Bonus by Whimsy

by Paul Eldrenkamp

Having tried several types of employee bonus programs over the years, I have developed two strong opinions about their effectiveness. First, although bonuses can help solve short-term problems, they're a poor long-term strategy. Second, a bonus plan based on a mathematical formula represents an easy way out and too often rewards the wrong kind of behavior.

Bonuses can be useful motivational tools. For example, you could use a bonus to focus short-term attention on changing a bad habit. Suppose your new lead carpenter is visiting the lumberyard two or three times a day, and you want him to plan better and go only two or three times a week. He thinks you've been out of production too long. He can't see a way to plan in advance for something as chronically unpredictable as a remodeling project.

A $100 bonus, offered as a reward for two weeks in a row of one lumberyard trip or less per day, may motivate the new lead to break an old habit. After three or four weeks, the bad habit will have been broken. If not, you have a problem beyond the scope of this column.

A situation like this may appear to be an ideal time for a bonus because it's simple, easy to measure, and of limited duration. Keep in mind, however, that although offering a bonus may be the easiest and most immediate approach to solving a problem, it is not the only way or the best way.

The Formula Approach

The bonus programs that seem to attract the most attention are also the ones that tend to be rather complex. So complex, in fact, that the person in charge is often unable to offer a coherent explanation of how it works without resorting to spreadsheets and graphs and lots of intricate hand gestures.

Formulas for bonuses take on a wide variety of shapes and sizes. The common element is a densely packed equation for determining how much, if any, extra money is distributed among employees at the end of a specific job or period of time.

Some bonus plans, at least one of which I've tried, are based on job profitability. For example, a lead carpenter brings a job with a production budget of $6,500 in at $6,000. Company policy may dictate that the lead is entitled to half of the savings — $250 in this case (50% of $500).

Or the plan could be based on the company's overall profitability. Let's say the company's goal is a $50,000 net profit, a big job, but the actual profit is $80,000, a $30,000 windfall. The policy might distribute at least some of that windfall to the employees using a prearranged formula. This formula might be based on the ratio of an individual's total compensation to the whole. For example, a crew member earning $50,000 a year would be entitled to twice the amount of a crew member earning $25,000 a year. Or maybe the number of years of employment would be used, or some combination of the two.

The True Cost

What are the consequences of such plans, both short- and long-term? One consequence is that you focus everyone's attention on whatever outcome will be rewarded. If you're rewarding job profitability, you will get a focus on job profitability. But it may come at the expense of other important goals such as client satisfaction, subcontractor loyalty, and good teamwork between the salesperson and the lead carpenter.

As a countermeasure to this problem, some bonus advocates promote an "affidavit of satisfaction" to be signed by the client before the lead can collect the bonus. However, clients, even those dissatisfied with a job, are often reluctant to tell company owners the truth and may sign such affidavits out of a sense of responsibility or loyalty, or just to get you out of their lives.

Formula-based bonus systems are capable of rewarding only a few of the many behaviors that you are trying to instill in your employees. A mathematical formula can result in a bonus dollar amount, but I view it as tantamount to the company owner abdicating responsibility for the evenhanded implementation of a program.

There's also a good chance, especially with "company profitability" bonuses, that employees won't really understand what they're supposed to do, and why, to get the bonus. You want them to help you make the company more profitable, but you haven't *taught* them how to help make the company more profitable. You haven't taught them how because you're not sure yourself. Otherwise, you wouldn't need the profitability bonus program in the first place.

These are all short-term consequences. A long-term consequence is that everyone comes to expect the bonus, and it becomes a part of their salary, except that it comes a little later and makes the owner feel generous. I have read several studies on the long-term effect of bonuses on employee productivity and satisfaction, and there is little, if any, correlation between them over time. So why go through the hassle? Why not just pay the appropriate salary to begin with and save everyone time?

The Owner Whimsy Approach

One type of bonus program, however, I do advocate: the Owner Whimsy

Bonus. The rules are simple: I pay out the money when I feel like it.

I might choose to reward something that was done particularly well, or an unusually good effort, or someone who had a rough time recently. I'll write a check, or I'll pass on getting reimbursed for a tool, or I might give someone a few paid days off.

I once even rewarded a lead carpenter who blew up at a client at the weekly job-site meeting. After the meeting, I made it clear that that was totally unacceptable behavior, while I wrote out a check for a couple hundred dollars. Let me explain: The lead blew up because the client was methodically very demanding, and I wasn't there to provide the lead with enough coaching or support in dealing with this difficult person. The lead carpenter was feeling abandoned, and the bonus was really for blowing up only once, despite many good and reasonable opportunities to do so. I was acknowledging the extremely difficult situation the lead was in.

There is no formula for circumstances like that. With the Owner Whimsy approach to bonuses, not only can I consider showing an employee his or her value and appreciation in this way, but I can go ahead and do it — whenever I like. And I can tailor it to the individual or individuals: money, time off, a gift certificate, whatever I think they would appreciate the most. It allows me to use bonuses as a positive reinforcement without incurring a continuing obligation. And that, I like the best.

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