Performance-related pay system – A New Reading

When you can measure what you are speaking about, and express it in numbers, you know something about it; but when you cannot measure it, when you cannot express it in numbers, your knowledge is of a meager and unsatisfactory kind.

William Thompson (Lord Kelvin)

4.1 A Deeper Influence to the Meaning

The essence of Performance related Pay is that Differential performance must be differentially rewarded. PRP emerged from the management need of performance budgeting and performance management.

PRP is defined as: Performance Related Pay is the variable component of the pay which is awarded ex-post, after individual/group performance is measured again pre-set and mutually agreed upon goals for a given period of assessment (which will vary by levels of hierarchy). It is non-additive and non-cumulative. It is not an automatic default incentive which is given for the nature of duties and responsibilities or levels of difficulty (working condition) for a certain rank/post.

There are many different types of PRP, ranging from individual to group performance schemes, from those based on largely objective performance criteria to those based on judgemental appraisals, and from those where PRP is paid as a one-off bonus to those where it is consolidated into base pay. All schemes are designed and implemented with the motive that the promise of increased incentives will provide an incentive for greater performance.
The theoretical underpinnings of PRP lie in three broad management theories: expectant, agency and goal-setting. The Expectancy theory deals with PRP at a psychological level. It was propagated by Lawler (1971) and Vroom (1964) and implies that if there is a suitable reward for performance; people will be motivated to increase their efforts in order to achieve a level of performance that will entitle them to the reward. It also implies that if managers expect a negative incentive emanating from certain actions, they will desist from it. It is also connected to the idea of motivational Theory X and Theory Y in the management literature.

The Agency theory proposes that performance related rewards and incentives are needed when the principal (employer) cannot regularly monitor and control the agent’s work (employees). It argues that in the absence of suitable reward for agent’s efforts, the motivation to perform will go down and the overall performance will suffer. It assumes that people act in self-interest and thus PRP is a tool of generating that self-interest on the part of the agents, else the agent will put in only a minimum level of effort with which he can get away with. It also promotes employees risk-taking guided by the motivation of extra reward (PRP) else agents are presumed to be risk-averse. The essence is that agents will work (better) if there exists reward for extra performance.

The Goal-Setting theory presumes that there exists a direct link between the efficacy of the goal-setting process and enhanced employee performance in an organization. It argues that if employees are co-opted in the process of goal-setting and benchmark creation against which their performance will be judged, then the employees are much more committed and motivated for the achievement of those mutually agreed goals. It also presents an opportunity to ensure goal congruence between organizational and individual/group level goals.
The three theories are actually converging and integrative in nature. They together highlight the key operationalizing levers of PRP – effort and motivation for performance is directly related to the expectation of resultant reward; and the crucial importance of goal setting and performance measurement for implementing PRP.

4.1.1 Performance-Related Pay and Related Concepts

4.1.1.1 Performance Measurement

The major purpose of performance measurement is to raise questions. It seldom, if ever, provides answers by itself about should be done.

- Common Complaints about Performance Measurement
  - You can't measure what I do.
  - The measures aren't fair because I don't have total control over the outcome or the impact.
  - It will invite unfair comparisons.
  - Performance data will be used against our program.
  - It is just a passing fad.
  - We don't have the data/we can't get the data.
  - We don't have the staff resources to collect the data.
  - We can't measure prevention.
  - It's not our responsibility.

Whether we use process improvement, process reengineering, Kaizen, just-in-time, activity-based costing, total quality management, continuous quality improvement, or cycle time reduction, we share one basic goal: to do more, better and faster with less. A critical enabler in each of these endeavors is the
ability to measure performance. As the saying goes, “You can’t improve what you can’t (or don’t) measure.”

It has been discovered that performance measures can help any organization:
- Determine where they are – that is, establish an initial baseline “as is” performance level.
- Establish goals based on their current performance.
- Determine the gap or delta between a set of desired goals and current performance levels.
- Track progress in achieving desired performance goals.
- Compare and benchmark their competitors’ performance levels with their own.
- Control performance levels within predetermined boundaries.
- Identify problem areas and possible problem causes.
- Better plan for the future.

The insights gained from systematically measuring performance can be truly amazing.

Some key concepts and definitions relating to performance measurement include:

- **Baseline performance**: This is the current level at which an organization, process, or function is performing. A company currently producing 25 units per week has a current baseline performance of 25 units per week.

- **Family of measures**: This represents a group of usually four to six interrelated but still separate key aspects (or family members) of performance. Key types of measures within a family of measures typically include –
- Productivity measurements (e.g. 25 units produced per week)
- Quality measurements (e.g. 3.8 defects per 25 units)
- Timeliness measurements (e.g. 96 percent of orders completed on time)
- Cycle time measurements (e.g. a production cycle time of 6 hours per unit)
- Resource utilization measurements (e.g. production workers utilized 65 percent of the time)
- Cost measurements (e.g. production cost of Rs. 325 per unit)

- **In-process performance measure**: This is a performance measure collected within a process. For example, if a process is comprised of three major activities, the cycle time of each individual activity would be an example of an in-process performance measurement. So would the number of generated defects associated with each individual activity.

- **Key performance factors**: These performance variables are especially critical in achieving a desired set of outcomes. Key performance factors are normally linked to core products and services and associated customer expectations. For example, in a service industry, timeliness, quality and cost represents three key performance factors.

- **Performance**: An actual work accomplishment or output. In this context, performance should not be confused with work behaviour. Performance focuses on actual accomplishment or produced output. It also could be understood as what’s left behind at the end of the day.
- **Performance goal:** This is a targeted level of accomplishment expressed as a tangible and measurable objective against which actual achievement is compared. For example, a performance goal may be to process, on average, 60 procurement requisitions per day.

- **Performance indicator:** This is a comparative performance metric used to answer the question, “How are we doing?” for a specific issue. The average number of requisitions processed per day is an example of a performance indicator.

- **Performance measure hierarchy:** This is when the same performance measure (e.g. cycle time) is tailored to different user needs at different levels within an organization. For example, whereas front-line supervisors are probably most interested in the cycle time of their own particular activity, the general manager is interested in the total cycle time of all combined activities.

- **Performance measurement:** This is the process of measuring work accomplishment and output, as well as measuring in-process parameters that affect work output and accomplishments. Measuring the cycle time of a service process would be an example of taking a performance measurement.

- **Performance measurement system:** This is normally a graphical and numerical information system used to achieve desired performance levels. A performance measurement system involves the collection, synthesis, delivery, and display of information related to the measurement of work output and accomplishments, as well as in-process parameters that affect work output and
accomplishments. All of the varying elements of an organization’s performance measurement program comprise a performance measurement system.

- **Performance metric:** This is a specific performance measurement such as a cycle time or quality yield.

- **Process:** This represents the transformation and blending of a set of inputs into a more valuable set of outputs. Outputs can be products, services, or accomplished tasks. A process can be further subdivided into individual process steps (e.g. operation, transportation, delay, inspections, storage, and rework).

### 4.2.0 Introducing Performance-related Pay

PRP should be introduced on the fundamental belief in the virtues of rewarding people according to their contribution and that it will make a striking impact on organizational performance.

PRP schemes should provide:

- A clear and strong link between performance and contribution and subsequent reward;
- A fair and consistent basis for measuring performance and contribution;
- A worthwhile reward in line with employee expectations;
- Value for money (cost effectiveness) – the gains to the company in terms of improved organizational performance should exceed the cost of the scheme.
4.2.1 Factors to be considered while introducing PRP

- **Matching the culture**: There is no magic set of performance measures or simple set of rules waiting for adoption on a universal basis. Successful PRP schemes need to match the culture and core values of the organization.

- **Linking PRP to the performance management process**: The focus when relating pay to performance needs to be on issues which emerge from the business planning process such as profitability, productivity, cost control, research initiatives, product and market development and generally increasing shareholder value.

- **Balancing performance measures**: The performance measures used as a basis for rating must include a balanced mix of both input and process factors (skills and competencies) and output factors (performance and contribution). The assessment upon which pay decisions are made should be based not only on performance in achieving objectives, contribution to organizational success and the levels of skill and competence achieved, but also on the degree to which the behavior of individuals supports corporate values in such areas as teamwork, total quality management, customer service and innovation.

- **Flexibility**: PRP arrangements should allow for some flexibility in the criteria for reward and the method of payment. There may be occasions, when it would be more appropriate to pay a lump sum achievement bonus rather than to increase the basic rate of pay.

- **Teamwork**: Poor PRP schemes can produce a lot of single-minded individualists. The importance of teamwork should be recognized in structuring the scheme and in defining critical success factors and
performance indicators. Individuals should be aware that achieving their targets at the expense of others is not considered competent performance.

- **Avoiding short-termism:** To avoid the danger of PRP focusing attention on short-term results at the expense of more important longer-term objectives, long-term as well as short-term goals should be set wherever appropriate and short-term objectives should be discussed in their overall context.

- **Involvement in the design process:** The design of PRP schemes is usually an iterative process – trying and testing ideas on measures and structure with those who will eventually be involved in the scheme. It is also a valuable learning process which can throw up fundamental strategic and business issues. Those due to participate in the scheme should have an input into agreeing critical success factors and performance indicators both for themselves and the organization.

- **Getting the message across:** PRP provides a very powerful form of communication. To get the right message across, the following questions will have to be dealt with –
  
  Q – How can the scheme achieve the best possible launch?
  Q – Is it better to give no payout than low payout?
  Q – What is the best psychological moment for payout?
  Q – What communications should be used to ensure that all concerned appreciate the aims of the scheme, understand how it will work, and appreciate how they will benefit from it?

4.2.2 Development Programme
Performance-related pay schemes need careful implementation over a period of time to achieve maximum effectiveness and acceptability. Most appear to believe that all they have to do is wave the magic wand of PRP and, miraculously, all their motivational and performance problems will be over. There is a tendency for some managers to think that people at work do not want to do a good job and must therefore be bribed to increase their efforts through the offer of extra cash. It is certainly true that they expect too much too soon!

The sequence of activities in a PRP development programme is illustrated in Figure 4.1
1. Asses reasons for PRP
   - Why introduce PRP?
   - What, realistically, is expected out of it?

2. Asses readiness for PRP
   - Is PRP right for the organization’s culture and is the organization’s culture right for PRP?
• Are performance management and other processes in place for successful PRP?
• Are the attitudes of management and other employees in favour of PRP? (An attitude survey can be conducted to establish opinions)
• Do the people, concerned with managing PRP, have the required skills and resources?
• Is PRP likely to make a significant enough impact on performance to justify the costs of developing, introducing and operating the scheme?

3. Decide whether or not to introduce PRP
• Does the result of the above assessment indicate that PRP is right for the organization?
• If so, what are the objectives of PRP? Consider Improving performance, delivering messages about performance expectations, focusing attention on key issues, culture change, and maintaining a competitive pay position.
• If not, what are the alternatives? Consider performance-related team pay plans, organization-wide profit sharing or profit-related pay plans, gain sharing, the use of incentives or bonus schemes, concentrating more on the motivational aspects of performance management, job re-design to increase motivation, performance-related training, more intensive management coaching and training to improve leadership abilities, process re-engineering to improve organizational performance and productivity.

4. Brief, consult and involve employees
• How should employees be informed of the organization’s objectives and intentions concerning the introduction of PRP?
• To what extent should the employees be consulted and involved? (The more the better)
5. Design scheme

- What criteria should be used to determine PRP awards? Consider the use of an appropriate mix of:
  - Input criteria related to the skills and knowledge brought to bear on fulfilling role responsibilities;
  - Process criteria related to the behavioural competencies used successfully in achieving results;
  - Output performance indicators related to the achievement of objectives and meeting performance requirements as set out in statements of principal accountabilities or main tasks;
  - Outcome contribution indicators which measure how outputs contribute to the achievement of team, departmental and organizational objectives and how the behaviour of individuals supports corporate values.

- To what extent will it be possible to define the criteria in the key jobs for which PRP will operate?

- Are performance measures available for these criteria which will enable fair and consistent assessments to be made?

- What form of rating system should be used?

- How are we going to ensure that ratings are fair and consistent?

- What are the policies to be on the size of payments in relation to performance, contribution, skill and competence?

- What should our policies be on the rate of progression and any limits to progression within pay ranges?

- Are any provisions made for performance-related lump sum bonuses for special achievement or sustained high-level performance at the top of a range?

- Should PRP reviews be separated in time from performance reviews conducted as part of the performance management process?
• What rating, pay increase and budget guidelines are to be issued to managers implementing PRP in their departments?
• Should performance matrices be used? If so, how should they be constructed?
• How should PRP be monitored and its effectiveness evaluated?
• How should the cost of PRP be controlled?
• What is the programme for developing and introducing PRP?

6. Brief and train
• How to brief and train line managers on the PRP scheme?
• How to brief employees in general on PRP in a way which ensures that they understand how to operate and how will it be beneficial?

7. Implement
• How to start the process off? It is necessary to introduce the scheme with great care. However carefully it has been planned, some unforeseeable problems will inevitably arise. It is often advisable to start with a pilot scheme, probably at management level so that they understand the principles, benefits and problems before applying PRP to the people for whom they are responsible.
• How to monitor the introductory stages? It is essential to keep closely in touch with how things are going so that problems can be anticipated or dealt with swiftly when they arise.

8. Evaluate
• Have clear objectives been established for the scheme the progress towards which can be measured and evaluated?
• How to carry out a continuing monitoring and evaluation process?
• Who is responsible for evaluation and taking any corrective action that may be required?

An essential set of requirements for an PRP scheme includes an agreed set of targets (either objectives or developing competences or both), an effective and robust method of measuring the performance against the
targets and regular feedback to the employee. The outcome of a review at the end of the period (usually a year) is normally a performance rating. This can be fairly simple, such as the rating from 1 to 5 in figure 4.2 or a more complex calculation as in figure 4.3. The figure for pay increase is pre-determined, based on the budget available for increased labour costs.

Figure 4.2 – Conversion of ratings into pay increases

<table>
<thead>
<tr>
<th>Performance Description</th>
<th>Rating</th>
<th>Pay Increase</th>
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</thead>
<tbody>
<tr>
<td>Excellent performance, all targets greatly achieved</td>
<td>5</td>
<td>8%</td>
</tr>
<tr>
<td>Superior performance, majority of targets met or exceeded</td>
<td>4</td>
<td>6%</td>
</tr>
<tr>
<td>Normal performance, good proportion of targets met although a few missed</td>
<td>3</td>
<td>4%</td>
</tr>
<tr>
<td>Below average performance, with a number of key targets missed and weaknesses shown</td>
<td>2</td>
<td>2%</td>
</tr>
<tr>
<td>Very weak performance, with few, if any, targets met and disciplinary action to be considered</td>
<td>1</td>
<td>0%</td>
</tr>
</tbody>
</table>

Figure 4.3 – Conversion of ratings into a pay increase in a complex scheme

There are six objectives for the employees to achieve with the following weightings:

<table>
<thead>
<tr>
<th>Objective</th>
<th>Weighting</th>
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<tbody>
<tr>
<td>Objective 1</td>
<td>30%</td>
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<tr>
<td>Objective 2</td>
<td>20%</td>
</tr>
<tr>
<td>Objective 3</td>
<td>20%</td>
</tr>
<tr>
<td>Objective 4</td>
<td>10%</td>
</tr>
<tr>
<td>Objective 5</td>
<td>10%</td>
</tr>
<tr>
<td>Objective 6</td>
<td>10%</td>
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</tbody>
</table>

At the end of the period, a decision is reached that the level of performance on the objective is:
<table>
<thead>
<tr>
<th>Objective</th>
<th>Achievement Level</th>
<th>Rating</th>
<th>Outcome</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>80%</td>
<td>30%</td>
<td>24 points</td>
</tr>
<tr>
<td>2</td>
<td>100%</td>
<td>20%</td>
<td>20 points</td>
</tr>
<tr>
<td>3</td>
<td>90%</td>
<td>20%</td>
<td>18 points</td>
</tr>
<tr>
<td>4</td>
<td>50%</td>
<td>10%</td>
<td>05 points</td>
</tr>
<tr>
<td>5</td>
<td>100%</td>
<td>10%</td>
<td>10 points</td>
</tr>
<tr>
<td>6</td>
<td>60%</td>
<td>10%</td>
<td>06 points</td>
</tr>
<tr>
<td><strong>Total Points</strong></td>
<td></td>
<td></td>
<td><strong>83 points</strong></td>
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</tbody>
</table>

Conversion to salary increase

<table>
<thead>
<tr>
<th>Points</th>
<th>Salary increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-50</td>
<td>Zero</td>
</tr>
<tr>
<td>50-69</td>
<td>2%</td>
</tr>
<tr>
<td>70-89</td>
<td>4%</td>
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<tr>
<td>90-99</td>
<td>6%</td>
</tr>
<tr>
<td>99-100</td>
<td>8%</td>
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In both of these examples, the schemes are set up as an **incentive**, to demonstrate to the workforce that there are opportunities to achieve a higher pay increase than average through working harder and smarter to meet the agreed targets. They can also act as a **reward** to those employees who perform above average.

**The arguments in the favour of PRP are:**

- It is fair to distinguish between the high performer and those that are only average or below average.
- Making payments to high performers reinforces the message that the organization recognizes and encourages high performance and establishes a clear culture throughout the organization.
• The process of setting objectives clarifies what an employee needs to achieve and thereby focuses his or her attention and effort.

• By being focused, employees act in a flexible way to achieve the required results rather than simply carrying out their job as defined by their job description. They become facilitators and problem solvers and circumvent bureaucratic barriers.

• The opportunity for differential earnings is a recruitment aid, attracting ambitious, result-oriented applicants.

• Achieving results and obtaining good pay increases is a positive force for raising morale in the organization.

4.3 PRP in the Private Sector

Incentive for performance is the norm in the private sector for quite some time now. Traditionally, it was largely concentrated on high level managers and was a means of awarding them something extra for good performance and good behaviour. Now it has been extended to the entire organization including the lower level employees. Managers normally receive cash incentives or stock options as incentive for performance and lower level employees receive individual or group bonus for good performance.

PRP schemes are tightly coupled with organizational objectives which are translated into individual/group level objectives for each group in consultation with his immediate supervisor and the expected level of performance is mutually agreed upon. Employees' performance is then measured against this on an annual basis (largely) and variable component of performance-pay is determined according to the level of performance achieved. Usually PRP schemes in the corporate sector incorporate a variety of criteria for measuring performance and awarding PRP - individual level, group level, team-based, skill based, development
based etc. and most of their annual incentive increases emerge from this set of criteria.

Certain organizations have a system of imposing forced ranking system and quotas wherein employees are necessarily ranked in different categories. For example, only 20% of the employees can be rated at the highest level for the award of PRP. This system of imposing quotas is increasingly becoming popular in the corporate sector.

An important point to note here is that every single organization has a different system that best suits its needs and complexities. This fact must be kept in mind when implementing PRP so that each organization is given a choice about the matrix of PRP implementation.

4.3.1 Why is PRP desirable?

PRP may improve individual motivation and accountability and thus in turn performance. It will also promote innovation and risk-taking.

Processes and systems required for PRP implementation act as a catalyst for introducing organizational changes and helps organizations in recasting their culture. It leads to wider management and organizational change like effective appraisal and goal setting processes, clarification of tasks, acquisition of skills, enhanced team work and increased flexibility in service delivery. In fact, PRP can be seen as a strategic tool in the hands of the management to bring about a lot of process re-engineering in their organizations. It will give organizations an opportunity to re-visit their archaic processes and mechanisms and update them in the light of current social, economic and technological development.
This might eventually turn out to be a greater advantage of implementing PRP than just being a tool for allocating additional incentive to selected employees. The benefits of re-engineering will be available to the entire organization; this makes it highly desirable and critical for effective and efficient functioning of organizations.

4.3.2 Life Cycle of PRP

Performance related pay systems, like all systems are organic and must evolve with time; else they will become redundant and unsuited to the environment as the context in which they are applied changes because of social, economic and technological changes. If PRP systems don’t keep pace with these changes they will become irrelevant and may even cause a downward spiral in organizational performance if goals of the organization change, but the performance pay structure still rewards old priorities.

PRP systems must be used as a tool to focus on evolving priorities and to implement changes that are presently important and critical for the organization. The pace of change within the organization can be accelerated if the performance pay structure can be tightly aligned and coupled with new organizational objectives and priorities. In fact, if the organization identifies a particular area where it needs to focus change, it can re-design its PRP systems accordingly to create incentives for its employees to bring about the desired change. Once the employees have the right incentives which are attractive enough, they will quickly modify behavior and bring about the required changes.

It can be argued that performance related pay systems have their own life cycle and loose the strength of their initial design and logic over time. They must be fundamentally reformed with changes in
the organizational structures, processes, nature of work, priorities and in line with the changes in the external environment (economic, labor conditions, social, technological changes etc)

4.4 Performance Management System – Managing, Planning and Reviewing

The company’s Performance Management System is a process for improving performance by optimizing the contribution, skill and capability of the staff. It is not another task but a 365 day process based on a two-way communication between managers and job holders.

There are two distinct activities to Performance Management which should take place each year:

A. Performance Meeting
B. Development Meeting

A. What are Performance Meetings?

Performance Meetings are the annual formal review of the past 12 months’ performance against KRAs and Objectives, along with developing a new performance plan for the future. Most plans will cover a 12 month cycle. However, for some jobs a shorter cycle may be appropriate. Performance meetings are scheduled to take place in August/September each year, the results of which are a contributing factor to any bonus review later in the year.
a) What are KRAs?

Key Result Areas (KRAs) are the on going results or outputs a job is expected to achieve. The characteristics of KRAs are:

- Taken together they represent ALL the key outputs of a job.
- They focus on RESULTS not duties or activities.
- They refer to WHAT has to be achieved not how.
- Each one is distinct from the others and describes a discrete area in which results must be achieved.

There are two elements to a KRA:

i) **Statement** describing the output or service.
ii) **Measures** which indicate how the KRA can be evaluated.

Whilst the output statement will stay the same, it is possible that some of the measures (or the results) may changer year on year to represent new performance levels or changes in business requirements.

b) What are Objectives?

Objectives are the specific activities or projects the individual is required to achieve in a given period. Typically, objectives are written to either “develop” or “improve” performance. Objectives differ from KRAs in that individuals doing the same job may have different objectives because of the need to focus on different things, whilst their KRAs are the same. Objectives change at each meeting whereas KRAs would not change unless the job changed significantly.

It is important to test whether the objectives are S.M.A.R.T
The ‘SMART’ approach:

S  Is it **specific**? Does it state exactly what is to be accomplished? ‘Improving quality’ is too vague; ‘implementing a system for improving response times to… etc’ might be the start of a more specific objective.

M  Is it **measurable**? How will you and the job holder know whether or not the objectives have been achieved? Can performance be quantified and assessed?

A  Is it **achievable**? Is the objective challenging, but within reach if the job holder is committed and performs effectively? What constraints might affect performance and have you allowed for them?

R  Is it **relevant** to business goals? Are you clear about the long and short term company objectives and strategies? What should your function be doing to contribute to these? Does the job holder’s objective focus on these priorities?

T  Is it **time framed**? What deadlines need to be met? Are there any key milestones which must be met if the overall objective is to be achieved?
Performance Plan and Review

1. Objectives for Oct 2008 to Sept 2009
   
   Set objectives in order to focus employees actively for the next twelve months
   
<table>
<thead>
<tr>
<th>Objectives</th>
<th>Date</th>
<th>Interim review</th>
<th>Final review</th>
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2. KRAs Review

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<thead>
<tr>
<th>KRA Heading</th>
<th>Performance review October 2008 to September 2009</th>
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<tbody>
<tr>
<td></td>
<td>Comment on those KRAs where there has been either exceptional performance or where performance has not met expectations.</td>
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Employee Comments

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<thead>
<tr>
<th>Development Meeting Jan/Feb 2009</th>
<th>Performance Meeting Aug/Sep 2009</th>
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Interim Sign-off Jan/Feb 2009

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Final Sign-off Aug/Sep 2009

<table>
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<th>Employee</th>
<th>Date</th>
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Manager

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Manager’s Manager

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Performance Rating
By linking the performance management cycle to the business planning cycle, there is an opportunity to have an interim review at the development meeting in January/February of each year. This will help align individual performance objectives with the need of the business.

**The Organizational Climate**

Performance Management has been described as “managing people to do the right things, in the most effective way to the best of their ability.” To ensure that this happens, there needs to be an honest and open working environment between employees and their managers where they can voice their feelings and opinions freely together.

Creating an appropriate organizational climate is an essential feature of the company’s Performance Management process. This climate is created by the management styles used by our managers at all stages in the Performance Management Cycle.

By climate we mean those aspects of the environment that directly impact on peoples’ ability to do a job well. To create the desired climate the following factors need to be considered:

- **Clarity:** The feeling that employees know what is expected of them and they understand how those expectations relate to the larger goals and objectives of the organization.

- **Standards:** The emphasis that employees feel management put on doing one’s best. It also includes the degree to which people feel that challenging but attainable goals are set for both the organization and its employees.
• **Responsibility:**

The feeling that employees have a lot of authority delegated to them; the degree to which they can run their jobs without having to check everything with their manager, but feel fully accountable for the outcome.

• **Flexibility:**

The feeling employees have about how easy it is to get new ideas accepted in the organization. Also they are able to do their work as they see it needs to be done; versus the feeling that there are unnecessary rules, procedures, policies and practices which interfere with them doing a good job.

• **Team Commitment:**

The feeling that employees are proud to belong to the organization and to trust that everyone is working towards a common objective.

• **Recognition:**

The degree to which employees feel they are being recognized and rewarded for good work, and such recognition is directly and differentially related to levels of performance.

• **Development:**

The key action taken to ensure employee key skills and behavior are constantly developed to support the business, and the feeling that their career aspirations are being considered.

B. **What are Development Meetings?**
Development Meetings are the annual formal review of progress against a previously set Personal Development Plan, with a particular focus on assessment against the Success Factors. By comparing Personal profiles and Role profiles, the manager and the employee are together able to:

- Evaluate the effectiveness of previous development activities.
- Identify future key development areas.
- Identify important actions to improve performance, forming a new Personal Development Plan.

Most personal development plans will cover a 12 month cycle. However, for challenging areas of development (e.g., Becoming a project manager or under performance), a shorter cycle may be appropriate.

Development Meetings are scheduled to take place in January/February each year, the results of which are contributing factor to any salary review later in the year.
a) What are Success Factors?
‘Success factors’ are the key behaviors that are required to deliver superior performance within the company. As a result of internal research 12 ‘Success Factors’ have been identified which have been split into 4 clusters as follows:

![Table](image)

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- **Analytical Thinking**
- **Achievement Drive**
- **Business Understanding**
- **Leadership**
- **Purposeful Creativity**
- **Teammwork & Cooperation**

<table>
<thead>
<tr>
<th>Success Factors</th>
<th>Role Profile</th>
<th>Personal Profile</th>
<th>Development Objectives</th>
<th>Date by when</th>
<th>Progress Action</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Development Recommendations:</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>Development Recommendations:</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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**Personal Development Plan**

<table>
<thead>
<tr>
<th>Development Review</th>
<th>Annual Rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sign off Jan/Feb 2009</td>
<td></td>
</tr>
</tbody>
</table>

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Employee: 
Manager: 
Manager’s Manager: 
Date Sign-off: 

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- **Analytical Thinking**
- **Achievement Drive**
- **Business Understanding**
- **Leadership**
- **Purposeful Creativity**
- **Teammwork & Cooperation**
In addition, each Success Factor has been classified into one of 3 groups:

1. Core: Success Factors that are applicable across ALL jobs (highlighted above by a √)
2. Critical: Success Factor that is critical to achieving the results in the job. These will vary from job to job and department to department.
3. Contributory: Success Factors that are relevant, but less important compared to the critical Success Factors.

**Setting Objectives**

One of the key elements of PMS is the way in which objectives for the Performance and Development plans are both set and written.

In most cases an objective is a ‘statement of intent or action’. It is a means of offering guidance on what needs to be achieved and by when. Objectives can
vary from stating various sales targets to be achieved, to producing a report on a competitor, booking or organizing a conference, improving relations with another department, developing a specific skill etc.

The ‘SMART’ approach mentioned above offers criteria to use as guidance in writing objectives. The manager can use the checklist to validate the objectives set for his staff. An employee can also use the checklist to validate the objectives set for him.

For the **MANAGER**, the performance management system will:

- Translate business plan objectives into meaningful department and, ultimately, individual objectives for employees to help the company achieve its business goals.
- Provide a framework to initiate discussion on PERFORMANCE and help keep performance ‘on track’.
- Promote discussion on personal opportunities and DEVELOPMENT needs.
- Promote a motivational climate to support superior performance.
- Develop relationships with team members, and allow him, the manager, to deal with performance and development issues in an open and constructive way.

**The Performance Meeting**

The Performance Meeting will ideally be linked directly to the business/department plan. It enables the manager to determine a team member’s KRAs and Objectives that will help support and achieve the business plan. Typically, the meeting takes the form of a one hour session between the manager and a team member in August/September each year. The focus of the time together is primarily on the team member’s present job and performance
against the KRAs and Objectives. Once this review is complete, confirm the
KRAs are still relevant and set objectives for the next review period.

The Manager’s Role in Undertaking a Performance Meeting

There are three key stages to undertaking a performance meeting:

I. Before the meeting:
   - Arrange the meeting (give at least 2 weeks notice).
   - Book a meeting room.
   - Ensure the employee is aware of the Business/Development plan, where available.
   - Remind the employee of the importance of the meeting.
   - Ask the employee to prepare.
   - Consider the contribution the employee has made against their KRAs and Objectives and make notes.

II. During the meeting:
   - Use the pre meeting notes to discuss progress against KRAs and Objectives.
   - Obtain feedback from the employee on their performance.
   - Discuss any areas where expectations are unclear or further clarity/agreement is required.
   - Give feedback.
   - Jointly agree a new Performance Plan and Objectives along with criteria to assess performance for the next 12 months.
   - Give the employee an overall performance rating (see below).
   - Make notes of what was discussed and agreed.

III. After the Meeting:
   - Complete the KRA and Objectives review on the form.
• Write up new Objectives with target completion dates.
• Write in the performance rating (see below).
• Sign and give form to employee to sign and make any necessary comments.
• Pass to the manager for sign-off.

Performance Rating for August/September

(This table should be used to identify the Performance Rating. If an employee is achieving the criteria described for both KRAs and Objectives, a rating should be given. However, where performance against KRAs and Objectives is different, an overall judgment should be made based on the importance and complexity of the KRAs and Objectives allocated, and the environment in which they were allocated).

<table>
<thead>
<tr>
<th>Rating</th>
<th>KRAs</th>
<th>Objectives</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Exceptional Performance. Has exceeded expectations in ALL KRAs.</td>
<td>Exceptional Performance. Has exceeded expectations on ALL Objectives.</td>
</tr>
<tr>
<td>AB</td>
<td>High Performance. Exceeded expectations in some KRAs, fully met others.</td>
<td>High Performance. Exceeded expectations with some Objectives, fully met others.</td>
</tr>
<tr>
<td>B</td>
<td>Good all-round Performance. Has fully met KRAs</td>
<td>Good all-round Performance. Has fully met Objectives.</td>
</tr>
<tr>
<td>BC</td>
<td>Fair Performance. Has achieved most KRAs. However, some have not been met.</td>
<td>Fair Performance. Has achieved most Objectives. However, some have not been met.</td>
</tr>
<tr>
<td>C</td>
<td>Poor Performance. Has not achieved the majority of KRAs. Considerable room for improvement.</td>
<td>Poor Performance. Has not achieved the majority of Objectives. Considerable room for improvement.</td>
</tr>
</tbody>
</table>

(Agreeing the Performance Rating involves making an evaluation of performance based information gathered over a 12 month period. The overall rating should be based on performance against KRAs and Objectives agreed in the Performance Plan).

The Development Meeting

There is clear evidence that those companies that invest in developing their people are able to demonstrate significant economic benefits. If a company
makes a decision to do this, where does it start? In a business setting, learning is best encouraged and managed by introducing Development Meetings and their associated outputs, Personal Development Plans.

**What can a Development Meeting provide?**

Employees have jobs, careers, and lives outside of work. Sometimes they are so involved with their everyday lives that they rarely take the time to pause and think about whether their lives/careers are really satisfying, or what they should do to make them more satisfying.

They know that it is useful, often vital, to stop occasionally to review and reflect. In this case, perhaps the most valuable benefit of a Development Meeting is that it should provide them with an opportunity to reflect and then plan elements of their career. More specifically, it is a chance for them to:

- Collect data about the employee, his skills, interests, the type of person that he is, how he behaves, what is important and unimportant to him and his preferred career path.
- Find out what opportunities there might be for him in the company now and in the future.
- Think about how he would like to learn and develop.
- Discuss his development needs openly with his manager.
- Make suggestions as to how his manager and the company could help him develop.
- Produce a Personal Development Plan.

Typically, the review takes the form of a one hour session between him and his immediate manager in January/February each year. The focus of the time together is primarily on his performance against the 12 Success Factors and his current level of skill and knowledge. Development Plan (past Success Factor
evaluation) from the previous meeting would also be examined, leading to a new Development Plan being defined and agreed for the next 12 months.

The Employee’s Role in Participating in a Development Meeting:

There are three key stages and associated actions to participating in a Development Meeting:

I. Before the meeting:
   - Remind him of the Success Factors and the levels defined for his role/job.
   - Prepare by reviewing and considering his actual performance against the performance expectation detailed in his job profile and his present development plan.
   - When his manager distributes a copy of his profile (which is based on their current view), make a note of his views against his manager’s rating.
   - Collect evidence to support his achievements, especially if his view of his performance differs greatly from that of his manager.
   - Identify any support or development activities that may be required to close gaps between Success Factor and Performance.
   - Complete the Personal Development Plan Section: ‘Progress Action’.
   - Document his evidence in preparation the meeting.

II. During the Meeting
   - Review his Personal Development Plan Objectives.
   - Use his pre meeting notes to discuss progress against the role profile of Success Factors.
• Take responsibility for identifying and discussing issues, including any help that he may need.
• Actively listen to his manager’s views, look for compromises and understanding. Jointly agree his Personal Profile.
• Discuss any areas where expectations are unclear or further clarity/agreement is required.
• Jointly agree whether any objectives need to be revised in light of new business plans.
• Jointly identify and agree new development areas, along with the criteria to assess your Development for the next 12 months.
• Jointly agree support or development actions.
• Make any relevant notes through the discussion.

III. After the Meeting
• Sign and return the document to his manager after making any necessary comment.
• Take ownership of the agreed development actions.
Agreeing the Annual Rating involves an evaluation of potential in the company. This is indicated by development progress in the past 12 months and Performance in the role (i.e. against the KRAs and Objectives – the role expectations) during the preceding few years.

<table>
<thead>
<tr>
<th>Rating</th>
<th>Criteria</th>
</tr>
</thead>
</table>
| A      | Exceptional Performance.  
         | Has exceeded expectations in the role and ALL their development objectives. |
| AB     | High Performance.  
         | Has exceeded expectations in most part of the role as well as most of their development objectives. |
| B      | Good all-round Performance.  
         | Has fully met expectations in the role, as well as their development objectives. |
| BC     | Fair Performance.  
         | Has met some expectations in the role, as well as some of their development objectives. |
| C      | Poor Performance.  
         | Has not met expectations in the role and/or their development objectives. |

For the EMPLOYEE the performance management system will:

- Ensure he knows what is expected of him and the criteria against which performance is evaluated, along with providing him with regular and consistent feedback on performance.
- Provide him with a sense of participation in setting objectives and ownership of accomplishing meaningful department objectives that help the company achieve its business goals.
- Provide him with a framework for initiating discussion on PERFORMANCE and help keep performance ‘on track’.
- Promote discussions on his personal opportunities and DEVELOPMENT needs.
- Promote a motivational climate to support superior performance.
- Help develop a relationship with his manager to allow discussion on performance and development issues in an open and constructive way.

**The Performance Meeting**

The Performance Meeting will ideally be linked directly to the business/department plan. It enables him to understand the KRAs and Objectives that he will be required to achieve in order to help and support the business/department plant. Typically, the review takes the form of a one hour session between him and his immediate manager. The focus of the time together is primarily on his present job and how you have been performing against the KRAs and Objectives. Once this review is complete, he will need to confirm his KRAs are still relevant and set Objectives for the next review period.

**The Employee’s role in participating in a Performance Meeting**

There are three key stages and associated actions to undertaking a Performance Meeting:

I. **Before the Meeting:**
   - Consider progress made against his KRAs and Objectives, and make notes to demonstrate his achievement.
• When available ask to see an updated copy of the Business/Department Plan.
• Prepare questions for areas that need clarifying.

II. During the Meeting:
• Use his pre meeting notes to discuss progress against KRAs and Objectives.
• Discuss his overall performance, highlighting his successes.
• Discuss any areas where expectations are unclear or further clarity/agreement is required.
• Give feedback to his Manager when appropriate.
• Jointly agree a new Performance Plan and Objectives along with criteria to assess your future performance for the next 12 months.
• Make notes of what was discussed and agreed.

III. After the Meeting:
• Check the comments made on the review form.
• Review the new Objectives that have now been set with target completion dates.
• Sign and give the document back to his manager after any necessary comments have been made.

The Development Meeting

There is clear evidence that those companies that invest in developing their people are able to demonstrate significant economic benefits. If a company makes a decision to do this, where does it start? In a business setting, learning is best encouraged and managed by introducing Development Meetings and their associated outputs, Personal Development Plans.

What Can a Development Meeting Provide for a Team?
Employees have jobs, careers, and lives outside of work. Sometimes they are so involved with their everyday lives that they rarely take the time to pause and think about whether their lives/careers are really satisfying, or what they should do to make them more satisfying.

They know that it is useful, often vital, to stop occasionally to review and reflect. In this case, perhaps the most valuable benefit of a Development Meeting is that it should provide them with an opportunity to reflect and then plan elements of their career. More specifically, it is a chance for them to:

- Collect data about themselves, their skills, interests, the type of person that they are, how they behave, what is important and unimportant to them and their preferred career path.
- Find out what opportunities there might be for them in the company now and in the future.
- Think about how they would like to learn and discover what resources are available to help them learn and develop.
- Discuss their development needs openly with his manager.
- Make suggestions as to how you and the company could them develop.
- Produce a Personal Development Plan.

Typically, the review takes the form of a one hour session between the employee and his immediate manager in January/February each year. The focus of the time together is primarily on the employee's performance against the 12 Success Factors and their current level of skill and knowledge. Development Plan (past Success Factor evaluation) from the previous meeting would also be examined, leading to a new Development Plan being defined and agreed for the next 12 months.

The Manager's Role in Undertaking a Development Meeting:
There are three key stages to undertaking a Development Meeting:

I. Before the Meeting:
   - Prepare by reviewing Performance and making notes.
   - Arrange the meeting (give at least 2 weeks notice).
   - Book a meeting room.
   - Collect information on performance against Success Factors.
   - Talk to colleagues/customers to help provide broader feedback.
   - Distribute a copy of the role profile score detailing the employee’s person profile based on the current views.
   - Remind the employee of the importance of the meeting.
   - Identify support or development that may be required to close gaps between Success Factor and performance.

II. During the Meeting:
   - Review past Personal Development Plan objectives.
   - Use prepared notes to discuss progress against the role profile Success Factors.
   - Invite contribution from the employee on their performance.
   - Actively listen, don’t pre-judge performance – seek to understand. Jointly agree a Personal Profile.
   - Offer support and coaching to overcome problems or to explore new development opportunities.
   - Discuss any areas where expectations are unclear or further clarity/agreement is required.
   - Jointly identify and agree new development areas, along with the criteria to assess future development.
   - Jointly agree support and development actions.
• Jointly agree whether any Objectives need to be revised in light of new business plans.
• Provide an annual rating.
• Document what was discussed and agreed.

III. After the Meeting:
• Write in annual rating
• Sign and give form to team member to sign and make any necessary comments.
• Send form to the Manager for sign-off.

4.5 Questions / Myths on Performance Pay

1.0 How can we reconcile the often conflicting needs for our pay structures and levels to be equitable, both internally and externally?
Ans: For employees, a ‘felt-fair’ pay structure is one in which they believe that they are paid appropriately for what they do in comparison with others. Initial comparisons will be internal and they will be aggrieved if they feel that, without justification, they are being paid less than others who are doing the same or even less demanding work or contributing less effectively. Internal equity also means, of course, paying equal salaries or wages for work of equal value. It is important as a means of achieving both job satisfaction and meeting legal requirements.

To get and to keep the right people, organizations have to pay competitively. And the ‘felt-fair principle’ applies just as much to external as internal equity. Employees will be unhappy if they know or think that they are being paid less than the going rate, even if they have no intention of leaving or little chance of getting work elsewhere.
The importance of being competitive depends partly on the degree to which the organization relies on the external as distinct from the internal labour market. And the need to be competitive may only apply to certain jobs where the demand exceeds the supply. Organizations which have to use the external market in these circumstances may well find that they have to offer people more to join than the job is worth according to their internal job evaluation. This situation is commonly dealt with by paying a market premium on top of the normal rate for the grade in which the job holder is placed, according to the rules of internal equity. When this is a recurring problem for a category of employees, the solution may be to form special market pay groups for the job family concerned, with different pay scales, thus sacrificing the principle of internal equity to the imperative of external competitiveness. The extent to which this approach is adopted depends on the strength of the market forces and of the needs of the organization for an individual or a category of employee. If these are both strong then there may be no alternative but to accept that competitiveness must be given priority.

Problems can occur if an organization has to respond to market pressures for recruits but fails to increase the pay of those in the same jobs within the organization in line with market rate increases. People will complain if they find that newcomers doing the same work are paid more than those who have been in those jobs for some time. And they will find this out, even when the pay structure is not published. Managements should never underestimate the propensity for employees to exchange information amongst themselves on what they are paid. Discrepancies can be justified if they result from a decision to pay recruits according to their market worth where this reflects higher levels of competence and experience. The problem would not exist in an ideal situation when internal rates keep pace with market rates. But in the real world this frequently does not happen,
either because the organization cannot afford it or because it is unaware that its pay levels are lagging behind market rates.

The only way to respond to reasonable complaints from employees that newcomers are being paid more than they are is to state, honestly and openly, that the organization needs these people, which were only available from outside and could not be attracted for less. An undertaking could be made that the problem will be addressed in future pay reviews in line with the company's policy to do its best to maintain a balance between the demands for internal equity and external competitiveness.

This answer may not satisfy anyone, but it is the only possible one to give if the company has to recruit at a higher rate and if it cannot afford to bring everyone into line with the new rates immediately.

Employees who are very dissatisfied may threaten to leave if they do not get an immediate increase to restore the balance. This process of 'putting a pistol at an employer's head' can, of course, happen at any time when employees feel that they have a strong case (e.g. when they have received a firm offer from another employer – people sometimes test the market by applying for jobs) or when they are just trying it on, possibly on the strength of one or two job advertisements.

The theoretical answer to this sort of approach is to reject it on the grounds that the organization is not going to respond to blackmail – 'if once you start doing this you'll never be able to stop'. Some organizations insist on a policy of refusing to bow to such demands, which is easier when the person concerned is not vital to the business and substitutes can easily be obtained. The decision may be much tougher in the case of someone who is crucial to the organization and cannot be readily replaced, and in exceptional circumstances businesses have been known,
reluctantly, to abandon their policy line. Organizations without a clear policy on this issue have to decide on the merits of the case, but this is one decision which should not be left entirely in the hands of line managers. They should be required to seek approval for any action they take from higher authority and/or the HR department. Sometimes, in our experience, it is an issue which requires decision at board level, especially for senior or significant contributor posts.

2.0 How can one be satisfied that the market rate data that he is getting is valid and reliable?

Ans. The validity and reliability of market rate data depends mainly on three factors:

I. The sample frame – the data collected should be fully representative of the organizations with which comparisons need to be made.

II. Job role matching – the extent to which good job matching has taken place, so that it can be said with some confidence that like is being compared with like.

III. Timing – the degree to which the information is up to date or can be updated reliably.

But it is most unlikely that a perfect sample, precise job matching and the complete coincidence of timing will always be achieved. This is why it is usually advisable to obtain data from more than one source. It also underlines the point that, ultimately, a judgement has to be made about the level of pay in the market-place which should be used as the reference point for decisions on rates of pay within the organization.
3.0 What are the implications for reward management of the ‘flexible firm’?

Ans. The two main characteristics of the flexible firm are role flexibility and the ‘core/periphery’ approach to resourcing the organization.

Role flexibility arises because, in a constantly changing business environment, jobs also change. People have to expand their roles by taking on new responsibilities and roles can develop in line with capability of the person carrying them out. In other words, both roles and the people in them grow. To keep pace with change and the varied demands made on people individually or in teams, workers have to become multi-skilled. Flexible roles require flexible pay processes. Traditional grade structures, which constrain people into narrowly defined jobs, and job evaluation and pay schemes which result in people being rewarded for non-adaptive behavior, are no longer appropriate.

The focus has increasingly to be on competence and skill development and rewards for growing roles (lateral growth) and flexibility. Both for individual roles in broad-banded structures and job families, templates and role profiles can be produced jointly with employees, which help to clarify expectations of what is required while not constraining flexibility when it is needed.

Core/periphery structures retain a relatively small core of key workers on continuous and long term contracts in the core, while relying on a peripheral work-force of part timers and temporary or contract workers to enable the firm to adapt rapidly to increases or decreases in activity levels. Special care has to be taken over the reward packages and development of the key core workers. But tension may be created if the differences between the way in which core and peripheral workers are treated become too large. Peripheral workers are an important part of the firm and
should not be neglected or taken for granted. As far as possible, values and practices should be shared with the core.

4.0 How can we motivate the bulk of our employees on whose efforts we depend when there is not much money available in the pay-for-performance kitty?

Ans. Much of the thinking that went into the performance-related pay schemes of the 1980s centered on rewarding ‘key players’ and ensuring that high performance produced significant rewards.

In some organizations the overall results achieved depend crucially on the effective performance of a small number of people, who are directing the enterprise or who are responsible for innovation, marketing and sales. In such cases, it makes business sense to reward these people highly and put a large proportion of pay at risk. Most organizations, however, depend on the efficient performance of employees at all levels. In these circumstances, a pay system that siphons off resources to a few ‘star’ performers would be at best irrelevant and at worst counter-productive in motivating the ‘engine room’ of the organization.

But when performance pay budgets are tight, the range of performance awards on offer is limited. A few high performers may get one-off bonuses of 10 percent or so. However, the majority of employees have recently been getting overall increases in pay covering both individual performance pay and across-the-board awards of 3 to 5 percent. This is in line with the general movement in earnings or what they would expect in any case.

A performance-related increase of, in effect, 1 or 2 percent is not going to provide much of an incentive at all. PRP in these circumstances will not directly motivate. But this does not destroy the validity of the concept that people should be valued according to their contribution.
The good, reliable ‘core’ performers should be rewarded according to their market worth and this should increase as they gain experience. Even if they cannot be given large performance-related increases, they should at least be eligible for an achievement bonus if they make a special contribution or for a special sustained performance bonus if they consistently deliver a fully competent level of performance. There may be scope for including them in team bonus schemes and there is certainly much merit in their participating in organization-wide gain-sharing, profit sharing or profit-related pay schemes.

5.0 Performance-related pay has had a bad press over the last few years. Why is this so?

Ans. The concept of performance-related pay (PRP) suffered from over-marketing and crude approaches in the 1980s. That was the decade in which most private sector organizations got rid of their expensive fixed incremental pay systems and, under the influence of the entrepreneurial / finance / economic / transactional ethos of the time, believed that PRP could be a major lever for culture change as well as a powerful motivator. The government of the day joined in and fervently believed in the miracle-working powers of PRP as a means of converting its own departments / agencies etc in to commercial enterprises overnight.

Performance-related pay was viewed as an instrument for producing high levels of individual and organizational performance. This asks too much and there has been no evidence that PRP is guaranteed to deliver this result. Research has also shown that PRP can demotivate people if it is managed badly and, consequently, is felt to be unfair. Vicky Wright has pointed out that: ‘Even the most ardent supporters of performance-related pay recognize that it is extraordinarily difficult to manage well … it is a part of managing people which requires constant attention and improvement.’
In spite of the perceived problems of managing PRP effectively, most still believe that it is right to reward employees according to their contribution and competence and that, directly or indirectly, this will motivate them to improve their performance and develop their competences. But some are seeking alternatives to the crude model of output-based schemes for individuals and many are reconsidering how they measure contribution and competence. Alternative approaches are summarized below:

- Competence-related pay – This may be attractive because it addresses the key issues of increasing levels of competence and furthering continuous development policies. It is also forward-looking. Individuals can be fully involved in developing competence profiles and assessing their levels of competence against these profiles. However, competence-related pay can be just as difficult to operate effectively as PRP – possibly even more difficult. And the extent to which it does improve competence levels and therefore performance is as yet unproved.
- Team-based pay – this can be easier to run and fairer than conventional PRP but it is not universally applicable.
- Spot rates – These are fixed rates for jobs which do not vary with performance but may be adjusted to reflect increases in market rates. They are used by some organizations for shop-floor or unskilled workers, but they are not often applied elsewhere. Flexibility may be achieved by ad hoc increases to ensure that individuals are paid competitively or by more formal competence-related pay progression up to the rate for the job. There may be scope for variable pay, in the shape of lump sum achievement or sustained high performance bonuses.
Performance management – Performance management processes can and increasingly do include the assessment of competence (inputs) as well as the achievement of objectives (outputs).

6.0 Is competence-related pay no more than a ‘flavour of the month’?

Ans Interest in competence-related pay was generated by writers such as Ed Lawler, who advocated people-based as distinct from job-based pay – paying people according to their value in the market and in relation to their knowledge, skills and competence. Interest was also created by the drive for organizational and role flexibility resulting in moves from narrowly defined jobs and job standards to broader generic roles, where the importance of competence development and continuous improvement is fully recognized. Other factors have been dissatisfaction with conventional performance-related pay and a belief that, having established competence frameworks and profiles for recruiting and developmental purposes, it is logical to extend this to reward, thus providing an integrated approach to human resource management.

There are good reasons for competence-related pay remaining in one form or another as a permanent feature in the reward management scene. But organizations are still experimenting with it and most of those with competence-related pay recognize that they have not yet found the perfect approach. Much has still to be learnt about how it should be developed and operated. Pure competence-related pay in its present unproved state may still be something of a fad, but many organizations are now developing hybrid approaches to job evaluation and performance management in which competence-related factors and assessments are used in conjunction with more traditional evaluation factors and performance criteria.
7.0 Is there a risk that competence-related pay will mean that businesses are likely to pay out for competences that people do not use?
Ans This potential problem exists for both skill-based and competence-related pay. The answer is to plan the scheme on the basis that skills or competences will only be paid for if they are used effectively. In the case of competence-related pay, this means that people are not rewarded just for behaving in ways in line with their competence profiles. Rewards are paid out only when it can be demonstrated that their behavior has delivered the expected results or that they are developing their competences as they proceed along a learning curve to reach a fully defined competence level for their role.

8.0 Why should we move to variable pay?
Ans Variable pay is pay that varies with performance. It is ‘at risk’ pay, in the sense that people may receive a lump sum bonus one year but risk not getting it next year if their performance or that of their team or organization does not justify it. The argument for variable pay is that, because it is not consolidated into base pay, people will not go on receiving the benefit of a previous increase which is not justified by their present performance. In addition, awards can be more focused on specific attainments and can be made at any time as a spot bonus to recognize a major achievement. The acceptability of variable pay depends on a number of factors, including a reasonable level of base pay, shared values regarding risk, and clarity on the relationship between risk and reward.

9.0 How can we introduce a more flexible and performance or competence-related pay scheme to replace our present fixed incremental system?
Ans The decision to move to performance or competence-related pay is often made as part of a cultural change programme – moving from an environment in which people are rewarded just for being there and carrying out the same old job in which they have to earn their increases.
Another reason is simply to save money. In an organization with low staff turnover there is nothing to stop staff moving inexorably to the top of the scale, with the likelihood that a proportion of them will be paid more than they are worth.

The first thing to recognize is the need to think very hard about how the change is to be managed. Clearly, a proposal to abolish a deeply embedded fixed incremental system will be resisted by any people who think they are going to lose by it or who believe that to adjust pay on the basis of managerial judgement is likely to be intrinsically unfair. Trade unions are often vociferously against performance-related pay.

This means paying attention to the following guidelines on change management:

- ‘People support what they help to create’ – commitment to change, or at least its acceptance, is improved if those affected by change participate in planning and implementing it.
- Hard evidence and data on the need of change are the most powerful tools for its achievement (e.g. attitude survey findings)
- Identify people who can act as champions of change.
- Remember that resistance to change is inevitable if the individuals concerned feel that they are going to be worse off. Therefore take steps to remove or at least diminish those fears by explaining how the change will work and how it will affect them.

Tinkering with a pay spine by allowing extra increments to be earned on the basis of ratings produced by an existing performance appraisal scheme is generally doomed to failure. It could be adopted as a transitional policy but this needs to be explicit. PRP will only work and will only be acceptable if it is based on a fully developed performance
management process. And it is essential to provide training in face-to-face briefing for all concerned in how the process works and the part they play. Reliance should not be placed on written material alone.

It is also necessary to monitor the introduction of PRP carefully to ensure that it is operating fairly. Attitude surveys and focus groups can be used to obtain reactions from managers and other employees and action taken to deal with any weaknesses these identify.

10.0 To what extent, if at all, should we provide rewards for individual performance or competence to those taking part in a team-based pay scheme?

Ans A few team-based pay purists assert that the whole ethos underpinning team pay will be destroyed if there is any variation in the rewards paid to individual members of the team. But team pay enthusiasts are more likely to concede that team bonuses should be a percentage of the basic pay of team members which, they assume, will reflect the value of the individual to the team.

Others point out that the difficulties of managing the performance of individuals within a team cannot be ignored. Vicky Wright and Liz Brading comment that:

*Leaving team dynamics to manage performance by such things as team pressure can be dangerous and unfair. Managing team performance is important, but it is not a substitute for managing individual performance.*

This suggest that there might be a case for providing individual rewards to team members, but how can this be done in a cohesive work team in which there is a high degree of interdependence amongst team members? Would it not be invidious to single out individuals?
An answer to this dilemma can be provided by the use of competence-related pay. This is necessarily always oriented to individuals and it is reasonable to assume that as competence increases (including competence as a team worker) the contribution of the individual to team results will increase correspondingly.