

Incentive Based Pay

A fair, transparent and well-structured incentive scheme can be a strong staff motivation and retention tool and also a great tool for improving business performance. However, you need to take care that the scheme is structured to get the results you want. Employers sometimes find themselves paying out hefty bonuses, while not being totally satisfied with the performance of their staff.

The key steps in creating an effective incentive scheme are:

1. Analyse the objectives of the scheme.
2. Link incentive payments to performance.
3. Anticipate problems.
4. Establish measurable targets.
5. Determine the amount of the incentive.
6. Communicate effectively.
7. Review the incentive scheme periodically.

Analyse the Objectives of the Scheme

The first step is to think about what you're trying to achieve with the incentive scheme and ensure that a financial incentive is the most effective way of getting the result you're looking for. You then need to consider whether your objectives can best be met by providing rewards based on individual, team or company-wide performance. Your incentive scheme may need to include more than one of these options.

Link Incentive Payments to Performance

An incentive scheme should be operated in conjunction with a performance appraisal system that measures the employee's overall performance. (Click [here](#) for more information about performance appraisals). Ensure that your people are not focussing their efforts solely on achieving the targets that will earn them an incentive payment and ignoring other aspects of their performance.

Anticipate Problems

It's important to try and anticipate unforeseen outcomes of an incentive scheme. For example, if your incentive is based just on sales, will customer service levels drop?

Establish Measurable Targets

Performance-driven incentive schemes work best when goals are linked to the company's business plan and everyone knows where the company is heading and how it's going to get there. Consulting employees when setting the goals will ensure greater buy-in to the process.

Focussing on a few, simple, objective measures will produce the best results. Some examples are:

- Sales
- Profit
- Expenses
- Productivity
- Customer satisfaction

Each measure should be quantifiable and supported by robust monitoring systems. Targets should strike the right balance between being challenging and achievable and individual targets should be within the control of the employee.

Determine the Amount of the Incentive

To motivate employees, an incentive scheme must be externally competitive and the reward large enough to be valid. It's important to carry out market research on salaries and ensure that the total remuneration, including incentive, is in line with market rates.

Ensure that you structure your incentive scheme so that it rewards the company as well as the employees. The scheme should be self-funding. The value added by the employees in achieving the goals set for the scheme must flow to the bottom line in the form of additional profits or lower costs for the company. The scheme should also protect the company against windfall payments.

Communicate Effectively

Effective incentive schemes require open and honest communication about the financial position of the business. You should ensure that people clearly understand the company's position at the starting point of the scheme, the objectives of the scheme and what they need to do earn the incentive payment. Regular updates on progress (at least monthly) will keep people motivated and focussed on achieving goals.

Review the Incentive Scheme Periodically

An annual review of an incentive scheme is important to ensure that it keeps delivering the outcomes you wanted when it was first established.