A guide to team incentive systems

Jody R. Hoffman and Steven G. Rogelberg
Bowling Green State University, Bowling Green, OH, USA

Are you confused about team incentive systems, either wondering if your organization should implement one and, if so, how it should be designed? If your organization uses teams, compensation experts would argue that to the extent your organization desires optimal performance, some form of team incentive system is required (Bartol & Hagmann, 1992; Doyle, 1992; Geber, 1995; Johnson, 1996; Sisco, 1992). A team incentive system sends a message to employees that their team's output and performance is valued by the organization (Englander, 1993; HRFocus, 1993; Pritchard et al., 1989). If team performance is not rewarded, such performance is not likely to be optimal (Doyle, 1992; Geber, 1995).

After reviewing empirical and trade journal literature and analyzing the characteristics of team incentive practices, we have concluded that seven major categories of team incentive systems exist (see Figure 1). The seven categories are: 1) team gainsharing/profit-sharing, 2) team goal-based incentive systems, 3) team discretionary bonus systems, 4) team skill incentive systems, 5) team member skill incentive systems, 6) team member goal incentive systems, and 7) team member merit incentive systems. The present paper will review each system in turn, presenting relevant research evidence. In addition, guidelines for choosing among team incentive systems will be reviewed. Overall, this paper provides a much needed synthesis of the extant literature.

System I: team gainsharing/profit-sharing
In the case of team profit-sharing and gainsharing systems, team incentives are tied to organizational outcomes (e.g., organizational profit, organizational productivity, customer satisfaction, and so on). Specifically, in team profit-sharing systems, the organizational outcome evaluated is financial in nature; that is, teams are rewarded when the organization makes a certain amount of profit (McNerney, 1994; O'Neill, 1994; Swinehart, 1986). In these systems, cash rewards are generally shared equally among all of the various teams in an organization.

Unlike profit-sharing, gainsharing systems distribute incentives as a function of non-financial organizational outcomes, such as improvements in quality, productivity, and customer satisfaction (Miller & Schuster, 1993; Schuster, 1993; Swinehart, 1986). At Du Pont, for example, all teams receive bonuses when the company experiences at least a 4 per cent increase in productivity and sales over a financial period. Six main variants of gain-sharing are found in practice (Miller & Schuster, 1993; Swinehart, 1986), including
Scanlon plans, Rucker plans, Improshare plans, Productivity and Waste Bonus plans, Group/Plant plans, and DARCOM plans. These plans differ on a number of dimensions, including the focus of the plan (e.g., improvements relative to historical company standards, in productivity, quality, the ratio of labor hours to product output, and so on) and the degree of team participation in developing improvement schemes (Miller & Schuster, 1993; Swinehart, 1986).

When deciding whether to implement these team incentive plans, it must be kept in mind that as the basis for a reward becomes further removed from the team’s immediate control (e.g., organizational profit), profit-sharing and gainsharing are thought to become less effective at improving team performance. This has been termed the "line-of-sight" problem: teams feel they cannot affect organizational profit (or other outcomes) significantly or directly, so they do not try to improve their performance (O’Neill, 1994; Sisco, 1992). If line-of-sight is a concern, a Group/Part gainsharing plan that targets departmental objectives may be more appropriate, as departmental outcomes may be easier for a team to perceive control over (Nickel & O’Neal, 1991).
Additionally, when profit or gainsharing systems are instituted, it is argued that payouts should be frequent, so that the relationship between team performance and the reward is clear (Thornburg, 1992).

An additional consideration when implementing a profit or gainsharing system concerns the reward distribution between teams. Profit-sharing and gainsharing systems with equal payouts across teams are thought to work well in highly interdependent organizations, where inter-team cooperation is important (Recardo & Pricone, 1996; Pritchard *et al*., 1989). Field research has found such systems institute perceptions that different teams share common goals, thus improving cooperation among teams (Anfuso, 1995; Tjosvold, 1988). However, when team interdependence is not a factor in organizational success, gainsharing or profit-sharing systems with equal reward distribution among teams may be less appropriate. In such cases, more competitive structures (i.e., the size of a reward is dependent upon team performance) may actually improve team productivity (Johnson, Maruyama, Johnson, Nelson, & Skon, 1981). However, when introducing competitive team gainsharing or profit-sharing structures, it is important that teams perceive such structures to be equitable (i.e., a perception exists that each team could attain the same rewards if they put in the same amount of effort); otherwise, feelings of unfairness will result (Pritchard *et al*., 1989; Thornburg, 1992).

The next issue the organization must consider concerns how to distribute incentives among team members whose teams qualify for cash rewards. If team members perform similar functions, or if their tasks are highly interdependent, equality of reward distribution has been argued to be most likely to ensure optimal team performance. As the need for cooperation among team members increases (e.g., encouraging one another, pooling information and ideas, etc.), the need for equality of rewards also increases (Doyle, 1992; Rosenbaum *et al*., 1980; Slavin, 1977; Tjosvold, 1984), although some recent laboratory work (Wageman & Baker, 1997) suggests that the beneficial effect of such team rewards on performance does not come from an increase in cooperative behavior. Organizations may be concerned, however, that distributing rewards equally among team members will encourage slacking. Research evidence does not support this contention (e.g., Sheppard & Wright, 1989; Stonem & Dickinson, 1989; Wageman & Baker, 1997).

If, however, team member interdependence is not essential for success, or if some members of the team clearly make more important contributions than others, the team incentive system reward distribution should reflect this by being equitable (i.e., a reward distribution based upon relative contribution may be most effective). Indeed, equality of reward distribution in experimental research has been found to negligibly or negatively impact group performance when team member tasks were not highly interdependent, while equitable rewards resulted in higher performance levels (Farr, 1976; Young, Fisher & Lindquist, 1993). When instituting a differential reward distribution system, however, the organization must ensure that it is possible to effectively measure
the relative contributions of team members to team outcomes (Pritchard et al., 1989; Johnson, 1996).

**System II: team goal-based incentive systems**

At Lotus Development Corp., sales teams earn one-time monetary bonuses when the team meets or exceeds sales goals (Sales and Marketing Management, 1991). At Saturn, a "Risk and Reward" program exists for self-managed work teams. Teams are evaluated quarterly, and when a team meets or exceeds its productivity and/or quality goals, team members earn variable pay, which generally amounts to 10% of their salary (HRFocus, 1995).

The team incentive systems at Lotus and Saturn are examples of team goal-based incentive systems. In this type of system, the organization (often in conjunction with the team) formulates "goals" or "targets" for each team that are believed to reflect effective performance outcomes (e.g., predetermined production objectives, customer service goals, etc.). Such goals may be very short or long-term objectives. When the team's performance meets the target in question, its members earn a predetermined monetary or nonmonetary reward (Johnson, 1996; McNally, 1992). In the case of monetary incentives, rewards can take the form of bonuses or variable pay. In the former, one-time cash rewards are provided. In the latter, team members' base pay may be decreased by five to ten per cent, with the lost salary becoming variable pay. If the team meets its target(s), team members earn their variable pay back; if the team exceeds its targets, variable pay can double or triple (Geber, 1995; HRFocus, 1995; Overman, 1995; Zingheim & Schuster, 1995). Although variable pay percentages are the same for all team members, this does not ensure that each member receives the same amount of variable pay. That is, some team members may have higher base salaries, thus earning more reward. Similarly, in the case of team bonuses, team members do not necessarily receive equal rewards. If an unequal bonus distribution is used, it may be based upon each member's relative contribution to the team outcome: alternatively, rewards may be allocated proportional to each team member's salary (Bartol & Hagmann, 1992). Winsharing is one interesting monetary reward system which is a combination of goal-based and profit-sharing team incentive systems (Schuster & Zingheim, 1992). In such systems, teams qualify for profit-sharing payouts based on their performance relative to their predetermined goals. Finally, with regard to nonmonetary rewards received for meeting goals, innumerable examples exist, including time off work, achievement awards, special dinners (Klubnik, 1995). Nonmonetary rewards, on the other hand, tend to be shared equally among the group (i.e., generally no member receives more of a nonmonetary reward than another member).

Team goal-based system effectiveness is thought to be dependent upon the type of team the system targets. That is, this system is thought to be most appropriate for full-time teams, as these teams are thought to benefit most from clear, predetermined performance targets, particularly because the activities of full-time teams should be clearly specified in advance (Gross, 1995; HRFocus,
One exception occurs when such teams face ambiguous tasks in which pre-determined goals can quickly become obsolete. Additionally, these systems may be less appropriate for part-time teams when more time is spent on individual tasks, as opposed to team tasks, as such systems may send the message that the team’s work is highly valued and should be emphasized over team member’s individual tasks (Pitman, 1994). Finally, when distributing rewards among team members, the same considerations presented in the previous section apply to these systems as well (e.g., as the interdependence of team members’ tasks increases, equal reward distributions are recommended, while equitable reward distributions are most helpful as team member tasks become more independent).

System III: team discretionary bonus systems
At a major retail clothing company, teams are provided with one-time cash awards when management believes the team has done an exceptional job in developing products or marketing strategies, among other types of performance (Geber, 1995). This is an example of a discretionary team bonus system. Also known as “spot reward systems,” these team incentive systems, like goal-based incentive systems, evaluate team outcomes (i.e., customer satisfaction) when determining whether a specific team should be provided with incentives. Unlike goal-based systems, however, the team is not provided with a predetermined performance standard which will guarantee the receipt of a specific predetermined reward. Instead, when the organization feels a team has done an outstanding job, the team is provided with a monetary or nonmonetary reward (Kanin-Lovers, 1993).

Like team goal-based incentive systems, it may be the case that discretionary team bonus systems are best for full-time teams, especially when a high degree of cooperation is not required between teams in an organization. However, when inter-team cooperation is necessary, such incentives may create conflict and resentment, decreasing a team’s motivation to perform well. Specifically, when teams must cooperate, yet only certain teams receive rewards, those teams which do not receive such rewards may become less cooperative in the future.

In the case of part-time teams, it is important that a team reward system not be so enticing that it leads team duties to conflict with the team member’s primary responsibility, namely their individual job. Therefore, no monetary rewards should be offered to part-time teams under this system (Gross, 1995; Wageman, 1995). Finally, when deciding whether to distribute rewards equally or equitably among team members, one must keep in mind the same guidelines described earlier, namely the degree of cooperation required among team members.

Systems IV and V: team and team member skill incentive systems
At the Alliant Health System, teams are rewarded when they demonstrate the acquisition of certain skills. For example, when supervisory staff and team
members agree that the team has developed cooperation skills, monetary bonuses are provided to team members (HRMagazine, 1995). On the other hand, when the employees of the Aid Association for Lutherans (AAL) were grouped into a number of cross-functional teams, AAL implemented a team incentive system in which team members were able to increase their salaries by demonstrating the mastery of new skills (e.g., individual initiative and cooperation with other team members) which allow them to perform well in the team. The mastery of skills was evaluated via regular performance appraisals performed by managerial staff (HRFocus, 1995). The former is an example of a team skill incentive system, the latter an example of a team member skill incentive system.

Team skill incentive systems differ from the incentive systems discussed thus far in that team skills, not team outcomes, are evaluated when determining if a reward should be distributed. That is, when a team is deemed to have acquired or improved upon valued skills (generally as determined by supervisors), the team is rewarded, regardless of the team’s outcomes. Such systems are based upon the idea that, if circumstances are favorable, a team exhibiting the proper processes, such as collaboration and interpersonal understanding, will achieve desired outcomes (Geber, 1995; Musselwhite, 1988). Incentives in team skill systems can be monetary or nonmonetary.

Team member skill incentive systems are similar to their team skill incentive counterpart. However, the team member’s skills and competencies, and not the team’s, are the focus of evaluation. That is, team members are rewarded for acquiring team-related skills, as indicated by evaluations provided by other team members. Some examples of such skills are adaptability (i.e., learning the tasks of other team members), oral communication, personal growth, problem-solving, commitment, initiation of ideas, and leadership (HRFocus, 1995). Such systems are effective in improving team performance, as they target the ways in which individual team members contribute to effective (or ineffective) team processes. A common monetary reward in this system is as follows: team members are paid 50% of their base salary until they are deemed to have learned the skills necessary to be an effective team member. When competency is demonstrated, base pay increases (Musselwhite, 1988). Alternatively, demonstrated skills and competencies may be rewarded with one-time monetary or nonmonetary rewards.

The skill development encouraged by team and team member skill incentive systems can take an enormous amount of effort and time (Gross, 1995). Thus, it has been argued that encouraging skill improvement is really only appropriate when team members will be spending substantial amounts of time within teams. In highly interdependent teams, such systems encourage members to learn each other’s tasks, thus facilitating high performance (Geber, 1995). Skill incentive systems, therefore, are most useful for full-time, permanent teams.

When team members spend little time in team roles, focusing upon skill development is likely to be unnecessary and undesirable. That is, encouraging employees to develop team skills which they will rarely use is likely to be a
waste of resources. Additionally, placing a focus on team skill development will take at least part of the team member's focus from other aspects of their job, such as achieving non-team related skills.

**Systems VI and VII: team member goal-based and merit incentive systems**

The final team incentive systems evaluate the contributions and outcomes of team members when distributing rewards. First, team member goal-based systems will be described. A team member goal-based incentive system is found at Dial, the soap manufacturer. A prototype team at Dial is composed of marketing, financial and customer service specialists, and team members are rewarded when they achieve individual goals (e.g., sales or customer service objectives) which further the team's overall performance (Bartol & Hagmann, 1992). Team member goal progress is evaluated twice a year via performance appraisal, and goals are set in conjunction with team members and supervisors.

Incentives in team member goal-based incentive systems may be monetary or nonmonetary. In the case of monetary rewards, variable pay and bonuses are most common. In the case of nonmonetary incentives, achievement awards are most common.

At Trigon, Inc., a team member merit system exists, where high performing team members earn special recognition dinners when they contribute in an exemplary manner to a team (HRMagazine, 1995). Team member merit systems are also found at Boeing's Corinth plant. Unlike team member goal-based systems, no definitive level of performance exists which ensures that a team member will receive an incentive. Instead, in team member merit incentive systems, when a team member is deemed by peer or supervisor evaluation to have made an outstanding contribution to his or her team's performance, the team member is recognized with monetary or nonmonetary rewards (Heneman & von Hippel, 1995). These rewards can take the form of salary increases, bonuses, and nonmonetary rewards (Sales and Marketing Management, 1994).

Both team member goal-based and merit incentive systems are thought to be effective for both full-time and part-time teams (Gross, 1995). With regard to part-time teams, such a system allows the organization to reinforce its emphasis on team member performance. With regard to full-time teams, such systems allow the organization to reward differential member contributions, a very common scenario when team members' tasks are somewhat independent. However, such team member incentive systems may be inappropriate for full-time teams where substantial cooperation among team members is desirable.

**Summary**

The arguments of compensation experts regarding team incentive systems are clear: team incentive systems, in some form, are generally necessary to facilitate optimal team performance (e.g., Geber, 1995; Gross, 1995; Team Pay Case Studies, 1997). Unless "teamwork" is recognized by the organization with rewards, team members will not perceive their work within teams to be valued.
by the organization. Many organizations which use teams have not accepted this argument, however, believing that team incentive systems are ineffective or unnecessary. Hence, the introduction of team incentive systems in the workplace has lagged behind the introduction of teams, with surveys finding only 20 to 35% of organizations which use teams have some form of team incentive system (HRFocus, 1993, 1994a&b; Management Services, 1996; Pastrenak, 1994).

Although many questions concerning team incentives need answering, this paper hopes to provide a starting point for researchers and practitioners alike who are interested in implementing team incentive systems or investigating ways in which their effectiveness may be improved. When examining the "guidelines" regarding the effectiveness of each of the seven types of team incentive systems presented in this paper, the reader may have become aware of some emerging themes. To date, it appears that two basic factors need to be considered when choosing a team incentive system, namely team interdependence concerns (both between and within teams) and team type (i.e., part or full-time). For example, organizations with high interdependence within full-time teams should consider implementation of team goal-based or team skill incentive systems with equal reward distributions among team members. Those with low interdependence among full-time teams might consider a team discretionary bonus system with equitable distribution among team members. These are just a few examples of systems which would be effective in different situations. Using this paper as a guide, organizations can more effectively identify and choose a team incentive system that encourages high performance.

Researchers can also use the present paper as a guide for future investigations. For example, boundary conditions for the effectiveness of different team incentive systems, other than team interdependence and team type factors, must be identified and examined. Additional factors which may affect the usefulness of different team incentive systems include: the composition of teams (e.g., same or mixed gender teams; same or mixed occupation teams, and so on); organizational context factors (e.g., type of industry, size of organization); and team pressures (e.g., time pressure, stress), to name a few. Researchers may also continue to gather evidence for the effectiveness of team incentive systems, by demonstrating the positive effects of such systems on team performance and organizational productivity. As the use of teams grows, such evidence will become increasingly important to ensure selection of an incentive system which ensures maximal team performance.

References


Further reading


HRFocus (1996a) “Team-based pay still lags teamwork”, Vol. 73 No. 1, p.15

HRFocus (1996b) "What's the payoff for variable pay?", Vol. 73 No. 1, p.15

