

**BONUS PLAN EFFECTIVENESS –
chasing the dream**



The role of bonus within Reward Strategy

SUMMARY

Organisations seeking the Holy Grail of reward management have come to the conclusion that there is no such thing – but they do believe that an effective and co-ordinated strategy, covering base pay, benefits, bonus and offering employees a good range of career opportunities and interesting work should meet the company requirements.

However, new results from a survey by Innecto Reward Consulting reveal the disturbing news that 63% of HR managers; from a range of company sizes and backgrounds, believe their schemes are ineffective in motivating employees. Recent research from CIPD (Reward Management Annual survey 2006) shows that overall, across the private sector, approx 84% of employers have one or more bonus schemes in operation, which represents a huge cash investment in bonus payments. CIPD research finds that companies are focusing on bonus arrangements which link between pay and performance, increase productivity and improve financial results: by contrast, Innecto's findings suggest that, for many organisations, their schemes are currently ineffective in delivering these objectives. **Would the organisation invest funds in other schemes which have so little guarantee of return on investment?**

FINDINGS

What conclusions can be drawn from the research?

The vast majority of HR directors do not believe their company bonus scheme is effective at motivating employees or improving performance.

Research carried out by employee reward experts Innecto Reward Consulting questioned 183 HR directors and managers about their use of company bonus schemes. Despite bonuses coming top of the list of elements making a positive impact on the motivation of employees; over and above appraisal, career development plans and line management, 63% said they could not draw a direct conclusion that their bonus scheme was effective in improving workplace performance.

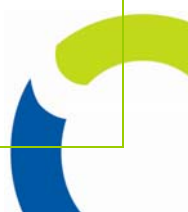
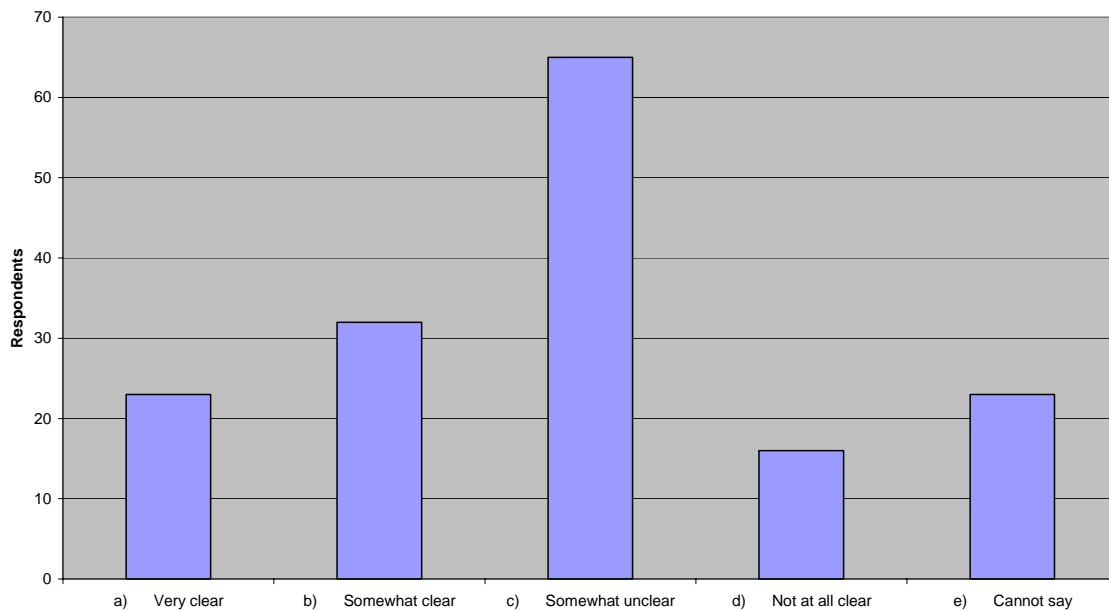
Another 70% of respondents said their organisation had awarded staff bonuses in the past that weren't justified, either because of pressure from the board or employees, or to appear successful to the outside world.

Most HR directors do not measure, evaluate or test their employee bonuses. When questioned only 18% said they had carried out studies to measure the effectiveness of their bonus scheme, with 7% doing so in-house and 11% using an outside consultancy. Eight-two per cent had never evaluated their bonus schemes.

Within the survey results, it is clear that HR professionals feel that bonus schemes and decisions over them are out of their hands, with only 3% of HR Managers believing that HR have control of whether bonuses are paid. Overwhelmingly, in organisations in our survey, the Remuneration Committee (44%) makes the decision, but equally, MDs, the Board and Financial Directors have a major part to play in the process. However, as a result, HR professionals have little faith that the investment in bonus schemes is driving changes in behaviours and business performance.

In fact, when specifically considering the link between employees' own performance and their bonus payment, 65.4% of HR managers believe that this link is unclear, or they cannot evaluate its importance.

Do your employees make a clear link between their performance and bonus?



Deborah Rees, senior consultant at Innecto, said, "It amazes me that UK plc is throwing away billions of pounds each year on bonus schemes without certain knowledge that they are a wise investment. Bonuses can be an excellent way of motivating staff but only when clearly linked to performance and communicated properly."

"HR directors have an opportunity to take the lead in investigating the role and purpose of their bonus schemes. Such poor investments would not be accepted in other business areas and so they shouldn't be accepted in the area of employee reward"

From the CIPD survey, it is clear that HR professionals are planning to amend bonus schemes this year, with over 65% of companies intending to change, disband, or amend their scheme, but without objective analysis of the impact of the bonus scheme, this could be throwing good money after bad.

It is a golden opportunity for HR Managers and Directors to take a strategic perspective on the business effectiveness of a key part of the Reward package, by having the determination to challenge senior management and Board colleagues about the impact of the businesses investment in bonus schemes.

RECOMMENDATIONS

Phase 1 – Analysis

- Assess how much money is actually invested in bonus schemes as a % of total cash (base salary + bonus), and as a £ figure
- Make comparisons with the general market position for the industry – where is your organisation placed in positioning around base pay, bonus and total cash. Is the business paying too much, too little or is market competitive? Does it vary by role – management, sales or administrative employees?
- What are the metrics that drive the bonus plans currently? Are they directly linked to what your organisation needs people to contribute in order to be successful?
- How do employees view the schemes in place – do they understand what they have to do to be paid bonus, and do they see the connection between their own performance and that of the organisation?

Phase 2 – Design

- Work with the business to assess the key metrics that drive business performance.
- Assess the culture and requirements of the organisation. Will a 'one size fits all' scheme work? Should the organisation segment its bonus plans according to function requirements – for example sales or senior management?
- Is the organisation keen to incentivize or to reward employees?
- Is there a team-based or an individual-based culture?
- What are the Key Performance Indicators (KPIs) so that the organisation can evaluate whether the scheme has succeeded?

Phase 3 – Implementation

- Involve some end-users in the design and communication of the scheme, so that they can act as ambassadors for its operation.
- Remember an average quality scheme design which is well communicated will be far more effective than the most elegant design, poorly explained.
- Remember employees should be able to understand what they actually do at work affects their bonus payout.
- Measure whether it has achieved the organisation's KPIs

CASE STUDY; BONUS AS PERFORMANCE MANAGEMENT

WestawayGillis is a small consulting firm, providing consulting services to the pharmaceutical industry. Like many organisations that have grown quickly, their informal system of managing performance had gradually started to become ineffective as the business has grown.

Over two years, the company has migrated from an informal performance management system, based on targets based on overall company results, to breaking targets down for individuals. This has meant that each employee has a specific target in terms of profitable project delivery and developing business to achieve which assesses their overall contribution to business success. Karen Westaway, joint CEO explains how the performance management system has benefited the company....

I learned very early on in my management career that “you get what you measure” is a universal truth! However, this is very easy to forget when you are running a company that is growing very quickly as WestawayGillis has done. We were falling behind on our sales targets and getting embroiled in all kinds of issues that all growing companies face.

In order to refocus every member of the company on essential elements that are critical to the success of the business, we have put in place a performance management system that directs individuals to measure the key aspects that they contribute to both sales and quality delivery – the life-blood of any service company.

Since doing this, we are back on track with our sales targets as a company, and although we do not have concrete data around quality delivery at this point, all the indicators suggest that our clients are more than satisfied.

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Innecto Reward Consulting is a specialist consultancy in the world of pay, job evaluation, bonus scheme design and performance management.

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