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Incentive Plan Design: Get This Right and You Will Kill It in 2016

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Imagine this scenario: Your employee finishes a project Friday at 3 p.m. He logs his hours and has two hours left before the weekend starts. He can either

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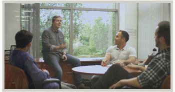

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Pearl Marketing Group Increases Utilization by 25% with Mavenlink start the next project task, or he could just charge the extra two hours to the prior project task that he's already completed.

This decision may seem inconsequential, but when multiplied across your organization, they can impact profitability

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profitability.

Here's the key to your success: What this employee does will depend probably on how you've set up his incentive plan.

Not All Incentive Plan Designs are Created Equal

The right incentive plan design gets your business its best bottom line. Typically we see two types of designs: those based on utilization or revenue.

Utilization-based incentive plans encourage employees to hit billable hours (time to client work). The downside is you may lose out on realized revenue (as in the example above, where the employee hits his marks and discontinues work revenue-generating work; he is hitting his utilization marks, but in the process he is negatively impacting revenue, margin, and client satisfaction).

Revenue-only incentive plans, on the other hand, could leave you with under-utilized resources. Or it could leave you with expensive resources working on the wrong projects. In the same example as before, an employee whose performance is based on revenue will probably start the next project.

So, after years of trying both utilization and revenue driven plans, I finally found the ideal balance. Here is the incentive plan design I've found that works.

To Hit Your Margin, Set Both Utilization and Revenue Goals

In professional services, there is one metric that matters above all: margin. We want to maximize revenue generation while improving margins. So in my department, we rolled out an incentive plan that measured both.

At our annual services kickoff, we explained that employees would have two targets: revenue and utilization. We saw good signs instantly.

To hit utilization goals, our billable employees started proactively sending out emails stating the number of extra hours they had to lend to other projects that week. We included a measure that let employees give hours to teams that weren't theirs, even globally. So Billable Bill in Utah could give five hours to our team in London. Bill would hit his utilization goals, London's team would hit its revenue goals, and the whole company would see benefits.

In just that first year, our revenue went up by 15 percent and our utilization rates rose by five percent.

"You can increase revenue by $1M just by getting 1 more hour out of each billable employee per week." — Chris Scalia, SVP Services

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So what does this mean for you? I calculate that if you run a services team of 100 people and realize an average bill rate of $200 per hour, you can increase revenue by $1M -- just by getting one more billable hour out of every employee per week.

Keep in mind that no one has to stay at the office longer. Billable Bill goes home on time; he just worked one extra billable (i.e., revenue-generating) hour while he was there, and the company saw massive gains.

And it's all thanks to that incentive plan for resources.

What About Margins? Introduce MBOs for Managers

Your managers ensure their resources hit utilization goals and revenue generation targets. Yet they are also concerned about margins. That's because your managers care more about the costs -- how they are delivering services. This introduces some questions.

Does a manager's team have the right mix of expertise?

Is the manager leveraging subcontractors to help scale up or down based on demand?

Is there an offshore component to a manager’s delivery process and capacity?

By using margins as part of the manager’s incentive plan, you ensure your leaders are thinking about these questions, so they will implement the most cost effective and efficient delivery capabilities.

In our pilot incentive plan, we therefore also included a management by objective (MBO) plan for our managers. For instance, one of our MBOs was the sales of services packages, which in our industry would help ensure our clients’ success with our solution. As a result of this MBO, we saw a revenue boost.

Typically, one significant MBO goal per quarter will help you drive the progress you need in order to continue to up-level your organization and team.

Things to Keep in Mind about Your Incentive Plan

It's important to set realistic goals. In fact, before we landed on this joint-incentive model, we kept telling ourselves that no plan would be perfect. However, we knew that if we motivated our employees with attainable goals, they would actually exceed our business objectives. As a result, we saw continuous improvements.

We also understood the importance of a feedback loop. This could be a dashboard, an automated email with targeted and actual performance metrics, or direct managerial feedback (e.g., a monthly services "all hands" meeting). The important thing is that billable resources have direct, regular access to their performance, so nothing comes as a surprise at the end of the quarter. They need an easy-to-understand plan with clear visibility into how they are performing, so they have the motivation and empowerment to improve their performance — before a semi-annual review.

Coming Full Circle: Additional Gains

In the years we initiated this incentive plan, we exceeded our margin goals. A tertiary benefit of this is that we had additional funds to explore further opportunities.

Specifically, we were able to take a portion of our additional profit and reinvest in our employees. When we set a goal for 20 percent net margins and hit 25-30 percent instead, we took a portion of the extra profit and invested in tools and technologies to help our team become even more efficient.

We more than drove profit. We fed constant performance improvement, employee retention, and client satisfaction.

That's the value of a joint incentive plan.

What kind of incentive plan do you use and why? Let me know in the comments section!

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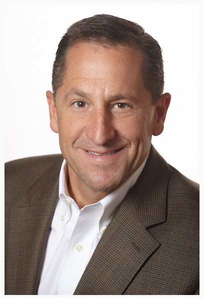

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