# Focus on Compensation - Steer Teams with the Right Pay

By Charlotte Garvey

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(www.shrm.org/Publications/hrmagazine/EditorialContent/Pages/0902toc.aspx) *Team-based pay is a success when it fits corporate goals and culture, and rewards the right behavior.*

Shifting your company's compensation structure from an individual-based system to one that includes team-based pay can yield powerful results, such as increased efficiency, productivity and profitability. But making the switch is not for the faint of heart and does not work for all companies.

The notion of team-oriented corporate structure came into vogue in the United States during the 1980s and 1990s, prompted by the example of successful Japanese companies. Over the past 10 years, the use of team-based pay has ticked upward, says Edward Lawler, director of the Center for Effective Organizations and a distinguished professor of business at the University of Southern California's Marshall School of Business. The center's periodic surveys of *Fortune* 1,000 corporations indicate that in 1990 about 59 percent of companies surveyed were employing a team-based compensation system. The figure had risen to 80 percent by 1999, the most recent year for which data are available.

But Lawler cautions that this figure does not mean that team-based pay is widespread throughout the halls of corporate America; it "just means they used it somewhere." He adds, "In virtually no organization is it a companywide practice."

**Finding the Right Fit**

Teams can be structured a variety of ways. They can be groups of multi-functional employees brought together temporarily to accomplish a specific task, such as developing a new product or penetrating a new market. But the more common and more successful structure is a manufacturing cell or other type of small group where employees are brought together along functional or business unit lines on a permanent basis to produce a product, perform an ongoing task or provide a service. Team pay also is occasionally used in the sales arena.

Teams vary in size as well. Verizon Directory Graphics, a 300-employee Yellow Pages directory production center in Valley Forge, Pa., that is part of telecommunications giant Verizon Communications, operates essentially as one large team.

Consumer products company Dial Corp., of Scottsdale, Ariz., has organized its operations using the team concept, with multi-functional teams grouped according to the company's four core business units: personal products, laundry products, home products such as air fresheners, and food products. But Dial is looking at breaking its business-unit-based program into smaller groups, possibly based on work groups or production cells within each business unit.

While there is no hard-and-fast rule about appropriate team size, some experts suggest that communication and coordination can become difficult for groups larger than 15 to 20 people.

The reasons that companies pursue team-based pay vary. In some cases, an employer uses teams to reinforce an underlying change in business strategy, corporate structure or production method. In other cases, an employer implements team-based compensation to support the company's operational philosophy, using compensation incentives to motivate employees to work more cooperatively and to connect their actions to its bottom line. Sometimes this approach succeeds, and sometimes it fails.

"Does team pay deliver results? No," says Brad Hill, an incentive-based-pay expert with the Hay Group consulting firm in Chicago. "But team pay supports initiatives that can deliver results." Employers who venture into the complex world of team pay without an underlying strategic goal or philosophy risk major problems communicating their goals to employees, Hill advises.

Team-based structures have not always been accompanied by team-based pay. And there are a number of factors that have moderated team pay's acceptance on a broader scale.

One of the issues is corporate culture. "The reason companies don't like to do it is because it is very difficult for people to accept," says Jay Schuster, a partner in the Los Angeles-based compensation consulting firm Schuster-Zingheim and Associates. The notion that some of an individual's pay is at risk based on someone else's behavior or by the team overall is "a hard sell," especially in an American culture that celebrates individualism.

"Culture has a more powerful impact on rewards than rewards have on culture," says Schuster. Team pay works better in organizations that have an egalitarian, sharing orientation, he says. "Entrepreneurial companies have trouble with it."

**Multi-Layered Structure**

Many organizations that use team pay employ a layered compensation structure. This means a team member receives a base salary and is eligible for a bonus based on the team's success in achieving specific goals. The bonus is sometimes set as a percentage of base pay, such as 10 percent.

In other team-pay programs, the company sets up a bonus pool available to the team, and each member receives the same size bonus if targets are met. These goals are often set by team members but also can mirror corporate financial goals. At Dial, each business unit's goals relate to sales, earnings, inventory/cash flow and market share for that unit, says Ron Liggett, manager of corporate compensation. At Verizon Directory Graphics, "the driving force is pro.cess improvements," says Mike Gaudioso, a photo compositor and member of the compensation design team, which consists mostly of Verizon employees from the Valley Forge site. "The specific targets and goal of the program are set to mimic the corporate goals and expectations," he adds.

Many team-based programs are self-funded, meaning the bonus money is derived from the savings that result from meeting team goals. At Verizon Directory Graph..ics, payouts come from savings in controllable costs and from improvements in efficiency.

A number of companies add another layer of incentive pay to team-based pay—a bonus that is tied to the success of the company as a whole that usually is described as gainsharing. The resulting compensation system can be a rather complex web. Experts agree that a key success factor is setting an appropriate level for the team-based bonus vs. individual pay. "You have to have a threshold that's high enough" to influence team members' behavior, Schuster notes.

One issue that can limit employee acceptance of team pay is the fear of the "slacker" or "free-rider"—an unmotivated team member who doesn't pull his weight. Most experts acknowledge this is a real concern from the employees' perspective, but say layering bonuses can offset this problem.

For instance, companies can add a reward opportunity for individual team members as well "where people who contribute the largest amount to the team objectives receive the largest amount," says Robert Heneman, director of the Master of Labor and Human Resource Program at Ohio State University's Fisher College of Business in Columbus. But he cautions that "you've really got to have good performance measures" in place.

### Evolution

Team-based pay seems to be working well at Phelps Dodge's North American mining operations, says John Hall. But Hall, a senior compensation specialist at the Phoenix-based copper producer, also stresses the program has been "evolutionary."

The Phelps Dodge program, which involves more than 4,200 employees at six North American locations, was launched to help achieve a specific corporate goal. "We went to team pay to change the mind-set of the employees from an hourly mentality to a salaried workforce," Hall says. The company underwent a "massive decertification" at the mines during the 1980s, so the six locations are now non-union.

Under the Phelps Dodge system, employees get a base salary with additional compensation awarded for hitting team-based goals, along with goals set for the specific location or mine. For example, a typical team goal in a truck maintenance shop would be to shorten the time that trucks are off-line for maintenance.

As in many successful team-based programs, Phelps Dodge team goals are set by the team members. "It's much more of a participative process than it had been historically," Hall notes.

The company continues to reshape the compensation system to make it work better. Phelps Dodge is developing an individual bonus option to add to the compensation package, prompted by employee interest. "There certainly has been anticipation of getting some of the individual performance built back in," Hall says.

### Money Is Not Always a Motivator

At Verizon Directory Graphics, the jury is still out on the program. The company is fighting a hangover from a previous incentive compensation program that sank, partly because of employee apathy. Gaudioso says the complexity of the program and a lack of employee understanding of the system led employees to regard payments as an entitlement rather than an earned reward that required their involvement and innovation. He says apathy continues to be a problem to some degree. There always will be employees focused on getting the check but not on why they are getting the check, he notes.

But overall, Gaudioso says the program is an improvement over the old incentive plan because the new plan was designed primarily by production-level employees, and thus it is aimed at production-level employees. "The program has a lot of potential for both process improvement and worker empowerment," he says. "I do remain hopeful for its expansion" to other parts of Verizon.

Dial's Liggett, citing decades of compensation experience, cautions that team pay works well as long as a company is doing well and there is a payout. In a bad year, it may be a different story. He cautions against an excessive focus on compensation as a motivator, suggesting recognition programs can be an excellent motivator, too.

"It isn't always the money," Liggett notes.

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