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Viewpoint: Tips for using incentive-based management to grow your company.

By John M. Collard

Business owners willing to invest in realistic incentives that reward achievements accomplished by managers and employees, reap the proceeds.

The key to success is to set realistic goals and timeframes; hold managers accountable for performance; and communicate measurement and reward methodology . then step back and let them perform. Always be sure to reward positive results when goals are achieved, but never give a reward when goals have not been accomplished. If goals are met, the cash will be there to pay a bonus.

Incentive plan

When employees can see dollar signs and goals are clearly stated, their mindset changes and they become more creative. Incentive Compensation (IC) should reward performance and teamwork, which produces results.

The ultimate goal of the motivational plan is to improve the equity value of the company. Share profits in proportion to the risks being taken. Owners accept risk when entrusting operations to the capability, judgment and decision-making of the people who work for them.

WHEN EMPLOYEES SEE DOLLAR SIGNS THEY BECOME MORE CREATIVE.

When an employee' s income is based purely on performance, as it is in sales, the risk-to-reward scenario is much greater than for a salaried employee. An employee working under an agreement or union contract governing work behavior and performance will receive less of a bonus by comparison for achieving their goals. If they want the rewards, they should share the risk.

Develop an incentive pool based on the amount of gross margin (G/Mgn) and distribute bonuses based on a weighted average to the team. When the company does well, G/Mgn improves thereby increasing the size of the bonus pool, and IC is greater. Tie the incentive at budget to a percent of salary to help the weighing average calculation. Managers will have to control several components to achieve results without losing sight of the end goal.

Pay management incentive compensation based 50 percent on what the employee is directly responsible for, 30 percent on how their performance impacts other key departments (i.e. how sales can improve production throughput), and 20 percent on their ability to improve equity value or other elements within their control. The intent is to measure performance, and just as importantly, cooperation between departments and personnel.

Viewpoint:

Structure a bonus payment scale in accordance with "worst," "likely" or "best" scenarios. In the "worst" case, few bonuses should be paid because goals were not met. In the "likely" case, pay 40 percent to 60 percent of the full bonus rate. In the "best" case, pay maximum bonus rates. The scale is clearly weighted toward higher bonus for greater performance. Communicate progress early and often.

Incentive payments

Distribute on a year to date (YTD) calculation, paid quarterly. So the company doesn't take all of the risk, pay two-thirds of the YTD bonus at the end of the first quarter, 75 percent at the end of the second, 85 percent at the end of the third, and the remainder at the end of the year. This reserve within the company will avoid early payout for exceptional results without sufficient catch-up period if these results don't continue. Employees can share in the rewards as they occur rather than waiting until year-end, an added incentive.

Plan specifics

Function: General manager

Focus on: Company value

Incentive: 50 percent — equity value improvement; 30 percent — Earnings Per Share (EPS); 20 percent — employee motivation

Function: Sales

Focus on: Sales revenue

Incentive: 50 percent — profitable revenue generated; 30 percent — consistent/flexible work flow; 20 percent — EPS/net profit

Function: Estimating

Focus on: Profitable work

Incentive: 50 percent — new business win ratio; 30 percent — consistent work flow; 20 percent — EPS/net profit

Function: Production/project management

Focus on: Throughput project profit

Incentive: 50 percent — gross/ margin, resource utilization; 30 percent — billing rate over-recovery; 20 percent — EPS/net profit

Function: Human resources

Focus on: Employee relations

Incentive: 50 percent — employee motivation; 30 percent — employee satisfaction; 20 percent — low rate of turnover

Function: Finance

Focus on: Financial cash flow

Incentive: 50 percent — timely and accurate information; 30 percent — overhead cost control; 20 percent — cash availability

Focus

Direct the general manager to guide the value of the company in terms that an investor or purchaser would use to measure the company. Emphasize interdepartmental coordination. The best measure of plant throughput is hours worked versus hours billed; those hours on timecards compared to invoiced to customers. The closer this ratio is to a one for one relationship, the better the productivity, the throughput and the profitability.

Conclusion

Tie them to your goals to create focus. Motivate the entire work force, allow creative thinking and gladly pay the bonus when the results improve the equity value of your company. When the equity value increases, share price improves the value of the investment for shareholders, you can pay dividends or reinvest in the growth of your company. Reinvestment often yields greater returns.

Incentive-based management is a catalyst toward improving direction and value creation.

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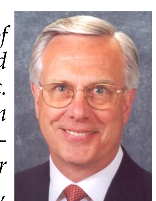

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