Reward Strategy:
Comparing Performance-related Pay and Team-based Pay

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ABSTRACT

Rewards are exclusive extrinsic motivators. It is often questioned that whether effective strategy should focus either on individual performance or team performance. The paper will address this dilemma for suggesting an effective reward strategy.

The basic concept of Human Resource Management in the mid-1980s led to the recognition that the workforce was one of the most important instruments to achieve competitive advantage and how they were recruited, trained, challenged and involved became critical components in ultimate organizational success. In each of these components, reward issues play a major role to produce a well-oiled high-performance people machine, focused on organizational objectives (Stredwick, 2000). Depending upon the organizational objectives, top-level managers need to formulate their reward strategies and align them with the organization's overall strategies. Organizations' aims are to be ranked among the leaders in providing excellent customer service and in contention to be listed in best companies to work for, certainly should have a contemporary and effective reward strategy to attract best people of the market and should be able to maximize the potentiality of their workforce. This paper will focus on different reward strategies and a comparison between performance-based pay and team-based pay.

Armstrong and Murlis (2007) state, reward management is concerned with the formulation of and implementation of strategies and policies that aim to reward people fairly, equitably and consistently in accordance with their value to the organization. They suggest, in order to achieve these aims reward management should focus on long term issues strategically and relate to the values of people of what they do and what they ahcieve. According to Taylor's scientific management concepts, people are primarily motivated by economic gain and therefore, the prospect of more pay is sufficient to bring about an increase in the desired behaviour (Wright, 2004). However, the pricipal-agent theory assumes that employers want high levels of effort relative to pay from employees, while employees want the reverse (Wright, 2004). At the same time, the employees are less informed than the employers about the employers' action.

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However, Milkovich and Newman (1996) request the modern organizations to be more open about pay in order to gain greater satisfaction with their pay and the system to determine with (cited in Wright, 2004, p. 9). Nevertheless, rewards and incentives are the loudest and clearest ways leader of an organization can send message about what they consider important (Cacloppe, 1999).

According to classical agency theory, when the interests of the employees and the organization are misaligned, employers try to design their reward strategies in such a way that encourages employees to act in their employers' best interests (McCausland *et al*, 2005). Mirlees (1976) and Holmstrom (1979) were among the first to demonstrate the theoretical dominance of performance-related pay (PRP) over alternative reward systems when monitoring effort is costly and imperfect (cited in McCausland *et al*, 2005, p. 637). Barth *et al*. (2008) also argue, when it is costly or impossible to directly observe effort and sort out the influence of the stochastic factor, the firm may benefit from implementing an incentive pay shceme in order to motivate workers to supply effort. Heery and Noon (2001) state, performance related pay can be defined in two ways (cited in Perkins and White, 2008, p. 162). First, it can depict the broad class of payment systems which relate pay to some measure of work performance. As such, it can embrace profit sharing, merit pay, gainsharing, piecework, sales incentives and other output-based pay systems. Second, it can refer to individualized systems in which salary increases are related to the results of performance appraisal. This latter usage corresponds to appraisal-related or merit pay (Perkins and White, 2008).

Both expectency theory and equity theory could be potentially applied to the practice of performance pay (Wright, 2004). According to the expectancy theory, introduction of PRP could be worthy if employees believe that they are able to achieve the set objectives and managers will recognise and reward good performance. However, Wright (2004) argues, lack of tranparency, problems in measuring outcomes or setting objectives and/or isolated incidences of favouritism in application of the process could be enough to undermine the whole process provided that expectency theory were to work in practice. On the other hand, equity theory depicts that employees evaluate their reward in relation to their input with others and consider they are equitably rewarded, relatively under-rewarded or over-rewarded (Wright, 2004). Wright (2004) also suggests, two people with same pay outcome in an organization may consider fairness in a different way, because they are comparing their experience with different people. As a result, performance related pay may generate confusion and fraustration if the process is not properly designed and implemented.

Wright (2004) claims, it is difficult to interpret the evidence on association between high corporate performance and the existence of performance pay. Pearce (1987) argues, individually contingent pay is based on the false assumption that market-type contracts are appropriate to the social contract between employer and employee (cited in Perkins and White, 2008, p. 165). He also asserts, most kinds of organizations succeed because of co-operation among their members, not because of members' discrete, independent performance. While criticizing performance related pay, Pfeffer (1998) argues, its nature is unclear and the practice of individual PRP is an expensive, time-consuming activity in many organizations (cited in Wright, 2004, p. 118). He also believes, it undermines teamwork, encourages a short-term focus, and leads people to believe that pay is not related to performance at all but to having the 'right' relationships and an ingratiating personality. According to Armstrong and Murlis (2007), the extent to which contingent pay schemes like PRP motivates is questionable since money may possibly motivate those who receive it but it can demotivate those who don't. They also believe, the numbers who are demotivated could be much higher than those who are motivated.

From the above discussion, it is quite perceptible that different drawbacks of individual performance related pay tends create an imbalanced reward strategy. Organiazations must modify their reward strategy to overcome these drawbacks and should redesign their pay policies which will promote their overall busienss objectives. At the same time, their reward strategy should not ignore the importance of individual contribution and should introduce a reward strategy which will emphasise both individual and team performance. Keeping the performance related pay in mind, this paper proposes the team based pay scheme where the employees will be rewarded on the basis of their team performance. The following sections will point out the design of team based reward strategy and implementation plan in details.

CONCEPT OF TEAM

In order to develop a team reward strategy, it is necessary to understand the concept of team. Katzenbach and Smith define team as, 'a small number of people with complementary skills who are committed to a common purpose, performance goals and approach for which they hold themselves mutually accountable' (cited in Armstrong and Murlis, 2007, p. 368). Zobal (1998) states, team members are linked by what they do, how they do it, and the results of their efforts.

TYPE OF TEAMS

Teams are classified by the type of work that they do and how that work is accomplished (Zobal, 1998). Perkins and White (2008) assert, team reward

strategy is formulated depending upon the form of team working adopted by organizations. Both Zobal (1998) and Perkins and White (2008) identify three types of common team:

Parallel or Problem solving teams: employees participate part-time on team activities in addition to normal work assignments (such as quality circle).

Project or Time based teams: full time team members committed to completing a project within a given timescales and in which membership may vary over time.

Process or Work teams: employees are permanently committed to the team and actively participate in an entire work process. Such teams tend to involve multi-skilling, with each member of the team trained to perform the full range of tasks within the team.

This paper propose to adopt the Process type team formation for Top Travel. Being a service-based company, Top Travel will be focusing on developing multi-skilled employees. The teams will be highly interdependent, both on members of the team and other similar teams and semi-autonomous teams. All the teams will be operated under strong external supervision of line managers. Initially, successful practices of Italy team will be followed and line managers from that team along with other UK managers will supervise the pilot project to achieve greater success.

MEASUREMENT OF TEAM PERFORMANCES

The team members along with line managers will develop a competency framework which will include factors that influence process and behaviour outcomes and they should be aligned with organizational objectives. Factors like communication, decision making and problem solving, leadership and teamwork ability, accountability could be considered initially. But the team members will come out with the factors so that they can easily understand the measures are used to evaluate their perfromances.

Distribution of Rewards:

The motive to introduce new reward strategy is to emphasize on teamwork so the individuals' contributions to foster team performance need to be valued carefully. At the same time, pay equity and motivation to work as a team member need to be valued. The top-level managers must ensure that all the employees will be valued equally for their contribution and they will be paid at a higher rate than the market rate to motivate them to adopt the new strategy and perform better in a team.

There will be three types of reward categories used in this pilot project which is adopted from the Zobal's (1998) research paper about team compensation system.

1. Base pay and base pay adjustments: The employees will be primarily compensated by base pay and it will be calculated through market pricing, job evaluation and market comparison along with competencies acquired by employees. The base pay will be adjusted over time when the employees acquire higher level of knowledge and skills, increase merits and changes cost of living. The base pay will be paid monthly.

2. Other financial rewards: The team members will be given other financial rewards on the accomplishment of pre-determined goals. Each member of the team will receive same cash sum through a collective short term reward strategy. The gainsharing approach will be used to provide bonuses or incentives. Among the different traditional gain-sharing plans, Improshare will be used and the employees will be paid quarterly. There will be some established standard which will define the expected hours needed to produce an acceptable level of output, based on work-measurement techniques. Any savings from the achievement of greater output in fewer hours will be shared between team members as well.

3. Non-financial Rewards: There will be a dinner party arranged in every quarter to celebrate teams' success. Team members will nominate one employee as employee of the period from each team. Other than that all the present facilities will be provided as well.

IMPLEMENTATION TIME SCALE

Since the all orgainzations' target is to be ranked at the top, the new proposal should be implemented as early as possible so that any modification could be done immediately. At the same time, the employees will be given sufficient time to cope up with new system. The competency framework and other strategies will be formulated first and the employees will start working in a group and follow the policies in the following three months. Finally, the pilot project will be implemented and continous modification will take place considering the outcomes.

JUSTIFICATIONS OF THE PILOT PROJECT

The reason behind the shift from individual PRP to team based pay is to ensure the desired optimal performance of employees. According to Gross (1995) and Johnson (1993), recent surveys show that the top reasons to implement team based pay were to

improve customer satisfaction, productivity and product and service quality but the main reason that teams have become so popular is due to their impressive track record (cited in Zobal, 1998, p. 237). Armstrong and Murlis (2007) also argue, the reason for developing team rewards is the percieved need to encourage group endeavour and cooperation, rather than concentrate only on individual performance. Cacloppe (1999) believes, in order to respond to the technological, competition and customer requirements, organizations are shifting to the team based pay and using empowered front line staff who function on teams is the best way to provide rapid response to changes in customer needs as they occur. Organizations like Federal Express, reduced service problems, such as incorrect billing and lost packages, by 13 percent as a result of moving to teams, Proctor and Gamble reported 30-40 percent increases in productivity due to their team-based plants and companies like Motorola, AT&T and Xerox also reported success for introducing team based pay (Zobal, 1998). However, despite the sceptcism voiced by some academics, a quarter of UK employers now recognize teamworking in their pay systems and another 17 percent are actively planninng its introduction (Brown, 1996).

The reason behind introducing basic pay is to attract and retain the top performers considering long term perspective. If basic salaries are set competitively, there will be less temptation to 'fudge' the incentive payments in lean years because employees will become more dependent than they should on 'risk or vaiable' payments (Armstrong and Murlis, 2007). The concept of dividing other financial rewards in team level rather than individual level is to promote the pay equality in teams. On the other hand, the choice of gain sharing is crucial and adequate since the research evidence on the effects of gain sharing is quite positive (as Sheild 2007 cited in Perkins and White, 2008, p. 221). The advantages of gain sharing are that rewards are closely related to monetary gains that employees can directly influence and it also improves employee commitment and reduce supervision needs (Perkins and White, 2008). Apart from these non-fnancial rewards will foster the desired behaviour and motivate to accomplish a particular goal (Zobal, 1998).

Finally, this paper propose a shift from individual PRP to team based pay strategy through a pilot project. However, it is quite difficult to recommend a single strategy which will work like a panacea for all reward problems. Customization could be the best way to make the reward system effective by aligning it with organizational structure, business strategy, perofrmance management system. Last but not the least, the success of any reward strategy vastly depends on the success of the implementation of that strategy.

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