win for a company and its employees. Done wrong, look out

It took Peggy Aulenback three tries to get her pay-for-performance structure just right.

The founder and president of Langley, B.C.-based Paramount Refund Management, which processes claims for clients of the federal Scientific Research and Experimental Development program, tried two designs before introducing her current one a year and a half ago.

"I had in the past put the targets in the wrong place, so to speak, and got the wrong results," says Ms. Aulenback of the system. "I had systems where I let employees participate in part of the profits, and some years they got no bonus because the company didn't hit its target for whatever reasons," she says. "And then one year I had an employee who was able to go back to school because her bonus was so big."

Pay-for-performance can mean anything from pure commission-based compensation, typical in sales environments, to annual bonuses, to salary increases based on merit (rather than cost of living). Used correctly, the structures can align staff with company objectives while providing a financial reward - creating a win-win for both employer and employee, says Andreas Hesse, a consultant with Clear HR Consulting in Vancouver.

If you're not tying raises or bonuses to performance you're "simply giving your money away," Mr. Hesse says.

But employers should tread carefully, says Lynn Brown, managing director of Toronto-based human resources firm Brown Consulting Group.

"What I see often is people doing pay-for-performance based on their own discretion," says Ms. Brown. "They'll say, "I think this person did a really good job and I'm going to give them an increase or bonus.'"

Such a lack of clarity can confuse and upset employees, particularly if the results are inconsistent. "Pay-for-performance needs to be spelled out or employees can become demotivated and disgruntled," she says.

The first step in setting up a good plan is identifying measurable goals. And that's where many employers go wrong.

"Business owners might be able to say, 'This is our revenue target for the year,' but they aren't able to tell their account manager how that translates into his goals," says Mr. Hesse.

Whether the goals are related to revenue, number of clients or cost-cutting, they must be realistic and measurable.

"If it's too pie-in-the-sky then [employees] likely are going to disengage or not try as hard - perhaps even sabotage," says Mr. Hesse. "Sabotage may take the form of talking to colleagues and saying there's no point in trying," he adds, which can quickly create a toxic workplace.

Setting goals for staff who do administrative tasks can be challenging, says Mr. Hesse. He suggests looking at process improvement and cost-cutting goals.

In the case of Ms. Aulenback's company, which sought advice from Clear HR Consulting in creating its system, goals are based on the number of claims filed by individuals and the entire team, a system Mr. Hesse endorses. "It helps the motivation of the employee if they feel they have ownership of achieving goals on a day-to-day basis," he says.

To come up with targets, Ms. Aulenback looked at three previous years of sales. "It's based on very real, attainable numbers, which I think is really important," she says.

Ms. Brown says it's important not only to set goals but to revisit them periodically through a performance appraisal system. "A lot of small businesses do not have that," she says.

Having regular check-ins ensures that there will be no surprises if an employee does not meet objectives, adds Mr. Hesse. "If you're seeing how an employee is doing against the objectives, then you can support them as necessary," he says. "The employee should know whether or not they've met their goal."

Some employers may not have a large sum of money to pay out in bonuses, says Ms. Brown. She encourages small business owners to consider all their options before committing to a pay-for-performance structure. "They should look at how much they have and play with what type of program they can put in place," she suggests. A three per cent salary increase may not seem significant spread over a year, but a bonus paid out quarterly in the same total amount may seem heftier to employees, for instance.

Not to be overlooked is the importance of simplicity. Not only must the goals be easy to understand, but the entire system needs to be easy for employees to participate in and managers to implement, says Ms. Brown.

Above all, the system should ensure fairness and consistencies.

"You can pretty much guarantee that the staff will discuss it amongst themselves," says Mr. Hesse. If employees catch wind of any inconsistencies in payment structures, they will quickly lose interest in participating.

Ms. Aulenback has found a side benefit of her pay-for-performance structure: "I can be a bit more hands off," she says. "The goals give us a bit of a road map, so everyone knows what they should be doing and is planning ahead. I'm not managing their work flow, they are."

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