

Compensation as a Construct for Employee Motivation in Healthcare

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There is no difference between performance of those employees receiving a salary as compensation for services and those employees receiving compensation based on output by the specific employee, (Null), or alternatively, incentive compensation results in increased employee productivity. This issue has been debated historically and the debate continues. This paper reviews the issue from a historical perspective and includes contemporary research and concludes with implications for further research.

Employee motivation has been debated since the inception of management as a discipline. The Chinese bureaucracy 1000 B.C. developed a theory of management based on rewards and Punishments as a way to manage productivity. Confucius, in the period 552 B.C. through 479 B.C. advocated that employee productivity could be managed by improving morale (Wren, p. 14). In 35 A.D., the Egyptians used wage incentives to motivate workers (Lee, p. 42).

In a study completed by Mercer, incentive compensation plans increased morale and increased productivity for those plans including all employees but not for firms offering incentive pay programs to only high-ranking managers (Wall Street Journal). Whitney argues that because of prejudices on the part of executives, wage and salary programs are poorly designed and, in most companies, are not true pay-for-performance programs. Evans argues that governmental regulations in unions demanding rewards based on seniority have eroded the pay-for-performance compensation programs (Evans, p. 726). Short-term incentive plans, however, are gaining popularity in the health care industry (Hospitals). Cash incentives have increased 5% to 10% in 2008 (Evans). Bonus payments are an (integral part of compensation) in healthcare. (Healthcare Facility Management) as bonuses will increase quality of healthcare and reduce costs (Armstrong). There are no consistent policies or body of theory regarding incentive compensation programs followed and practiced by organizations. It is clear, however, that incentive compensation programs are effective in increasing productivity if properly designed for the situation or goal to be accomplished. (Haman).

One such method of incentive compensation is payment based on the profitability of the organization. Charles Babbage "On the Economy of Machinery and Manufacturer" indicated "the mode of payment could be so arranged that every person employed should drive advantage from the success of the whole; that the profits of each individual should advance as the factory itself produces profit, without the necessity of making any change in wages" (Wren, p. 61). This was seen as a way to develop a synergy between the employee goals and the company goals from an economic point of view. Whitney maintains that good performance deserves a higher pay, and therefore poor performance should result in lower pay. If an organization's profits were reduced, compensation should also be reduced. Because this is taboo in America's culture, such plans will not work (Whitney p. 36). He argues that a bonus system would be a more effective way of rewarding high performers with a reduction in this program should the

performance not be achieved. Whitney also argues that management rewards are based on power, compensation and prestige opposed to technical excellence and therefore such plans may not provide the appropriate incentives for executives to achieve the goals of the organization. If compensation is 'based upon individual performance, cooperation among team members may be inhibited, whereas if compensation is based on team objectives, individuals may not work as diligently and may lean on other team members. Bonus systems are a way to achieve both team and individual performance based on appropriate measures and evaluations. However, if profitability drops and bonuses are not given, this may result in turnover or a feeling of mistrust on the part of the employee. This works successfully in the Japanese system, however, they have a concept of lifetime employment (Whitney, Part II, p. 47). Because there is not a direct relationship between individual employee performance and compensation, the typical employee is unable to see a relationship between merit increases and his/her level of performance and therefore may not provide the incentive to increase productivity (Evans).

Another system of rewarding employees for performance is the merit system. This is a system whereby employees are evaluated based on their merit each year and given an increase based thereon. However, the typical employee is unable to see a relationship between the merit increase and his/her level of performance in most cases. Based on a study of certain Fortune 500 companies that contributed approximately 40% of the Gross National Product in the United States in 1968, "job performance is not the primary determinate of wage and salary progression for non-supervisor employees". This is true even though "93% of the firms claims that they subscribe to the merit reward philosophy by advancing wage and salaries on the basis of job performance" (Evans, p. 730). Therefore, it appears that those companies, although of the opinion that incentive wage and salary programs influence employees to produce more, do not implement such programs in such a way as to increase productivity. Studies have indicated that "there is no significant link between paid performance and common merit pay programs" (Markham, p. 172).

One system of rewarding employees is to reward departments based on departmental productivity opposed to rewarding employees based on the organization's profits. Henry R. Towne thought that profit sharing was inappropriate because it did not reward individuals for their efforts. He proposed a method of payment that would reward work units or departments for their efforts and to split productivity gains by departments; 50% to the employer and 50% to the workers (Wren, p. 91). Incentive compensation advocated by Towne was based on the thinking of See who promoted paying "higher wages to attract better workers" (Wren, p. 87). Edward Atkinson, an American economist, suggested that "the cheapest labor is the best – paid labor" (Wren, p. 90) because more productivity will result and therefore unit cost will be lower leading to the concept that higher wages led to more productivity and therefore lower unit cost.

The individual performance incentive of compensation plans are the most attractive. Frederick Taylor suggested that the piece-rate system had failed because standards were poorly set and employers would game the system by cutting rates when productivity increased. This caused inefficiency and gaming of the system by the employees. Taylor developed his differential piece-rate incentive plan system at Midvale Steel (Wren, p. 106) based on time studies and set a rate where the standard for each element was determined by the time study. "This rate moved job performance from guess work and tradition to a more rational basis. The principle of the differential rate worked two ways: it forced those who did not meet the standard or receive a low rate of pay and greatly rewarded those who did attain the standard" (Wren, p. 109). Taylor strongly opposed paying individuals based on averages of the group and therefore opposed union attempts to set quotas. He advocated that higher paid workers would be more productive and therefore lower unit cost and suggested that workers be paid "from 30% to 100% according to the nature of the work which he does, beyond the average of his class" (Wren, p. 110).

Gantt, a disciple of Taylor, also advocated incentive compensation as a way to increase employee performance. "Gantt devised his 'task work with a bonus' system that paid the worker a bonus of \$.50 per day if he did all the work assigned for a particular day" (Wren, p. 134). He modified this plan to increase productivity by increasing wages for employees for completing a job below the standard as an incentive to increase productivity. In addition, foremen would receive a bonus if the workers performed better the standard providing an incentive for the foremen to teach the workers to be more productive. Harrington

Emerson installed an individual reward system in the Burlington Railroad Company. In two years, output increased by 57%, average pay increased by 14% and the cost decreased by 36% (Wren, p. 148).

Physicians are highly motivated by compensation plans (Helman, Hemenway). Physicians' concerns should be primarily for the patient's well being, however, "physicians do appear to respond to economic stimuli occasioned by their contractual obligations to third party insurers" (Helman, p. 86). Health Maintenance Organizations (HMO) have been designed as a way to reduce health care costs by paying physicians and other health care providers based on the number of enrollees in a plan as opposed to the number or quantity of services provided to patients. Therefore, physicians, in such a plan, are paid for not rendering services. One study showed that physicians on a salary based payment showed a reduction in hospital days of 13.1% and those on a capitation basis, i.e. paid for the subscribers in the program, also showed a reduction in hospital days (Helman, p.88). The study also showed there was a higher use of primary outpatient visits that are less expensive than inpatient care for HMO physicians. Bonuses were not found to be significant in terms of productivity. "Distribution of bonuses of may lack effect because such incentives delay any reward. Physicians, like anyone else, respond to economic stimuli that are immediate rather than delayed" (Helman, p. 91). The Affordable Care Act has created Accountable Care Organizations. Organizations can apply for this program providing financial incentives to reduce health care cost through wellness programs for Medicare /Healthcare government. Also the JCAHO has provided financial incentives to reduce cost through core measures sets.

In a study of physician financial incentives in a for-profit care center, it was determined that "substantial monetary incentives based on individual performance may reduce a group of physicians to increase the intensity of their practice, even though not all of them benefit from the incentives" (Hemenway, p. 1059). Therefore, it is clear that individual incentive compensation plans, if properly designed, do result in increased productivity.

There are other factors that influence employee productivity in addition to compensation. (Whitney) Williams hypothesized that motivation for employees was based on their feelings rather than their thoughts (Wren, p. 167). He said that a person's social standing is determined by his job. He indicated that "beyond a certain point, the increased wages are quite likely to lessen as to increased effort" (Wren, p. 168). Thus, salary is a negative motivator. Over-payment will not necessarily increase productivity but under-payment will cause decreased productivity, soldiering and turnover. Continuing this socialistic viewpoint, Henry DeMan viewed that work itself was a motivator and it was management's job to remove the hindrances such inequitable wage systems that prevent workers from finding joy in work (Wren, p. 172).

Winn looked at incentive to increase sales opposed to incentives to increase net income. He hypothesized that because of "personal self interest" factors, managers tend to increase sales opposed to increase compensation based on incentives. In other words, executive salaries appear to be more closely "correlated with the scale of operations of a firm than and with their profitability (Winn).

Taylor and Gantt concepts of compensation based on individual performance including accurate and fair standards is worth further research and study.

IMPLICATIONS FOR FURTHER RESEARCH

Current research on compensation plans is sketchy and in many cases flawed. There are many factors that affect employees' motivation including political, social and economic. An attempt to isolate economic factors is difficult and the research therefore is not conclusive as to whether incentive compensation programs positively or negatively affect employee productivity. Managers have developed principals of wage and salary administration based on inadequate research and individual bias indicating that the academic community has not provided appropriate guidance for the practitioner in this area. This area is right for research and should include not only the economic factors but the social factors as barriers to implementing the programs to positively motivate employees. It is clear that unless American companies and American industry respond appropriately to a threat of international competition, it will not remain as a predominate economic power.

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