

## A Study on Incentive Compensation Plans in Private Organizations at Hyderabad



## Management

**KEYWORDS :** Compensation, Incentive compensation, short term & long term incentive programs, ANOVA-test.

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### ABSTRACT

*Most of the high performing organizations are taking incentive compensation plans seriously. More and more organizations are using it as a strategic tool. Especially in today's era of globalization & knowledge economy, private organizations face unique challenges when designing short-term and long-term incentive programs. The present research is to find the need of the compensation package in private organization and to find how private organizations can structure incentive plans, the survey is concentrated only on 20 private organizations at Hyderabad; the data collected in the form of Questionnaire was tabulated and analyzed using basic statistical method percentages and ANOVA-test. From the study it is found that, there is a significant difference between short-term and long-term incentive programs and incentives acts as good motivators for the employees to work better and harder but also they need competitive salaries to attract and retain work force of the organization. Based on the findings of the study, some suggestions for the private organizations has been given which can be useful in designing the compensation structure of the employees.*

### INTRODUCTION:

In today's competitive scenario organizations have to take special measures regarding compensation of the employees so that the organizations retain the valuable employees. The compensation systems have changed from traditional ones to strategic compensation systems. The compensation packages of a growing proportion of firms include pay schemes that are linked to employee or company performance. By motivating individual workers to be more efficient at work and increasing their attachment and identification with the interests of the enterprise, incentive schemes are expected to improve interpersonal relationships, raise job satisfaction, lower absenteeism and waste of intermediate material or capital, and lower turnover rates, all of which should produce lasting effect on company performance.

The compensation structure needs to be elaborated dividing it into various components to address the needs and aspirations of the employees at different hierarchical levels.

Compensation provided to employees can direct in the form of monetary benefits and/or indirect in the form of non-monetary benefits known as perks, time off, etc. Compensation does not include only salary but it is the sum total of all rewards and allowances provided to the employees in return for their services. If the compensation offered is effectively managed, it contributes to high organizational productivity.

**Direct Compensation** Direct compensation refers to monetary benefits offered and provided to employees in return of the services they provide to the organization. The monetary benefits include basic salary, house rent allowance, conveyance, leave travel allowance, medical reimbursements, special allowances, bonus, incentives, Pf/Gratuity, etc. They are given at a regular interval at a definite time.

**Indirect Compensation** Indirect compensation refers to non-monetary benefits offered and provided to employees in lieu of the services provided by them to the organization. They include Leave Policy, Overtime Policy, Car policy, Hospitalization, Insurance, Leave travel Assistance Limits, Retirement Benefits, Holiday Homes.

### RESEARCH METHODOLOGY:

Twenty-five private organizations were contacted, but only twenty of them agreed to participate in this study. (Five nonprofit and government organizations were excluded because they tend to have a lower prevalence of incentive programs and would skew the results.) Responses from 20 organizations were analyzed and have been summarized in this survey report. Responded organizations represented include business and professional services;

manufacturing; financial services and insurance; retail, wholesale and distribution; health services and high technology.

### DATA COLLECTION:

The organizations were contacted, first by e-mail and then by phone, and direct interview. Data has been collected from the concern HRs of their respective organizations regarding their short-term and long-term incentive programs.

### STATISTICAL TOOLS:

The data collected in the form of Questionnaire was tabulated and analyzed using basic statistical method percentages and ANOVA-test. For this study purposive sampling method is used.

### HYPOTHESIS:

**Null Hypothesis ( $H_0$ ):** there is no significant difference between short-term and long-term incentive programs.

**Alternative Hypothesis ( $H_1$ ):** there is a significant difference between short-term and long-term incentive programs.

### OBJECTIVES:

To know the need of the compensation package in private organization.

To know how private organizations can structure incentive plans, and suggest the incentive compensation plans which motivate the employees.

### LIMITATIONS:

The time available was adequate in collecting the required information.

The survey is concentrated only on 20 private organizations in Hyderabad.

### NEED OF COMPENSATION PACKAGE IN PRIVATE ORGANIZATIONS:

A good compensation package is important to motivate the employees to increase the organizational productivity.

Unless compensation is provided no one will come and work for the organization. Thus, compensation helps in running an organization effectively and accomplishing its goals.

Salary is just a part of the compensation system, the employees have other psychological and self-actualization needs to fulfill. Thus, compensation serves the purpose.

The most competitive compensation will help the organiza-

tion to attract and sustain the best talent. The compensation package should be as per industry standards.

#### **INCENTIVE COMPENSATION PLANS:**

Incentive programs are alive and well at companies from all different sectors. Incentive plans are designed to support organizational results by rewarding staff for achieving critical operational and programmatic goals.

#### **Forms of incentives can include:**

Cash (one-time bonus or formal incentive)

Perquisites (additional leave, professional development opportunities, etc.)

Low-cost or no-cost recognition (lunches, movie passes, employee of the quarter, certificates of appreciation, etc.)

Plans to consider:

#### **Formal "Incentive" Plan:**

Establishes clear performance objectives and target payouts at the beginning of the performance period

#### **Discretionary "Bonus" Plan:**

General guidelines are established for performance expectations

Payouts are determined by management, if funds are available, based on overall results

#### **"Spot Award" Plan:**

Periodic lump sum payments are made to recognize special accomplishments or exemplary behavior

#### **Combination Plans:**

Use of several plan types for different types of contributors to encourage broad staff involvement in priority areas.

#### **SHORT TERM INCENTIVE PROGRAM:**

Short-term incentives, which is granted upon the achievement of a certain result with in current accounting year. This includes:

**Annual Incentive Plan:** A pay plan that is designed to reward the accomplishment of specific results. Rewards usually are tied to expected results identified at the beginning of the performance cycle. In contrast to bonuses, they are not primarily discretionary but may have a discretionary component.

**Discretionary Bonus Plan:** A plan in which management determines the size of the bonus pool and the amounts to be allocated to specific individuals after a performance period. These have no predetermined formula or promises, and are not guaranteed.

**Spot Awards:** Spot awards recognize special contributions as they occur for a specific project or task. The project or task generally is accomplished in a short time period.

**Profit-Sharing Plan:** A plan providing for employee participation in the profits of an organization. The plan normally includes a predetermined and defined formula for allocating profit shares among participants, and for distributing funds accumulated under the plan. However, some plans are discretionary.

**Gain-Sharing Plans:** Any one of a number of incentive programs designed to share the results of productivity gains with

employees as a group.

**Team/Small-Group Incentives:** Any incentive program that focuses on the performance of a small group, usually a work team. These incentive programs often are used when measurable output is the result of group effort and individual contributions are difficult to separate from group effort.

**Retention Bonus:** A payment or reward outside of an employee's regular salary that is offered as an incentive to keep a key employee on the job during a particularly crucial business cycle.

**Project Bonus:** A form of additional compensation paid to an employee or department as a reward for successfully completing a specific project within a certain timeframe.

#### **LONG TERM INCENTIVE PROGRAM:**

Long-term incentives, which are means to provide cash incentives or equity for employees to improve the overall performance of the organization by linking the employees' long-term rewards to the organization's long-term results and these plans, become invalid if the employee leaves the organization before a specific period. It includes:

**Stock Option:** A contractual right granted by the company to purchase a specified number of shares of the company's stock at a specified price (the exercise price) for a specified period of time.

**Restricted Stock:** Grants of shares of the company's stock subject to restrictions on sale and risk of forfeiture until vested by continued employment.

**Phantom Stock:** A type of incentive grant in which the recipient is not issued actual shares of stock on the grant date but receives an account credited with certain number of hypothetical shares. The value of the account increases or decreases over time based on the appreciation or depreciation of the stock price and the crediting of phantom dividends. Payout may be settled in cash or stock.

**Stock Appreciation Right (SAR):** A contractual right that allows an individual to receive cash or stock of a value equal to the appreciation of the stock from grant date to the date the SAR is exercised.

**Long-Term Cash Plan:** Cash awards where payment is contingent on performance as measured against predetermined financial or strategic objectives over a multi-year period of time (typically 3 years).

**Performance Shares:** Grants of actual shares of stock with payment that is contingent on performance as measured against predetermined objectives over a multi-year period of time; same as performance units except that the value paid fluctuates with stock price changes as well as performance against objectives.

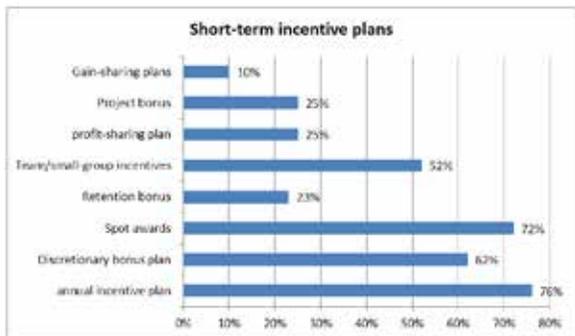
**Performance Units:** Grants of dollar-dominated units with value that is contingent on performance against predetermined objectives over a multi-year period of time. Actual payouts may be in cash or stock.

#### **DATA ANALYSIS AND INTERPRETATION:**

##### **1. short-term incentive plans**

Survey participants were asked whether they had any of the following 8 types of STI plans in their organizations, and the result is represented in a graphical form.

Fig 1: short-term incentive plans

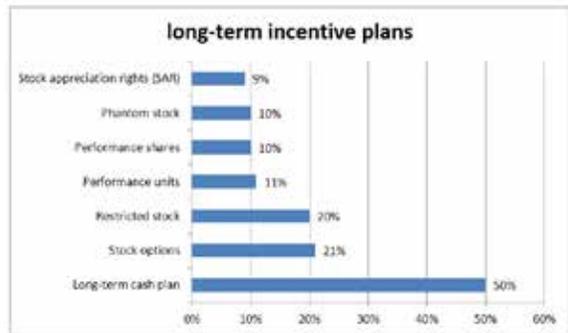


From the above figure, it is clear that most of the organizations give first priority to annual incentive plans, next priority is for spot awards and discretionary bonus plan, and the last preference is given for gain sharing plans.

**2.long-term incentive plans**

Closely-held businesses often rely heavily on a few key employees who are not owners or shareholders to perform roles critical to the company’s long-term success. A long-term incentive plan is an integral part of the compensation package, and there are many different types of plans from which to choose. Survey participants were asked whether they had any of the following 7 types of LTI plans in their organizations, and the result is represented in a graphical form.

Fig 2: long-term incentive plans



From the above figure, it is clear that most of the organizations give first priority to long-term cash plans, next priority is for stock options and restricted stock, and the last preference is given

for stock appreciation rights.

**STATISTICAL ANALYSIS:  
ONE WAY ANOVA TABLE**

Source of variation	Sum of squares	Degree of freedom	Mean sum of squares	f- ratio
Between sample	93.33	(k-1)=(2-1)=1	93.33	$f_{(1,13)}=4.8146$
Within sample	252	(n-k)=(15-2)=13	19.3846	
Total	345033	(n-1)=(15-1)=14		

f-ratio calculated value= 4.8146

f-ratio critical value for (1,13) at 5% level of significant is 4.67

Since  $f_{cal} > f_{tab}$ , we reject null hypothesis which means there is a significant difference between short-term and long-term incentive programs.

**SUGGESTIONS:**

The organizations should concentrate on the employee’s performance & productivity, and provide them incentives as a reward which boosts their morale, increase their interest on the job & create a positive image for the organization.

The organization should take care of satisfying the employees in terms of their compensation by their feedback.

The organization should also conduct surveys on compensation packages regularly in order to have up to date information of the incentives in the market and should be on par with the market so that the employees do not get disappointed or intend to switch to other companies.

**CONCLUSION:**

From the study it is found that, there is a significant difference between short-term and long-term incentive programs and incentives acts as a good motivator for the employees to work better and harder but also they need competitive salaries to attract and keep personnel. If the bonus would be removed they would have to compensate by increasing the fixed salary which would lead to an additional cost for the organization when it performs badly, as the bonus would have been nil when profit is nil.

Most of the organizations give first priority to annual incentive plans, next priority is for spot awards and discretionary bonus plan.

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