

— A Manager's Guide to —
Improving Business Performance
— Through People —

The Reward Plan Advantage

JERRY L. McADAMS

Foreword by Jack Stack

Author of *THE GREAT GAME OF BUSINESS*

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Foreword

It's the last half of the last decade of the century, and by the numbers the United States economy is on fire. All the economic indicators would lead us to believe that we are headed for some of the best years of our lives.

Yet this is not the first time in my life that the economic outlook seemed so bright. Twice before the stage was set, but we blew it. How were we to know the reliance our economy had on oil and its relationships in the Middle East? We thought we were self-reliant. How were we to know that the Japanese would have a major impact on our marketplace and blast us into global competition?

How do we know now what today's rosy outlook will deliver? Granted, we've accumulated capital—and a lot of it. But do we really know how to keep it this time? Where will the other shoe fall? I'm afraid it will fall between labor and management. I'm afraid that we haven't learned our lessons from the past and that we haven't learned how to win with a lead—that we are a come-from-behind society. We have an incredible ability to pull together in a life raft, yet ignore each other on a luxury liner.

It seems as though every time the economy gets going, we can't figure out how to bring everyone along for the ride. It seems as though the only thing that stops us is the friction that the success creates. The very core of capitalism is that those who create wealth should get to keep it. However, whenever it comes time to share that wealth, there is an imbalance between the workers' rewards and the owners' rewards. After all, the story goes, it is the owners who take the risks. And *this* is our weakness. How do we make everyone feel like they can make a difference? How do we adequately reward everyone who has contributed to company success? How do we balance the risks and the rewards and keep our global edge?

Is there a middle-ground approach that will not only prevent the labor-management shoe from falling, but also will keep us from shooting ourselves in the foot? I believe so, and I believe Jerry McAdams comes about as close as anyone to presenting a clear path for achieving these goals in *The Reward Plan Advantage*.

No one has all the answers, but Jerry does show us how we can put in place incentives that reward people for initiative, hard work, and productivity while keeping us competitive in the global arena.

Jerry addresses “the middle,” that gap between the haves and have-nots, and makes a convincing argument that if everyone understands the economic situations of the business, a compensation system can be implemented that provides job security, variable pay, and a chance at the brass ring—equity. Jerry believes as I do that if we don’t address “the middle” we will be faced with turmoil and discontent, and we will ultimately lose the competitive edge we have today.

This book presents a structure that allows owners to be competitive in the market while rewarding all participants if they do better than the market expects. These ideas may just be scratching the surface, but wouldn’t it be exciting if everyone had a role in building our future? *The Reward Plan Advantage* shows us how.

Springfield, Missouri
February 1996

JACK STACK
President and CEO
Springfield Remanufacturing Company

Acknowledgments

It takes a year to write a book. It also takes a lot of help. The people who read every word and gave me their feedback based on their own years of experience made the project seem worthwhile. Jane Bjorndal McAdams, my partner, is an expert in compensation; she made sure that what I wrote was clear and correct. Roger Stotz and Nancy Ogden of Maritz Performance Improvement Company, Maritz Inc., critically focused on the recognition and group-based incentive portion of the book. Elizabeth Hawk of Sibson & Company and my co-director of the Consortium for Alternative Reward Strategies Research (CARS) gave me input with her usual thoroughness and thoughtfulness. Don Barry of Chase Manhattan Bank stretched my thinking and enhanced my sense of humor. May Eagle Seyle refined my scattered words into a logical and understandable format. I cannot thank these good friends enough for their support and expertise.

A number of other people lent their expertise to more specific areas of the book. Jamie Hale, Andy West, Ed Bancroft, and Rick Beal (all of Watson Wyatt Worldwide) shared their experience and perspective. So did Sherry Tucker of Towers Perrin; Bob Holben of Westinghouse Energy Systems Business Unit; Bob Pike of the Lord Corporation; Melinda Branchini of VHA, Dallas; Mike Higgins of BankOne, Dallas; Roy Baum, Mike Lockwood, Bob Mai, Jeff Sherk, and Mary Anne Walton, all of Maritz Inc.; Pat Rowell and Nina Rappaport of Chase Bankcard Systems, Chase Manhattan Bank; Walter Nord of Florida State University; Dick Beatty and Charles Fay of Rutgers University; Laura Popo of Washington University, St. Louis; Brian Riedy of Hewitt; and Stephen B. Knouse of Southern State University. The Jossey-Bass professionals made the process much more interesting through their expertise: Byron Schneider, Mary Douglas, Alice Rowan, and Mary O'Briant.

To those at Maritz Inc. who believed that I could make a contribution to the body of knowledge, a special thanks. Their support

of the CARS project and of my research was critical. In particular, William E. Maritz, Norm Schwesig, Dan Westrich, and Steve Maritz created an atmosphere that allows this kind of research to continue. Jeff Reinberg was instrumental in getting support for my work and provided unique and practical insight during the writing process. Phil Moses and Charlie Vogt regularly demonstrated how to use the language in an effective way.

The members of the CARS project, particularly the American Compensation Association, in addition to those already mentioned, contributed their time, money, and expertise to make the research possible.

We all owe a debt of gratitude to the leaders and reporters of open-book management: Jack Stack of SRC and author of *The Great Game of Business*, who was kind enough to write the foreword of this book, and John Case and Bo Burlington of *Inc.* magazine. They are spreading the word and deed of making people a competitive advantage.

Finally, my thanks go to Gina Breadon, my friend and associate at Maritz, who kept things in order and made my working life considerably more productive and pleasant.

St. Louis, Missouri
February 1996

JERRY MCADAMS

The Author

Since June of 1995, **Jerry McAdams** has been the national practice leader for Reward and Recognition Systems, Watson Wyatt Worldwide, an international consulting firm specializing in human resources, systems, and financial management. Prior to joining Watson Wyatt, McAdams was the vice president for performance improvement resources at Maritz Inc., in St. Louis. Before joining Maritz, McAdams held a variety of positions with General Electric, working in the United States and Europe. McAdams also served as a member of the Reward Systems Committee of the White House Conference on Productivity in 1984, and more recently, in November of 1994, he testified about organizational performance's link to rewards and possible tax code changes before the House of Representatives Committee of the U.S. Congress.

McAdams is also a founder and co-director of the nonprofit Consortium for Alternative Reward Strategies Research (CARS). He is a member of the certification faculty of the American Compensation Association (ACA) on alternative reward strategies, and for several years he has taught a "soup to nuts" course in Europe, Central and South America, and Australia on reward and recognition plans and improving customer service. McAdams has worked with AT&T, Rockwell Automation, Johnson & Johnson, Xerox, Chase Manhattan Bank, McDonald's, and health care institutions. He has directed the design and installation of all forms of reward systems for sales and marketing, manufacturing, health care, and service firms.

A leading thinker in the research, design, as well as the implementation of reward and recognition systems, McAdams is the co-author of *People, Performance and Pay* (1987, with Carla O'Dell), *Capitalizing on Human Assets* (1992, with Elizabeth Hawk) and *Organizational Performance and Rewards: 663 Experiences in Making the Link* (1994, with Elizabeth Hawk). In addition, he has col-

laborated with Robert Mai on *Learning Partnerships* (1995), a book about reward systems and the learning organization. He was a contributor to *The Performance Imperative* (1995).

McAdams lives in St. Louis with his wife, Jane, and their two sons, Ryan and Mitchell.

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PART ONE

THE FUNDAMENTALS

Almost nothing makes me skip a part of a business book like the title, “The Fundamentals.” The more accurate description of “book overview, background, everything starts with objectives and measurements, and assessment of what you have now” is just too long. I’ve tried to put thoughts into this first part that you can use for each type of performance improvement reward plan you may wish to design and implement.

“Getting Something Useful out of This Book—Quickly” (Chapter One) gives you a brief overview of the contents. *The Reward Plan Advantage* is anything but a novel, so I expect you will jump around to your areas of interest. This chapter should help that process by laying some context for the book, explaining why open-book management (OBM) is so important, and then describing each chapter. There is also a discussion of rules, or, more accurately, the lack of them. “How We Got Here” (Chapter Two) is my journey from teachings of Frederick Taylor to our present view of employees as assets. The real fundamentals for improving your organization’s performance through people are laid down in “Objectives and Measurements” (Chapter Three)—everything starts with them—and “Assessing Your Current Situation” (Chapter Four), which helps you get

The Reward Plan Advantage

a clear picture of how your organization presently reinforces employees.

I wouldn't skip Part One. The rest of the book will be of greater use to you if you are clear on the fundamentals.

Getting Something Useful out of This Book—Quickly

It took about eighty years after the onset of the industrial revolution for management to discover the customer, and it has taken about ninety years to discover the employee. Management thought leaders had already figured out how to calculate the lifetime value of a customer, and we are now trying to figure out how to calculate the value of employee contributions to organizational success.

The importance of the employee to the company can be seen in the experience of Springfield Remanufacturing Company (SRC), an engine remanufacturing company located in Springfield, Missouri. In the early 1980s, CEO Jack Stack and his management team bought the operation from International Harvester with the highest leveraged loan I'd ever heard of—eighty-nine to one—at an 18 percent interest rate. Not having the money to invest in capital improvements (or anything else for that matter), Jack had to rely on his employees. He taught them how the financial game is played—by the use of financial measures and attention to performance—engaged them, and made them accountable for winning. His bonus plan and partial employee ownership gave them a financial stake in the game, and it worked. Sales have risen from \$16 million to over \$90 million among their nine companies. The 10-cents-a-share stock price is now over \$20. SRC is a compelling example of how an organization's performance can be improved by improving its people through financial literacy, trust, engagement of all employees, and a customized reward system. These are all elements of “open-book management,” or OBM, as John Case of *INC.* magazine coined it in an article titled “The Open-Book Managers,” in September of 1990.

While SRC was toiling away in obscurity in Springfield, I was equally obscurely toiling away at Maritz Inc., a performance

improvement agency in St. Louis specializing in the use of incentives. As were a lot of other researchers in business, labor, and academia around the country, I was trying to discover what human resource practices, particularly reward systems, can make a difference in an organization's performance. (Chapter Two describes that journey.) In the early 1990s, national focus came to rest on SRC's success through Stack's book, *The Great Game of Business*, and on the research that was being done on reward systems with the publication of *Capitalizing on Human Assets*, which I coauthored with Elizabeth Hawk. Jack and I had both discovered the power of employees at about the same time, gotten to know each other, and found that our experiences dovetailed.

This book is about using rewards to get employees to contribute to an organization's success. You do not have to work in an "open-book" managed organization to use this book. Most companies won't ever be as open with and engaging of their employees as OBM companies are, but the reward plans described here can make a big difference anyway. If, however, you are or are becoming a practitioner of OBM, the plans and processes described here will show you how to develop a reward plan for your organization.

Use Every Asset You Have

Competitiveness demands that organizations get the best possible return on their assets. If you believe that people are assets and not solely a cost of doing business, this book will show you how to get a better return on these employed assets. Most companies spend a good deal of money, time, and energy on all kinds of reward plans, in addition to base pay, with little understanding of what they are getting in return. It is often possible to put a dollar value on that return, but sometimes it isn't. Such plans can make good business sense even without providing a dollar return, such as rewarding for customer satisfaction improvement. In any case, when organizations want employees to make a difference, they must be clear about their objectives, and they must make their reward plans *positively reinforcing* to employees. In addition, if organizations want to maximize the return on their investment, they must have the courage to unleash the creative energy of employees, enabling them to become contributing stakeholders.

What You Will Find in This Book

- A means for line and staff management to gain an understanding of reward plan options and of how to use education, communications, and assessment to make these options work most effectively.
- An argument for using group-based reward plans in addition to or in place of a portion of traditional compensation, to enable and reinforce employees at all levels to become more effective contributing stakeholders.
- An approach to improving the return on your investment in all your reward plans.
- A guide for involving all employees in improving organizational performance.
- A presentation of “best principles” rather than “best practices.” There are few, if any, “best practices.” Improving performance through people demands that you create plans for the unique needs of your organization. There is danger in trendy, cookie-cutter answers. I have used examples only to better describe how an approach works, not to suggest that any particular method will be successful for your organization—although it may well be.
- An enjoyable read, a unique view, a “how to” book when you need it to be.

Most managers have a basic understanding of how pay systems work, and organizations are probably not going to change fundamentally the way they pay people. The focus of this book, therefore, is on improving understanding of what employers can get from existing systems and on using additional (or redirected) funds to launch plans more directly aligned with their organization’s objectives.

Compensation can become a little exclusionary in its language. But you don’t have to know much about the technical aspects of compensation to make this book work for you. In fact, it may be better if you don’t. The book is addressed to all managers in the organization—top, line, or staff—rather than strictly to human resources (HR) personnel. While most HR functions serve the crit-

ical function of attracting, developing, maintaining, and retaining individuals, they have rarely addressed improving the organization's performance. Line managers are becoming more responsible for improving performance through employees, while HR is being reengineered into teams of consultants dedicated to supporting (and getting out of the way of) line management.

The Reinforcement Model

The framework for this book is the *Reinforcement Model* shown in Figure 1.1. In this model, *business objectives and desired culture* drive the design of the *total reward opportunity*, which is made up of *individual compensation, capability, recognition, group incentive, and project team incentive plans*.

In the model, the plans are ordered from left to right on a continuum from their individual to group focus and according to their potential for contributing to results (that is, the degree to which performance improvement can be attributed to the plan). I have labeled the compensation end of the continuum (which includes base pay, benefits, and most adjustments to base pay) *cost of doing business*, because it is most difficult to attribute business results to these plans; I have labeled the project team incentive end *business results*, because these plans only reward when the result of the contribution is measurable and valuable.

Moving from left to right on the continuum also represents an evolution from an administrative mind-set to a creative one. Beginning with capability plans, the creative demand placed on an organization is for imaginative approaches to a constantly changing environment. The need for creativity grows as does the need for alignment between employees and as the objectives that determine organizational success increase. The ability of an organization to meet those objectives in a cost-effective manner requires creativity. Creativity can open up the organization's systems to allow employees to move from job-bound, narrowly focused, micromanaged cost centers to become engaged, contributing stakeholders with both accountability and reward opportunity.

My objective in this book is to make the model complete rather than complex. But paying, rewarding, and recognizing people for the right things and the right results are not easy. If they were easy, you'd already be doing them.

***If they were easy,
you'd already be
doing them.***

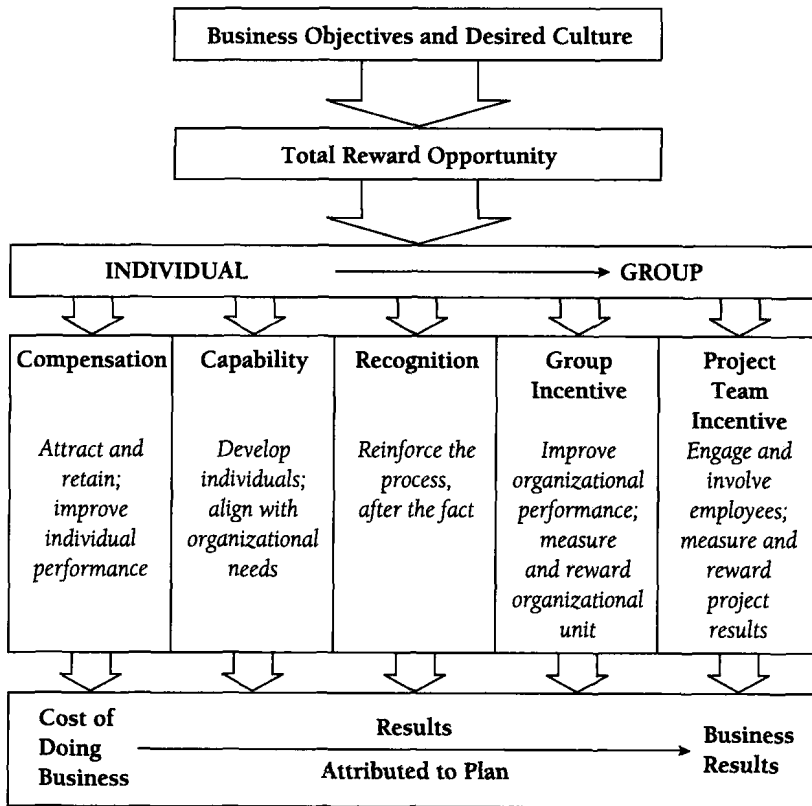


FIGURE 1.1. *The Reinforcement Model.*

It is critical to realize that the reinforcement model is just part of the picture. The real power comes from *performance management, assessment, education, communication, feedback, employee involvement, reassessment, and some fun*. These processes support the reward plans and create an environment of alignment and focus.

Results Through Individual Improvement

Most managers think that proper administration of individual compensation plans is their primary tool for performance improvement through people and that it can (or should) do it all. I disagree.

A good deal is already known about improving performance by focusing on the individual employee. This *bottom-up* approach is