**Step by Step to Understanding & Implementing**

**Human Resources – Pay Plans**

Installation Perfromacne Based Pay Systems

**Performance Based Pay for Installation – Piece Rate Pay & Bonuses**



#### Reward systems, specifically compensation, create incentives for employees!

**Compensation does not drive behavior, but it does influence behaviors. This also depends a great deal on the individuals involved in the culture of an organization. If compensation drove behavior, all employees who needed a raise would steal from the company, and all employees would be positively motivated by compensation plans that targeted specific behavior. In reality, compensation simply supports the overall goals, and culture of performance – good or bad!**

#### Many contractors believe performance based pay is complicated, or snake oil, or that it will create *employees with ill will who will leave the company* because they do not like piece rate pay, or pay for performance. Some contractors even believe that performance based pay, or piece rate pay is only for new house, where *quality* doesn’t necessarily count as much as in retrofit install or service. These are all statements that can be true or false, so the real question becomes, is that a good thing or a bad thing?

#### The ideas above are mutually exclusive, meaning *quality, customer service, honesty and integrity* stand alone, and have nothing to do with pay plans. Under performers who leave the company because they know they are going to make less money may not be a bad thing? You can indeed have quality, exceed the customers’ expectations, and a company of highly paid performers working together to improve the profitability of the company, while making more money for themselves.

#### *Piece rate performance based pay is not a magic bullet!* If you run a poor company with bad quality, no reward system will save you. However, performance based pay will lock in your labor cost as it applies to sales, which helps you operate a more efficient and profitable company.

#### The advantages of performance based pay are numerous:

#### Piece Rate pay is an effective means of compensation based on performance

#### Piece rate pay sets the labor rate at essentially a fixed cost against the sale price, making labor management easier to maintain at the desired rate

#### Piece rate pay is a privilege and allows those who perform to make more money than those who are on hourly wages.

#### Piece rate pay can be used in Retrofit Installation, Service, and New Home construction.

#### Piece rate pay MUST have two standards that are non-negotiable

#### Integrity with the company and the customer

#### Exceed the Customers Expectations

#### The Disadvantages of performance based pay are:

1. **It is different and therefore requires change, not easily accomplished for our industry.**
2. **It requires controls on quality as a trade for speed**
3. **It requires a disciplined, zero tolerance policy on and any integrity issues.**

**Performance based pay is an excellent way to focus the company on the benchmarks that support better practices, maximum profitability, and a culture of accountability and performance.**

**This compensation system does require the contractor to maintain a zero tolerance quality and customer service standard.**

Once implemented, performance based pay becomes like any other change, it gets less controversial and more accepted as the way we do things. In fact, it would be more of a mutiny to go back to hourly pay and remove performance based pay after it has been implemented. Going back to hourly pay as a system that rewards the less productive employees, at the expense of the most productive employees would end up not making your productive employees happy due to the fact they are now making more money.

#### Performance Based and Piece Rate Pay:

#### Performance based pay systems can be either bonus driven based on some standard or goal, or be based on piece rate, meaning employee pay accompanies the completion of a specific task at a fixed pay amount.

#### An optimum system to consider is the use both methods, piece rate and performance bonuses in concert with one another, simply tying the task based pay of piece rate to the benchmark (KPI) and rewarding employees for certain productivity achievements, so long as the standards of quality and integrity are always maintained. *Quality, customer service and integrity must be 100% maintained!*

An example of this combined pay for performance system would be as follows:

Retrofit Example:

1. Installer “A” gets paid $450 for a retrofit installation of a 90% furnace
2. This same installer completes the job in 14 hours instead of the task time amount of 16 hours and even though he finishes 2 hours earlier than the task time allows, we pay the $450 for the 16 hours allowing him to start another job, or go home, or help out somewhere else.
3. This same installer has maintained his labor percentage at 9% of less at the quality and integrity standard, effectively supporting the KPI standard, supporting our desired profits!
4. The company is going to share it’s overage in profits with all employees, including installers in a form of a bonus program called “Shared Success” so that any profit beyond 15% gets driven back as bonuses to the employees, including this installer because he met his labor KPI of 9% or less. This means a 20% pretax yields a 5% bonus pool to be subdivided among the employees that met their KPI’s, creating incentive to learn the KPI’s, learn how to beat the KPI’s within the quality/integrity standards. This installer would be getting an additional “Shared Success” bonus!

This is just one example, and there are many ways to tie piece rate pay systems of compensation to a bonus system for KPI’s known to be a good business model. Why not pay for performance?

Pay for performance also has the effect of tying the function of sales to the function of production, making both areas work together to achieve success. We call this ***ALIGNMENT and it is an immensely powerful tool in a business!***

**How do we implement performance base piece rate pay?**

1. Read the law – attached link defines the laws: Remain in compliance.

<https://www.ecfr.gov/cgi-bin/text-idx?SID=c78cc0c0b5b5fc2f7457bde207ebda6c&mc=true&node=pt29.3.778&rgn=div5#se29.3.778_1103>

1. Determine the timing of your implementation. The end of an accounting period is always a good choice to implement, as is the preseason to the busy season. There is also the psychological element of implementing the pay plan. Timing is critical in both of these areas, and should be a major factor in implementation.
2. The owner or manager should develop a plan for implementation, which includes a good understanding of who may leave the company based on the new system of pay. What if some personnel do leave, do you have a labor utilization plan to deal with their absence, or is it the slower time of year anyway? You may find the fact that some leave, they were under-performers! We recommend having a 90-day grace period to pay the personnel the better of the two pay methods, so no one should leave for 90 days, until you and they see how the pay plan affects them. The under-performers will either make less money, or they will leave, or they will learn to improve their performance. Either way, the company wins, and if the employee adjusts, they win as well!
3. A thorough understanding of which installation personnel are productive for the company, and to what level. It is not essential to implementation, but these figures of gross margin per man day, labor to sales percentage in the department, will be helpful to any subsequent discussion you will have with the employee group.
4. The owner must establish the performance based pay system policies for the company:
   * + - 1. What is the guideline policy for the piece rate system?
         2. What is the base labor rate to pay your production employees?
         3. What are the standards you will use to increase this hourly base rate? Your review process?
         4. How will you handle callbacks in installation?
         5. Develop a zero tolerance honesty, integrity and customer service policy. You need an employee review board.
         6. Develop new time ticket and overtime calculation method.
5. After the policy is established, you need the time cards to be adjusted to reflect the new time and task codes to properly get the paperwork to accounting. These are still employees of the company and they still get paid for overtime should their work time exceed 40 hours in a week. This time card tracking still continues. Overtime is calculated on the base hourly rate that is assigned as part of the installers pay plan, and of course how many hours are worked beyond the 40-hour workweek.
6. The Owner is now ready to introduce the ***CONCEPT of Performance Based Piece Rate Pay*** to the employees. This is not a negotiation, but the owner should make clear, this is where we are headed, and you (the employee) can help influence the outcome. You cannot change the fact we are going to implement performance based pay, but you can help design the labor hours required to do the work, and the task times for flat rate, the hours to deal with abstract options, and also the ***quality standards*** we need to live by. You have the opportunity to develop the company standards you will be held accountable to, and we will live by.
7. Have the teams design their labor hours for the work, and their task times for the piece rate pay system of installation, including the options.
8. The accounting team or bookkeeper should run concurrent pay plans for 90 days. Meaning the company will pay the production employees the better of the two pay plans for the 1st 90 days, and after that we are 100% committed to performance based piece rate pay.
9. The owner needs a training platform established to get employees in service and installation that are NOT meeting the KPI standard, trained. If they cannot be trained well, then your labor costs went down, but in the end you most likely will lose this employee, which is NOT A BAD thing!
10. The 2nd, and final communication to the employees, and training meeting can now be held with the installation teams. Separate timing on implementation is advisable. This meeting is to roll out the time card; the guidelines, the final labor tasks and pay per task, and the dual accounting plan to remove all psychological obstacles. There will be questions, and you should have the answers.
11. It is advisable to continue weekly meetings with the production team for a period of several months, to iron out any kinks in the plan, and mostly to show continued communication with your production team. Adjust as necessary the guidelines.
12. Additionally, a reserve should be established for each technician or installer, of say 1%, to maintain a callback system for paybacks to those technicians which need to run callbacks from dispatch that are not able to be fully owned by the original technician or installer.
13. Establish an employee review council. This is a group of peers that meet and discuss the pay for performance system issues, and come to conclusions about enhancing the system. This team reviews any disputes or discrepancies, and also has the say in integrity and quality issues. Any employee that is on pay for performance knows this council is a group of their peers, and deals with any issues.

**Pay for performance is an excellent way to reward employees who are productive. It will not solve problems beyond productivity. Those are leadership issues and must be dealt with by leaders! However, pay for performance does focus the company’s most valuable asset, its employees, on the important tasks at hand – customer service, honesty, integrity, and productivity!**

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**Here is a site from the DOL that may help answer your questions**

<https://www.ecfr.gov/cgi-bin/text-idx?SID=c78cc0c0b5b5fc2f7457bde207ebda6c&mc=true&node=pt29.3.778&rgn=div5#se29.3.778_1103>Why is this Critical to Your Success?

* Performance based pay can fix your labor cost as a percent of sales helping establish benchmarks for labor to sales ratios by department.
* Performance based pay systems create an opportunity for employees to maximize their compensation, only after the company has been properly paid for it’s services.
* Performance based pay puts the company in a position to reinvest back in its most valuable asset, its employees.
* **Based pay helps you make more Profit*!***

