The Realities of Reward

A recent study covering sales management methods and systems produced a number of intriguing results, not least of which was the data concerning the effectiveness of the incentive schemes operated by the companies in the sample studied. The researchers found no correlation at all between the proportion of sales peoples' income paid in incentives and sales productivity. Odd? True, but the plot thickens.

There was one notable correlation that did involve the proportion paid in incentives, and that was with staff turnover. Where the proportion was high or low, so was staff turnover, but the latter parameter peaked at 40% of sales income paid in incentives. If that were such an unusual figure, the result would be less surprising, but the fact is that most sales incentive programmes operate closer to that proportion than they do to the extremes.

Which raises some interesting questions. Why is so much time and effort spent on the design, introduction and administration of incentive and other reward schemes? Why are so many companies investing in such schemes, apparently with little to show in return, and much to concern them? What is it that causes senior managers, who presumably are good and competent fellows, to spend so much of their company's money to buy a problem for their businesses?

Again, if the results were not confirmed by a sense check, the questions would be less in need of answers. But the sense check works. If bonuses, profit sharing and other reward systems work so well, how come their beneficiaries manage to find the time to work on their golf handicaps, or enjoy their business lunches or the other various quasi business activities that are so popular?

The key question, that over rides all the others, is a simple one - do, in fact, reward systems actually change behaviour, or results? The answer, mostly, seems to be, or at least, not as much as their proponents would like to believe.

Now this is not to suggest that all such schemes should be discarded - far from it. There are many examples of good and successful schemes in operation, which give the lie to that argument. What is suggested, however, is that the factors that impact the success of any scheme are manifold and often subtle. If these are not factored in to the design of the scheme, then the return on investment is likely to be less than acceptable.

Moreover, a careful examination of the realities of how rewards and incentives actually work will suggest that the business goals that the good systems are designed to serve may not be the ones that are popularly assigned to them. But first, consider the organisational issues that get in the way of and modify the real pay back from all reward systems, unless they are designed out.

Human aspirations and norms

The issue may be a hotly disputed one, especially in the bars after another unsuccessful attempt to lower the golf handicap, but the fact remains that there is little evidence to support the contention that financial or material rewards, on their own, do much to get individuals or groups to pull out all the stops in the pursuit of business goals.

What is clear is that we all have a set of norms within us, and if our income is wallowing gently below that norm, we will be galvanised into doing something about it. But once we have reached it, the effort will die down again, as other issues become more important. What is also clear is that the other characteristics of the job, which do help people to produce above the norm, are more to do with the way they are managed by their individual bosses, than to do with the company, its policies and reward systems.

Which suggests that those managers who rely heavily on rewards to motivate their people may only be in a position of having to do so, because they have to compensate for some deficiency in their own managing style. Many studies have confirmed that excess upward pressure on material and financial issues by employees nearly always reflects something missing in the more abstract components of their motivational wellbeing.

A summary of the position might be that the corporation, via all its investments in the material and financial contributors to employee motivation, can do no more than get that motivation up to the norm. For starring performances, the contribution all has to come from the individual manager, and, as it all depends on his or her managing style, it's all for free. So any managers who blame the company for the source of their difficulties in motivating their people should, perhaps, go visit the bathroom and look in the mirror to identify the true source of their problems.

Reward systems that conflict with real business priorities.

All organisations send a myriad of signals down the line to their employees, which tell them what is and what is not important in the business – the ‘permissions’. Sadly, some of the signals contain messages the management does not wish to send, and frequently, of which they are not aware. This is bad enough in itself, but where the messages conflict with the ostensible objectives of the reward systems, real trouble may ensue.

The likely outcome is frustration and tension among the employees, recriminations going in all directions when results do not work out the way the management wanted, and, as an end out condition, the ultimate regression - people start to quit the business. Which sounds pretty good as a result of a scheme designed to raise employee motivation. A couple of examples may suffice to illustrate the point.

What is the employee to make of a business where the Managing Director has a daily report placed on his desk at 7.30 every morning, and starts to call people up immediately after 8 a.m.? The report details the business results generated the day before, and the MD's telephone calls are all querying why particular results were off the expected standard.

In practice, the message is very clear. What counts in that company is not getting a telephone call from the boss tomorrow morning, and the employees’ best energies are devoted to that end result. With everyone from middle managers downwards working to eight-hour time scales, it is a little difficult to get people to think about the longer-term implications of their actions. Moreover, since the only way to avoid the telephone ringing the next day is by generating departmental results at the expenses of someone else's, reward systems that demand cross-functional team working tend to get little attention. Which was the point where the company decided to introduce a total quality scheme, and incentivise the employees accordingly. Enough said?

Another example would be the sales operation in North America that was beaten up, by fax and email, from its UK head office, on a regular basis, to get the end of quarter numbers right. If the short term predictions were not looking good, the pressure came on, and the only escape route was to pull forward business from the first month of the succeeding quarter. Which was great for the figures supplied to the shareholders this quarter, but it guaranteed another similar problem by the time of the next quarterly merry go round.

All of this would be serious enough, but a minor aspect of the sales operation tended to get in the way of allowing the business to prosper. The normal selling cycle in that particular industry is about two to three years long. Which meant that while the sales team was rushing around drumming up more and often fictitious business to meet the end of quarter rush, no one was doing much about opening up new accounts.

So the company did the inevitable things. First, they blamed the sales group for being an idle, good-for-nothing bunch. Then they decided to solve the problem by introducing an incentive scheme that majored on new business. After three years, they managed to open one account, (and the local Sales Director did that personally), by which time nearly half the sales force had quit. And there are no prizes for guessing which of the sales people went first.

Meanwhile, the poor old shareholders were still wondering where their next year's dividends were coming from ....

Rewards and self-fulfilling prophesies

One of the difficulties with reward systems is that they are bound, by their very nature, to send the wrong message to employees. The problem stems from the basic observation that people, generally speaking, behave in the way that the ‘system’ educates them to. The most perceptive human of all - the child - works out this particular piece of psychology, from a young and tender age.

Try telling the child that if they repeat a specified piece of behaviour, they will go without their supper, and then relent, and watch their smoke. They will rapidly work out that unfulfilled threats mean they are home free to do pretty much as they please, and that the misbehaviour carries its own rewards. They get the benefit of the original misbehaviour, they get the benefit of being able to manipulate the parent, and they still get supper on top!

If companies insist on over-reliance on reward systems, and keep on talking about them, with all the usual ballyhoo that accompanies them, they should not be surprised if employees get the message very rapidly. If the assumption is made, they will start to behave as if the only reason they come to work is for the money. Their behaviour reinforces the original erroneous assumptions of the managing and the downward spiral is now well on its way to completion.

One short example concerns the Marketing Manager, who was acknowledged to be one of the brightest talents in his business. When the MD heard that he was very frustrated and thinking of leaving, the manager was called in and offered a large increase to stay. When six months later, the same information was relayed to the MD again, he repeated the medicine. (Why anyone would think that a larger dose of the same medicine that had already failed once, would work the second time, is, in itself an abiding mystery).

The real reasons for the Marketing Manager's frustration were all to do with his failure to get one creative idea past the directors, who were all firmly wedded to the established way of doing things. So, like night follows day, the manager left, joined a risky new business venture, threw all his considerable creativity and energies into it, having taken a 30% drop in income to do so, and over the next four years took a tasty slice of the market share of his previous employer's business.

Risk analysis and the normal distribution curve

Observation of real human beings shows that, for the majority, their approach to the question of risk is a sensibly logical one. 'Risk' in this context simply means any available activity where the outcome is uncertain, and there are both benefits and costs to consider. Either consciously or unconsciously, people seem to ask themselves four questions, before deciding to take the risk or not. The key questions are:

- What is the value of success?
- What is the cost of success?
- What is the cost of failure?
- What is the probability of failure?

(There is a fifth, which is about the person's confidence in their information about the answers to the other four, but, for the purposes of this discussion, it can be discounted).

What people do is to look for a reasonable balance between the four sets of criteria. For example, if the first is low and the others are all high, the decision to do nothing is an easy one. But supposing they are all high? The answer depends on the individual, but if the probability of failure and cost of failure are high enough, the answer is still probably masterly inactivity.

The key is to remember that if the balance is out, and if the last two are too high, putting more money into the pot will gain nothing. If this sounds implausible, try the thought of swimming the North Atlantic, solo, in the middle of a winter gale, with no rescue boat. Raising the value of success to millions or even mega millions is unlikely to get our reluctant hero into the water!

Turning to the normal distribution curve, this virtually always shows, in any group of employees, a small proportion of high flyers, an equally small proportion of poor performers and the majority wobbling about somewhere in the middle of the distribution. Any sensible company will base its employment policy on recruiting people in the group above the norm, but short of the stars. A sprinkling of the latter is welcome, but they should not be the subject of the main thrust of the policy.

(In case anyone doubts the validity of this last assertion, there are two snags with seeking only superstars. The first is that they are not there - there simply are not enough of them in the pool. The second is that, even if they can be found, the problems of employing them will be enormous. There is always a distribution of results, and someone has to be at the bottom of the stack. Superstars do not find that position comfortable, so the losers quit, and find another stack, where they can occupy the top slot).

The first conclusion that can be reached, bringing the two concepts together, is that where individual reward systems relate to absolute results, many employees simply will not bother to try. The balance in their analysis of the benefit and risk is too great, in the wrong direction. Unless the rewards are enormous, in which case, they are probably not economically supportable, it is only people in the top quartile, or thereabouts, who will find the four factors identifying the risk to be sensible in balance.

As an illustration, consider the large retail organisation that offered spectacular Far Eastern holidays as a special prize one year. All eight of them. The snag was the 15,000 people who were eligible to compete. Not surprisingly, most did not even go to the starting gate, and of those that did, most gave up after the first few weeks. Equally not surprisingly, the winners still had traces of the sun tan they had acquired from the preceding year! So guess what the company did the following year? The risk of failure in this little test is so small, that the value of success is bound to be even smaller - in this case nothing.

The second conclusion is that reward systems that relate to growth in results will work in exactly the opposite way. That is, it is the lower performers who will find the balance of benefit and risk/cost looking more sensible. This suggests that reward schemes that are intended to appeal to all employees should reward both absolute results and growth in results. But then the arithmetic gets tricky. The minute the high performers see lower performers getting a similar benefit for high percentage growth, but at a much lower level, you had better look out, or there will be trouble at the mill. Hey ho!

Which leads to the last two issues for consideration.

Peer group pressures

The effects of reward systems on work groups, and vice versa, are also manifold, complex and subtle.

To take a simple example, if, to counter the problems noted above, the business takes the escape route of rewarding everyone equally based on group results, this may work well, or it may be a disaster. If the group in question is a cohesive one, the chances are they will rally round the weaker members, share work, share results and allocate resources internally in a way likely to produce the best results.

If the group is not cohesive, internecine warfare is a more likely result than flourishing contributions to the health of the business.

Where cohesive groups are operating, and individual incentives are used, the key question is now the probability of failure. If most are likely not to make it, and hence will not try, the pressure on the stars to conform is great. To ignore the peer group is to risk being sent to Coventry. The more normal response is for the group to either ignore the incentive or start renegotiating rates. Neither of which is what the business normally intends. The spectacular failure of individual piece rate schemes, where cohesive groups exist, to generate net gains in productivity demonstrates the point neatly.

Where distributed groups are at work, and a field sales force is a good example, exactly the opposite effect can be seen. Here while the losers may feel jealous or even resentful of the super stars, the underlying sentiment is still normally one of admiration. It is difficult to avoid the conclusion that people who work on their own deserve the individual success they achieve, simply because they do work on their own. Until, of course, the question of non-equi-potential territories rears its ugly head. Or worse, if there are shared activities, around certain accounts, for example, and one or more of the high rollers is seen to be not pulling their weight.

Private payments and public recriminations

As a final thought, one easy way to avoid the problems of peer groups is to make all reward systems operate on the basis of secret payments. Then the differentials will be unknown and the problem disappears. And any one who believes that can go talk with the fairies at the bottom of the garden.

In any business, from moderate in size up to the conglomerates, the organisation will be riddled with influence networks. For example, in one organisation structure design, employing 10 people, in three layers, there will be 132 simple network links. In this context, 'simple' means without considering the content of those links and whether or not they are agreed or disagreed links.

In a large organisation, there are literally tens of thousands of links, most of which will not be known or understood by senior management. The chances of any 'secret' system staying that way are remote. Moreover, the chances of designing a system that will please everybody are even less remote.

The road to Damascus

So where does all this lead us. To think about reward or incentive systems as a means of motivating people, not very far.

To achieve this goal, the design work will be hideously complicated, and the chances are that, whatever scheme comes out at the end, will still be flawed. The design that makes everyone happy, in a large organisation, is a rare animal indeed. But does that mean that reward systems are useless? The answer is clearly no, but experience suggests that systems which are designed to be short term modifiers of behaviour, communicating what the immediate business priorities are, will have a higher chance of success than those intended to raise motivation overall.

A few simple guidelines could be summarised as:

- Remember that reward systems are information systems. They tell people what is important. What is it the company wishes employees to understand is important? Is that what the reward system is telling them?

- Remember that information systems are reward systems. What is the formal information system telling employees about what is important in the business? Is the message in sync. with the one flowing from the reward system? If it is not, which one is going to have to be modified? And if that is not possible, how can the effect be offset?

- Is the message going down the line through the information system in line with real, strategic business goals?

- Where are there cohesive groups at work in the organisation? How will they see the effect of the reward system? Where are the influence networks? Which of them are working for you? Which are working against you? Which will feel threatened by the new reward system? Which will feel aglow with excitement? Where are there likely to be outbreaks of internecine warfare, if the effect of the reward system is to encourage the worst effects of the mud hut syndrome?

- And finally, the most important question of all. If performance related rewards are to be used, beyond the standard package of salary, pension and life insurance, what needs to be done to avoid the self-fulfilling prophesy of telling people that they do not care about their jobs or the business, but only attend work for the cash? In other words, how to get the message across that employees are valued for their own sakes, as human beings and responsible and committed contributors to the business.

Alternatively, the standard cop out is always available. Blame the workers for everything, jack up the incentives and threaten them with everything from plant closures through five weeks hard labour to the kitchen sink. In which case, we can all meet at the pub and ponder the future of the business - unless the managers wish to get together at the nineteenth hole. Wednesday afternoon, perhaps?

