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Reward Performance, Not Attendance

By Frank A. Cania

I recently had a conversation with a friend of mine, who owns a business with approximately 50 employees. The conversation went something like this:

“How does your organization reward good performance?”

“With merit increases.”

“Fantastic! How do you determine who gets a raise and who doesn’t?”

“Well, for the last few years everyone has gotten a three percent raise at the beginning of the fiscal year.”

“Great. You give a cost of living increase to everyone, but what about performance-based increases?”

“Those are our merit raises.”

Is this how your organization handles “merit increases?” By definition, a merit increase means an employee receives a pay increase based on “merit!” However, in many organizations employees receive increases regardless of how stellar or poor their performance in the previous year. In fact, I’ve seen cases where the poorest performers in an organization receive “merit” increases year after year for just showing up. Giving pay increases to all employees, regardless of performance, sends the wrong message—both to poor performers who are rewarded for little or no measurable achievement and to exceptional performers who receive a smaller piece of the available pie. At the very least, this can have a negative impact on employee morale and at worst lead to legal repercussions.

The culture of many companies is to spread limited reward dollars around to all employees in order to avoid the conflicts that may otherwise arise from poor performers who were passed over. Some organizations even go as far as saying it would be unfair to employees who aren’t able to reach their full potential due to factors beyond their control.

By contrast, organizations that have adopted a strict policy of rewarding only employees who have shown measurable achievement say it has clear advantages: it doesn’t waste precious payroll-budget dollars, it send the message that development is essential, and it doesn’t reward underachievers at the expense of top performers.

One of the worst scenarios can play out when it becomes obvious that a poor performer needs to be terminated. Let’s say Tim has worked for your company for several years and has not been a good performer for the last four years. However, every year he receives a merit raise. You’ve decided that you need greater production from Tim’s position and decide to terminate him based on his poor performance. The fact that Tim has received unwarranted raises creates concrete evidence of inconsistency between what you are saying now and what was communicated then. It also opens the door to suspicion of an ulterior motive for the adverse employment action—the termination.

“It’s difficult to defend your actions and say this person was a problem when there is a history of regular raises,” says Stephanie Caffera, a partner with the Rochester, NY law firm of Nixon Peabody, LLP. “Unfortunately, I see automatic raises given by supervisors all the time. They just don’t want to confront the performance issue until it’s too late.”

If withholding an increase from an employee who has shown some promise appears to be a harsh punishment, then consider delaying the raise. Often if you give an employee three to six months to work through performance issues, and provide some coaching and guidance, they will earn the reward.

Another approach is to offer lump-sum rewards rather than an increase in base pay. For example, give a single lump-sum payout of four percent rather than a four percent increase in base pay. It has the same appearance as a bonus and comes from the merit increase budget. However, it keeps the base pay the same and can help stretch the dollars allocated for financial rewards. This is especially useful over the long-term to slow down the growth rate of the base wages you're paying.

No matter what type of merit increase system you use, keep it simple. It is important to apply the rules consistently; make an honest assessment of who in your organization deserves to be rewarded and who doesn't; and document your reasons for giving—or not giving—rewards.

As the competition grows for your best performers, show them that their efforts and achievements really mean something. That doesn't always mean more money. It can simply mean only rewarding those who have truly contributed at the highest level.

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