Performance Measurement, Rewards and Recognition: Aligning Incentives with Strategic and Operational Goals

ABOUT BEST PRACTICES, LLC

Best Practices, LLC is a recognized leader in the field of best practice performance improvement. Our suite of customized Research and Consulting services is designed to assist you in improving your company's performance by analyzing the winning practices of leading corporations and institutions. Best Practices, LLC has conducted leading-edge benchmark research for top companies since 1992. Our corporate motto is "Access and Intelligence for Achieving World-Class Excellence." Let us help you find solutions to your current business issues today! Visit our corporate site at http://www3.best-in-class.com.

HUMAN RESOURCES BENCHMARKING CAPABILITIES

Best Practices, LLC is ideally suited to assist companies in addressing their human resources and personnel development issues. We have extensive experience in conducting quantitative benchmarking research around rewards, recognition and performance measurement metrics for Fortune 500 organizations, as well as gathering the qualitative best practices that truly set world-class personnel development programs apart. For more information about how we can help your organization, contact Jonathan Tanz, Director of Research and Consulting, at (919) 403-0251, ext. 227 or jtanz@best-in-class.com.

A partial list of recent benchmarking studies and topics for rewards, recognition and performance measurement projects includes:

Benchmark Studies

- Employee Performance Management and Development
- Developing HR Performance Measures
- Measurement and Coaching: The Performance Measurement Dashboard
- Growing Leaders Through Employee Development Programs
- Incenting Collaborative Behavior
- Increasing Sales Performance Through Superior Sales Performance Management

Sample Topics Researched in Benchmark Studies

- Aligning individual and corporate strategies
- Coordinating for sales team effectiveness
- Promoting teamwork
- Pay-for-performance metrics
- Enhancing perceptions of fairness in rewards and recognition programs
- Handling sales territory variability
- Facilitating employee progress

Clients have used the results of these projects to identify improvement areas, adjust program goals or methods, build senior management support for new initiatives, lobby for greater resources and generate cost savings.

INTRODUCTION

Businesses must constantly adapt their strategies and goals to address the dynamic forces of the shifting challenges and opportunities of global markets, the organizational upheaval of mergers and acquisitions, and the rapid evolution of productivity tools and technologies. One critical—but frequently overlooked—dimension of this process of renewal is the impact of organizational change on employee motivation and behavior: Executives, operational chiefs and personnel managers must ensure that their systems of rewards and recognition are carefully aligned with overall strategic and operational goals. Rewards and recognition systems misaligned with corporate objectives can result in behavior that is not anticipated or desired by management. These unanticipated actions may be personally beneficial to front-line sales reps, manufacturing floor managers or even senior executives, yet they move the company away from its overall goals or cause systemic harm.

The challenge, then, is to assess and implement an incentive system that motivates employees to act in support of strategic and operational objectives. But how does an operational manager or executive know when they have the right rewards and recognition program, or if the one they have implemented is still having the desired effect? In addition to measuring progress of employee performance toward corporate goals, well-defined performance measurement systems help gauge employee reception, understanding and buy-in for reward systems. This critical feedback can help managers make adjustments necessary to drive improvements and avoid the unanticipated behaviors and actions that negatively impact corporate goals.

KEY INSIGHTS IDENTIFIED BY OUR RESEARCH

Best Practices, LLC has conducted extensive research in several areas of incentives and performance measurement. The following findings are excerpts from prior studies that highlight how Best Practices, LLC assisted human resources executives, operations managers and other key decision-makers at Fortune 500 companies improve the effectiveness of their employee motivation and progress measurement systems. Best Practices, LLC's talented research team can work with you to develop a research study uniquely designed to meet your immediate business management needs.

Link incentives to sales and service performance metrics to preserve high-quality customer relationships.

Most call centers work hard to ensure that service goals are not compromised when cross selling is introduced. Savvy managers disavow inappropriate, incentive-driven product pushing by ensuring their incentive programs reward quality service as well as sales.

To ensure that implementing sales incentives did not tip the balance away from service quality, one partner adopted a mixed incentive approach that weights a variety of performance factors in determining the amount of rewards. "For us," said this senior vice president, "although all our reps cross sell, customer service is seen at the primary function. We teach our employees to identify sales opportunities through serving. To preserve the service focus, our incentives are only partly based on sales. We measure and reward performance based on 45 percent customer satisfaction, 30 percent relationship deepening (sales) and 25 percent productivity."

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>
> *–Senior Vice President, Financial Services Company*

According to this financial services executive, the weighted system has been successful in retaining accounts and building sales because the approach "keeps them from pushing products at the expense of good customer relationships. We actively coach against pushing products." Another advantage, she said, is that associates with service-only backgrounds "feel comfortable because this doesn't feel like selling; it feels like helping – an opportunity to further assist the customer."

Benchmark partners said agents who sell and cross sell successfully see significant salary increases. In some call centers, high performers have the potential to double their base salaries through cross sales. Incentive plans vary significantly. Among the variations described are systems that:

- Pay a set dollar amount for every sale
- Pay an established amount for every sale above a set minimum
- Pay higher incentives for sales of higher margin products
- If some staff refer and others sell, split the incentives so both are rewarded for success
- Use accelerators to award higher sales volumes with larger incentives
- Award incentives to beginners for cross-sell attempts as well as for sales

Design incentive compensation to guide sales reps' behavior in balancing the dual objectives of customer service excellence and sales performance.

At one financial services company, executives learned that they needed to focus incentive compensation so that their representatives would sell the products that made the most sense for their customers, while also delivering revenue and profit growth for the company.

During one period, sales representatives were zealous in placing a financial card product among customers because of a handsome incentive to deploy this product into the marketplace. These were easy new-product placements because most customers were pre-qualified to receive these products. When managers observed that some customers were receiving four to five cards per household, they fine-tuned the incentive system to guide reps to a more balanced mix of service excellence and new-product placement.

Having so many cards may have benefited the customer service/sales representatives who sold them (with incentive pay each time a product was placed), but it did not enhance customer service and probably had the opposite effect – customers were likely confused about what it was they were getting each time they agreed to a new card. The company has now devised a modified incentive plan that depends on employee success in three areas:

> **"You have to understand what you're incenting for as a growth company. We want to incent for customer satisfaction, relationship deepening and productivity. And incentives are tied to those scorecards."**
>
> *--Senior Vice President, Financial Services*

- Customer relationship deepening
- Customer satisfaction
- Sales productivity

Now sales representatives' incentive pay is determined by how well they are judged in scorecards that take all three factors into consideration, not just sales volumes. That helps determine whether their sales activities are adding value to the customer experience, and ensures growth in customer business.

Link compensation with team performance to drive collaborative behavior.

Teams at one telecommunications company that are required to meet the "six-sigma" quality standards are paid bonuses tied to improved defect rates and cycle times (as are their bosses), and compete against one another for gold medals in company-wide performance contests. The link between team compensation and performance further aligns employees with high level corporate objectives because cycle time and quality (as measured through six-sigma standards or 3.4 errors per million) are performance measures and performance goals of all of the company's work units.

Link incentive compensation to cross-unit effectiveness.

One transportation company's system links incentive compensation equally to people satisfaction, customer satisfaction and profits; it also links individual and team performance. Compensation plans are balanced with components to reflect the corporate credo and its corresponding stakeholders such as people (employees), service (customers) and profit (shareholders). If the team does not meet its goals, all individuals will forfeit portions of their incentive compensation.

Allow Cross-Functional Teams to Participate in Merit Pay Allocation.

One technology company links compensation to team performance and the company also allows some teams to determine the degree of the linkage. Teams help set the criteria used for allocating merit pay. Company officials indicate that most teams start out with merit pay criteria that are based 80 percent on individual factors and 20 percent on team performance factors. As an on-going team matures, it may progress to a 50-50 allocation, which insures that merit pay distributions hinge equally on team and individual performance. Merit pay is zero-based, meaning that the allocation of merit pay in one period is not predicated on previous allocations. Placing merit pay on team activities helps ensure project teams, process teams and task forces work toward common goals. Linking compensation to teamwork and sharing establishes the proper incentive structure to drive district-wide improvement.

Deploy risk and reward compensation systems to drive employee development, team sharing, and teamwork excellence.

Incentive pay provides a constant challenge to all organizations. One automobile manufacturer's version links employee compensation with performance and creates a sense of ownership among all team members. This sense of common ownership —driven through the risk and reward system — encourages higher levels of communication, team work, idea sharing, proactive problem resolution and knowledge exchange. The system rests on some basic fundamentals:

- Determine bottom-line goals of the company and tie people's pay to the goals.
- Clearly set a benchmark for the average level of compensation.

In the risk component of the system, a portion of this base pay is withheld from each employee's paycheck every month. This percentage at risk started at 5 percent and now has moved up to 12 percent of pay at risk. The ultimate goal is to put 20 percent of pay at risk. Currently, the 12 percent is broken down as follows:

- Five percent is training based

- Five percent is quality based (Defects on quality audits)
- Two percent is related to team effectiveness

The risk components are measured on a quarterly basis. If the goals have been met, team members receive the portion of their pay that was put at risk.

Employees are willing to put a portion of their pay at risk because they have the opportunity to make substantially more than the industry average at their positions if another set of goals is achieved. In paying out the reward component of compensation, the following measures are employed:

- Production schedules achieved
- Profitability of the company

Develop standardized quality tools to measure cross-functional team and manager performance.

One technology company's key quality tools and initiatives are embedded in the performance review process, which focuses in part on creating managers and employees who can work together, problem solve together, engage in teams and innovate together. For example, the reporting process at this company shows an employee or manager's performance relative to:

- Customer satisfaction
- Employee motivation and satisfaction
- Market share
- Return on assets

Performance review data can be presented in diagrams that help the team move rapidly through the quality process. These diagrams include:

- Performance against target data
- Root cause analysis
- Pareto analysis
- Action plans / counter-measures

While the does not require that each manager perform the same performance review, the company has developed a set of core metrics for use across the organization. Practices and approaches vary - the goal is for the managers and employees to track the metrics and develop a plan to improve them.

Link cross-functional team compensation to non-financial goals.

One telecommunications company has linked management compensation to its financial and non-financial goals. The incentive compensation links are forged to Economic Value-Added (EVA), People Value-Added (PVA) and Customer Value-Added (CVA) goals. For executives to optimize their incentive compensation, they must achieve together on these organizational goals.

30 percent of middle management compensation is designated as incentive compensation; all elements of this 30 percent are anchored in goals that require cooperation and cross-unit cooperation:

- 10 points or one-third of total incentive compensation is linked to EVA.
- 10 points or one-third of total incentive compensation is linked to PVA.
- 10 points or one-third of total incentive compensation is linked to CVA.

At each mid and upper management level, managers craft action plans that relate to these higher level goals. For instance, one manager may have a goal to reduce “blocked calls,” knowing this will help improve CVA. All managers work with the same formulas.

Employ broad-based team recognition programs to strengthen business excellence.

Another interviewed telecommunications company believes that employee contributions are fundamental to the company's success, and so the organization employs multiple broad-based recognition programs to encourage achievement and to sustain a culture of customer focus and high employee involvement. The company recognizes the efforts of both individuals and groups. Its recognition programs are frequently non-financial or have a low monetary value but serve to reinforce business excellence as defined by the organization’s mission, values and Four Business Priorities. They include recognition gestures such as getting your picture put up on a wall of fame, profiles in internal publications, peer-to-peer accolades, free dinners, etc. Its recognition programs are benchmarked against other world-class companies.

Implement performance measurement scorecards that drive collaborative behavior.

A prominent transportation company employs various sorts of performance measurement scorecards to help focus all the organization on critical issues. Perhaps the most noteworthy example here is the company's SQI (Service Quality Indicators) scorecard. The SQI consists of 12 key performance measures. Each day the company captures and reviews performance on these measures. High-level executives review the SQI measures at a daily performance review meeting. There are teams in place supporting each SQI measure. When a measure moves in the wrong the direction, the executive team and the SQI team spring into action to resolve the operating issue. This structure supports cross-unit cooperation and alignment. Participation on the teams spans geography and departments.

CONTACT US:

This white paper contains excerpts from prior studies that highlight how Best Practices, LLC assisted human resources executives, operations managers and other key decision-makers at Fortune 500 companies improve the effectiveness of their employee motivation and progress measurement systems. Best Practices, LLC's talented research team can work with you to develop a research study uniquely designed to meet your immediate business management needs. For more information about how we can help your organization, contact Jonathan Tanz, Director of Research and Consulting, at (919) 403-0251, ext. 227 or jtanz@best-in-class.com.