

BUSTED: IF YOU PAY PEANUTS...

Remuneration schemes have no bearing on motivating executives or improving their performance, says **HARRY ONSMAN**, so why does the practice continue?

PAYING FOR performance is a tough issue for most managers. While some have the luxury of leaving the matter in the hands of the HR function, this still leaves them to cope with the consequences, which seems to be an almost universal dislike of whatever system is put in place.

The element of performance pay that has drawn most public and research attention recently is executive reward schemes. And the research suggests a sharp divergence between what is believed to be the impact of and reason for performance pay, and the corporate reality.

Executive remuneration schemes took off in the 1990s like a management mania unshackled. Most schemes focus on share options, profit-sharing or gain-sharing. The main driver for this sudden growth seems to be the idea of linking executive performance to organisational performance. Perhaps because of widespread publicity in the media, a herd mentality has driven many organisations to adopt the practice, often without a lot of thought as to its efficacy.



Academics soon became interested in the phenomenon and most early research focused on establishing a link between levels of executive pay, including the at-risk portions, and organisational performance. It is hardly news that the link has never been established. Whatever may be the drivers of high performance in organisations, high executive pay is not one of them.

The next link investigated was that between executive incentives and executive motivation. Those who craft and authorise performance pay systems generally seem to believe that contingent pay for executives motivates them to perform. In fact, most recent research

points in the opposite direction, suggesting that performance pay has a negligible impact on executive motivation.

So, performance pay neither motivates executives nor is linked to organisational performance. Which begs the question as to why executive incentive systems continue to be offered. The answer seems to be that they are effective in attracting and retaining executive talent. Even in surveys of executive opinion about performance pay systems where participants openly indicate that such schemes do little to motivate them, those same executives admit that they take such schemes into consideration in making career choices.

Which may also connect to another well-established link between level of executive performance pay and the pay ratios between the top of the organisation and the bottom. Executives who have a higher proportion of their pay at risk also earn many times more than those at lower echelons in their organisation. The disparity is much less in organisations that do not have executive incentive schemes.

There is some suggestion in the research that from a global perspective those national cultures that emphasise “reward for achievement” (e.g., the US and Australia) are more naturally inclined to offer incentives than those

cultures that emphasise other values (e.g., many European and Asian countries). Those who are familiar with efforts to introduce performance pay schemes in southern European cultures will no doubt concur with the research.

Of course, one outcome of the reality that incentive schemes do attract and retain executive talent is that the adoption of pay for performance by a few players in the executive talent market is likely to lead to others having to follow suit.

Regardless of whether such schemes are effective or not in driving organisational achievement or individual behaviour (and it seems clear now that they are not), the competitive nature of the executive job market will continue to drive their growth.

And so organisations are caught in a trap. Pay for performance will not improve executive or organisational performance, but not having such a scheme may mean that the organisation fails to attract the talent that it needs.

In the words of the philosopher Kurt Vonnegut, and so it goes.

Reference: M. Beer and N. Katz (2003), “Do Incentives Work? The perceptions of a worldwide sample of senior executives”, Human Resource Planning, vol. 26, no. 3, pp 30-44.

“UP AND AT THE OFFICE ALL THE MORNING; AND SO TO IT AGAIN AFTER DINNER AND THERE BUSY LATE, CHOOSING TO EMPLOY MYSELF RATHER THAN GO HOME TO TROUBLE WITH MY WIFE.”

Samuel Pepys, Diary, November 7, 1668.