

Practical Steps to Designing an Effective Bonus

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■ Introduction

Many people believe that the implementation of a bonus will be all that is needed to motivate employees to achieve the Company's goals. This is certainly not the case. Bonuses are only a small part of an overall management strategy, carefully put together to train and motivate employees to excel.

Managers must spend time deciding what their overall compensation package should be and whether adding a bonus will encourage employees to strive to achieve company objectives. There are many successful companies that have no bonus structure at all, and others that rely very heavily on bonuses to reward good performance.

Three important things to remember about bonuses:

- A bonus is a reward for achievement, not necessarily a motivational tool.
- You can be sure that the employees will strive to achieve the targets set out in the bonus, so it is essential that those targets reflect what it is that drives company profitability and achieves company goals.
- A poorly designed bonus can be a real "de-motivator" for staff.

Once the decision has been made to implement a bonus scheme, it is worth spending time designing a bonus structure that will successfully motivate employees.

■ Designing the Bonus

The following is one idea for designing a successful bonus for your Company.

There are three basic steps:

- Creating the bonus structure.
- Implementing the bonus
- Review procedures.

The first and maybe the most important step, is to perform a careful assessment of what it is that drives the profitability in your company and identify the company's goals.

For instance, a feeder pig production company might find that the biggest influence on profitability is the quantity of number 1 feeder pigs sold; whereas a company producing slaughter pigs may well find that feed cost per pig is the most important factor in driving profitability.

Costs and revenue influences need to be broken down and weighted according to their importance. This way a manager or owner can clearly see the key areas that need to be focused on to achieve goals

It is then important to decide which areas the different levels of employees can influence. It is no good setting up a bonus structure with goals that employees have no control over.

Managers have a great influence on profitability if they have purchasing authority. Employees in the farrowing department may not have influence in the same areas, but can certainly have an impact on the number of pigs produced. Therefore it is not necessarily correct to have a blanket bonus that is the same for everyone.

Bonuses based on profitability require a lot of time spent on assessing return on invested capital. A common mistake is to not include all costs when assessing profitability. Remember that interest, depreciation and other hidden costs have to come out after bonuses are paid. It is also good to remember that as profits increase, static bonus levels are a diminishing percentage of profits.

Some bonuses are based solely on sales. The plus side to this is that it is simple, easy to explain and the employees can watch the progress through the period and know where they stand at all times. There is no chance for the employees to feel they have been "stitched-up" by management with some financial sleight of hand. (As my dear brother puts it!)

The Company's ethics and beliefs need to be assessed. Companies with a "profit at any cost" attitude do not tend to last for very long. There needs to be a careful balance in the bonus so that employees do not circumvent company policy for the sake of a few dollars.

Once all this analysis has been done, it is important to enlist the help of key staff members in designing the bonus program. You will be surprised at how useful they will be. In addition, if they have been involved in the design of the bonus, they are much more likely to buy in to it and be excited about achieving its goals.

Of course, the amount or percentage of bonus for different levels needs to be decided on. There are many options here. Does it make sense to have one lump sum that is then divided amongst employees according to their input and level of responsibility? Or do you simply decide on a percentage of salary for each eligible employee.

You will also need to decide what qualifies an employee to go onto the bonus program. Is it length of service? Amount of responsibility?

Make sure that the levels of bonus are high enough to be motivational. Giving a staff member \$5 for achievements during an entire quarter is not likely to be too well received.

Also remember that bonuses do not always have to be financial. Gift certificates and leisure items, such as TV's and dinners, are also very useful tools for motivating employees.

It is necessary to also decide how much time you are willing to devote to calculating bonuses. Remember, the more complicated the bonus, and the more parts there are making up the bonus, the more time it will take each time you calculate it. There is certainly something to be said for simplicity; you will want to be in a position to show the calculations to employees and management and they all need to understand it. Ideally the bonus will be based on information the employees are already receiving so that they will already be familiar with the reports.

The last step once a bonus structure has been decided on is to trouble-shoot possible pitfalls. Some questions to ask are:

What are the maximum and minimum costs of the bonus program?

What potential changes in company policy will affect the bonus? E.g. changes in slaughter weights.

When targets are achieved, what mechanism is there for changing the targets and how will that be received?

■ Implementation

People will only fully trust a bonus program if they have access to all the information used in its calculation. It is also essential that the bonus be paid as close to the end of the bonus period as possible. As with any reward for good work, the positive effect diminishes the longer you wait to present it.

Management should be prepared to hold regular meetings with employees to go through production numbers so that they have an ongoing understanding of whether they are achieving targets.

With profit bonuses, managers will need to be shown accounts so that they can see what areas they need to focus on in order to impact the bottom line.

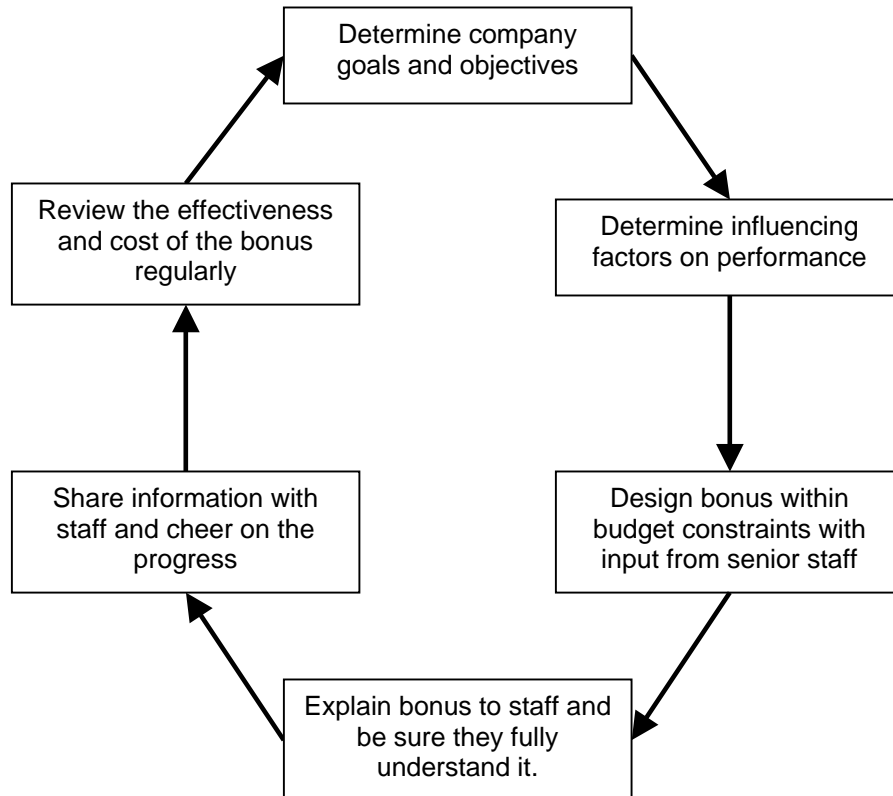
Once staff have access to information and understand the numbers, they will generally be pretty eager to make suggestions on how to go about impacting the performance. Be prepared to listen to their suggestions and consider them carefully.

Make sure each staff member understands why his or her job is important in the overall scheme. A person power washing might not be able to make the connection between what he or she is doing and its impact on performance and profitability. This needs to be constantly reinforced to all employees.

Cheer on the progress. Employees are much more likely to respond to positive feedback than negative. Results should be posted in the unit for all to see. Employees will be motivated to achieve targets if they can see the impact of their efforts and are receiving encouragement along the way. This is toughest to do when markets are down and the company is losing money. When the market finally turns into profit, you want to be in a position to take advantage of it. This can only be done if the foundation has been set at least a year ahead of time.

Allow staff access to learning and training. They will improve their performance if they are given the opportunity to learn new techniques and ideas. It is difficult for someone to move forward without fresh knowledge. Subscribe to industry magazines for the unit. You will be surprised how many staff will read it if it is on the coffee table during breaks.

Allow staff interaction with professionals in the industry. A manager or owner does not have all the answers, even if he or she thinks they do!



■ Review process

There needs to be a regular review process for assessing the effectiveness of the bonus.

Again, it is essential to have the managers in on this process.

Sit down at the end of the year and consider all the factors surrounding the bonus:

- Has the bonus been well received by staff?
- Has the bonus been effective in motivating recipients and focusing staff on targets?
- Are the areas identified in the bonus correct and are they still applicable?

- How much did the bonus cost and did it pay for itself with improved performance?
- How effective a recruiting tool has it proven to be?

■ **Conclusion**

In conclusion, the process of designing and implementing a bonus structure is circular. If enough time is spent designing the structure of the bonus and making sure staff buy into it, it will help to motivate staff to achieve goals.