

Wage incentive plans

Pay for performance (PFP)

- ***The evidence is insufficient to determine conclusively whether merit pay can enhance individual performance***----- The wall Street Journal
- ***Incentive plans cannot work***----- Harvard Business Review ***The approach is so flawed that it is hard to imagine a set of conditions which would make effective*** -----an expert on PFP
- ***The approach is so flawed that it is hard to imagine a set of conditions which would make effective*** -----an expert on PFP
- ***Financial incentives cannot motivate employees to improve their performance; however the absence of financial incentives can create employee dissatisfaction or demotivation***---- Kohn
- ***Don't motivate employees to improve their performance, "they motivate (them) to get rewards"***- --- Kohn
- ***Most people have a need to have their achievements acknowledged by others***---- Cummings
- ***Properly constructed pay-for performance systems can be successful*** ----- Cummings

Designing a PFP system

Requires three questions to be asked:

1. **Who should be included in the PFP system**
2. **How will performance be measured and**
3. **Which incentives will be used**

Individual PFP plans

- **Merit pay plans**
- call for a distribution of pay based on an appraisal of a worker's performance
- **Incentive pay plans**
 - a) **piece-rate systems** : paid per unit of production
 - b) **standard hourly rates**: payment is based on standard time (hourly rate)

Other incentive plans

- **Sales incentive plans**

- **Group incentive plans**

- a. profit sharing
- b. gain sharing
- c. employee stock ownership plans (ESOPs)

Types of some specific wage incentive plans

- >Straight piece rate >Straight piece rate with a guaranteed minimum wage
- >Differential piece rate system >Halsey plan >Rowan plan >Gantt plan >Bedaux plan
- >Emerson Efficiency Plan >Group incentive plan

Straight piece plan

Earning of a worker = No. of pieces X Rate per piece

Methodology:

- >Determine standard time >Find out wage for such job from job market

Advantage:

- >Simple and easy to understand and implement >Favorable to boost production rate

Disadvantage: >Possibility of quality problem >Minimum wage ignored

- >Straight piece rate with a guaranteed base wage

Method:

- >Determine output standard > Determine wage rate >Determine guaranteed wage rate

Advantage:

- >Provides a guaranteed minimum wage >Takes some care of the enforced idleness

Disadvantage:

- Does not offer sufficient incentive to a better former

Example:

Output standard per day = 10 piece

Wage rate per hour = 10 Tk

Working hours per day = 8

Wage per piece = $(8 \times 10) / 10 = 8$ Tk

The guaranteed wage rate = $8 \times 10 = 80$ Tk per day

Situation 1 : a worker makes 6 pieces will get 80Tk per day

Situation 2: a worker makes 20 pieces will get 160 Tk per day

Conclusion: variation in wage rate per piece!!!!!!

Differential piece rate system

- Suggested by F.W. Taylor
- Modified by Merrick

Methods:

- A higher wage rate for exceeding the standard output
- A lower wage rate for failing to reach standard output

Disadvantage:

- inferior or fresh worker will be in trouble
- wage calculation is complex

Taylor's differential piece-rate system posits that the worker who exceeds the standard output within the stipulated time must be paid a high rate for high production. On the other hand, the worker is paid a low rate if he fails to reach the level of output within the standard time. Thus, there are **two piece-rates**, one who reach the standard output or exceeds it, is paid **120 percent** of the piece rate. While the one who fails to reach the standard level of output, is paid **80 percent** of the piece-rate. The minimum wages of the worker are not guaranteed.

This system can be further understood through the example given below:

Standard Output = 200 units

Rate per unit = Rs 10 paise

Case (1): Output = 220 units

Earnings = $220 \times (120/200) \times 0.1 = \text{Rs } 13.20$

Case (2): Output = 180 units

$$\text{Earnings} = 180 \times (80/200) \times 0.1 = \text{Rs } 7.20$$

It is clear from the above example that the worker is paid a higher rate (**Rs 13.20**) for high production (**220 units**) and low rate (**Rs 7.20**) for low production (**180 units**). Thus, Taylor's differential piece rate system works on the principle that the inefficient worker must be paid at a low piece-rate for low production such that he is left with no other option but to leave the organization.

Halsey plan

- A minimum base wage is guaranteed
- An additional bonus is given to worker who exceeds standard output level (50-50 sharing)
- Output standard is based on previous records of production

$$W = (R \times T) + (P/100) (S - T) \times R$$

For 50-50 plan,

$$W = (R \times T) + (S - T) \times R/2$$

Where, R = hourly wage rate

T = actual time taken to complete the job and

S = standard time or allowed time

Example of Halsey plan

Situation 1:

Actual time taken by a worker = 4 hrs

$$\text{Therefore, } W = (10 \times 4) + (5-4) \times 10/2 = 45 \text{ Tk}$$

$$\text{Wage rate per hour} = 45/4 = 11.25 \text{ Tk}$$

Situation 2:

Actual time taken by a worker = 6 hrs

$$\text{Therefore, } W = (10 \times 6) + (5 - 6) \times 10/2 = 55 \text{ Tk}$$

$$\text{Wage rate per hour} = 55/6 = 9.16 \text{ Tk.}$$

Situation 3:

Actual time taken by a worker = 5 hrs

Therefore, $W = 10 \times 5 + (5 - 5) \times 10/2 = 50$

Wage rate per hour = 10 Tk

Advantages of the Halsey Premium Plan:

- 1. It is simple to understand and relatively simple to operate.
- 2. It guarantees time wages to workers.
- 3. The wages of time saved are shared by both employers and workers, so it is helpful in reducing labor cost per unit.
- 4. It makes distinction between efficient and inefficient workers because it provides increasing incentive to efficient workers.
- 5. Fixed overhead cost per unit is reduced with increase in production.
- 6. The employer is able to reduce cost of production by having reduction in labour cost and fixed overhead cost per unit. Lower cost gives him incentive to provide the best possible equipment's and working conditions.

Disadvantages of the Halsey Premium Plan:

- 1. Quality of the work suffers because workers are in a hurry to save more and more time to get more and more bonus.
- 2. Workers criticise this method on the ground that the employer gets a share of wages of the time saved.
- 3. Difficulties are experienced in determining standard time and hourly rate of wages which may be acceptable to workers.