Despite the numerous questions that can be raised about the limitations of individual pay-for-performance incentives (summarized in Exhibit 6-6), such plans are nonetheless becoming more popular. Although there is evidence that managers in non-U.S. countries are far more skeptical of the positive arguments U.S. managers make concerning the performance benefits of discretionary bonuses, such bonuses are becoming increasingly popular around the world.[15]

Team-based pay-for-performance plans are becoming more popular in direct relationship to the rising reliance on team effort. Among performance incentives aimed at nonexecutive employees, in fact, team-based plans have become the most popular.[16] Under such a plan, teams can share a performance bonus equally or allocate to individual members based on an evaluation of their contribution. Team-based bonuses enhance team performance, although the effect is relatively weak.[17] A caveat is in order, however. Team-level bonuses can hurt collaboration *among and between* teams.

Performance appraisals are inherently subjective, with supervisors evaluating subordinates according to their own preconceived biases

Emphasize individual rather than group goals that may lead to dysfunction conflict in the organization

Encourage a short-term orientation (the performance period being evaluated) at the expense of long-term goals

Merit pay raises become an annuity on which employees continue to draw regardless of future performance

The often lengthy time lag between actual performance and reward undermines perceived connection between the two

Many jobs cannot be individually isolated and precisely measured without taking into account complex interdependencies

Pay differentials between performance levels tend to be relatively small and therefore of questionable behavioral value

Actual payout of program often determined by organizational factors beyond the control of individual employees and only indirectly related to actual performance

Exhibit 6-6 Factors That May Undermine Effectiveness of Individual Pay-for-Performance Plans.

Based on Luis R. Gomez-Mejia, David B. Balkin, and Robert L. Cardy, *Managing Human Resources* (Englewood Cliffs, NJ: Prentice-Hall, 1995), p. 404 and Edward E. Lawler III, "Pay Strategy: New Thinking for the New Millennium," Compensation and Benefits Review 32 (January-February 2000), pp. 7-12.

Theory into Practice

Organizations call upon team-based performance bonuses to enhance the effectiveness of teams, but the bonus may undermine collaboration between teams.

Because strategic renewal focuses on organizational performance, *organization-level* incentives often supplement or replace individual bonuses. Traditionally, organizations have offered organization-wide incentive bonuses only to executives and upper management on the assumption that their actions are more closely tied to overall organizational performance than employees at lower levels. However, some organizations have adopted a different perspective. Part of Archie Norman's strategic renewal at Asda was to offer an organization-level performance bonus to all employees, encouraging everyone to keep focused on the same measures of overall effectiveness.[18]

Theory into Practice

Bonuses based on the overall performance of the organization make a symbolic statement recognizing the shared purpose and responsibility of all employees and organizational units.

Stock options are intended to tie the total compensation package of individuals to the performance of their organization.[19] The goal, as articulated by the board of directors of eBay, is to "align the interests of directors and executives with the interests of stockholders."[20] Favorable tax laws have made these plans more popular in the United States than elsewhere, although a number of multinational firms—PepsiCo, Bristol-Myers Squibb, DuPont, and Merck among them—have offered stock options to virtually all of their employees worldwide.[21]

The actual effectiveness of these various organization-level performance bonuses is unclear. Some sort of incentive tied to organization-level performance is a frequent characteristic of high-performance companies.[22] What is less certain is whether the organization-level performance bonus results *in* or *from* outstanding performance. The cause-and-effect relationship between specific behaviors and organizational outcomes may be far too vague, especially in large organizations, to create a powerful incentive on the part of individual employees.

Undoubtedly, the degree to which organization-wide bonuses are accompanied by communication and feedback on firm performance, as well as the empowerment of employees to impact performance, will enhance the plan's motivational impact. Tying all employees' pay packages in some significant way to the same organizational-level outcomes may help in both a symbolic and real way to communicate a mutuality of interests and concerns.

Intrinsic and Extrinsic Rewards

Incentive pay, regardless of the specific design, is an **extrinsic reward** : a reward external to the individual and provided by the organization. Money is the most obvious and prevalent example of an extrinsic reward. Motivational theory tells us that extrinsic rewards, although powerful, may not be terribly effective in driving long-term behavioral change.

> Building a Vocabulary of Change
> ***Extrinsic reward***
> rewards (pay, promotion, praise, and so forth) provided by the organization to employees.

Theory into Practice

By relying heavily on extrinsic rewards to shape employee behavior, organizations risk driving out the intrinsic rewards that might be associated with the work; as a result curiosity, creativity, and problem-solving behaviors may be lessened.

Commitment to adopt new behaviors comes from *within* individuals. If the goal of change is to create motivation—as internalized desire on the part of employees—to adopt new behaviors, then organizational leaders need to consider intrinsic rewards as well. An **intrinsic reward** is a positive outcome naturally associated with a behavior.