

Bonus Schemes and Performance Related Pay

Chapter 15

Terms of Reference

15.1 The Terms of Reference (ToR) of the Commission mandate that it examines the existing schemes for payment of bonus and their impact on performance and productivity. The Commission is also expected to provide recommendations on the general principles, financial parameters and conditions for an appropriate incentive scheme to reward excellence in productivity, performance and integrity.

Earlier Efforts

15.2 The concept of Performance Related Pay has emerged over the past three Central Pay Commissions (CPCs). The IV CPC recommended variable increments for rewarding better performance. The V CPC signalled its intent to establish a performance-linked pay component to the civil service pay structure. The VI CPC went further to recommend a framework for Performance Related Incentive Scheme.

15.3 The Second Administrative Reforms Commission (2ARC), while suggesting that performance appraisal system is a prerequisite for an effective governance system, recommended development of a strong job specific employee appraisal system, and annual performance agreements.

Details of the VI CPC Recommendations

15.4 The VI CPC provided the broad contours of a Performance Related Incentive Scheme (PRIS). Department of Personnel and Training (DoPT), as the nodal body, proposed a variable pay component to be awarded annually based on performance. The incentives as proposed were to be available both at the individual level as well at the team/group levels. The key elements of the PRIS guidelines, arising from the VI CPC, were:

- **Coverage:** The Scheme proposed to cover employees in those departments that fulfilled the following eligibility criteria:
 - Had consistently prepared a Results Framework Document (RFD) for two preceding years, and, had received a rating of 70 percent or higher in delivering the goals set in the RFD;
 - Achieved 'efforted' cost savings from the budgeted non-plan expenditure;
 - Implemented bio-metric access control system in its offices to ensure punctuality and attendance of officials;
 - Developed a Divisional Performance Measurement System, i.e., Divisional RFDs for evaluating the performance of individual divisions;

- Designed incentive scheme for categories of employees below the level of Joint Secretaries.
- **Delegation:** It granted flexibility to departments to design incentive schemes for employees below the level of the Joint Secretary.
- **Financing the Scheme:** The performance awards were required to be revenue neutral and had to be funded out of savings generated by the individual departments. The quantum of performance award was linked to the savings achieved by the department.
- **Voluntary:** The PRIS scheme was voluntary for ministries and departments as it was expected that its implementation might be easier for some departments which had clear, quantifiable targets.

Limitations of PRIS Guidelines

15.5 During the consultations for operationalizing PRIS, several issues arose, which included the funding of the incentive, the difficulty in implementing the Scheme as also administrative and implementation challenges.

- **Financing of the Scheme Considered not Feasible:** The Scheme was meant to be budget neutral and was to be funded through savings by the departments. However, it was difficult to define 'efforted' savings. It was pointed out that the size and budget of departments would differ significantly, making the implementation of the scheme easier for some departments compared to others. The fear/ apprehension of inflating the budget so as to effect greater savings, was also very real.
- **No Estimate of the Financial Implication:** It was pointed out that there was no estimate of the financial implications. The guidelines proposed that 15 percent of the projected non plan savings could be utilised for incentives. But whether this would be adequate for providing these incentives across the departments remained uncertain.
- **Problems of High Achievers in an Ineligible Division:** The introduction of PRIS in some divisions within a department could potentially exclude high performing individuals from an ineligible division, leading to their demoralization and demotivation.
- **Consultation with Stakeholders was Considered Important:** The system of Performance Linked Bonus (PLB) and Ad hoc Bonus have been prevalent in the Central Government for a fairly long time. Therefore, for the replacement of the existing bonus schemes with any other incentive scheme, prior consultation with the stakeholders was considered essential.

15.6 The Commission notes that while the PRIS emerging out of the VI CPC recommendation was comprehensive, there were a number of factors which resulted in a very limited uptake of the scheme. In the first place, the Scheme was voluntary. It was not binding on the departments. Secondly, the Scheme was dependent on savings generated by the departments. This was seen as a fundamental flaw of the proposed framework by a number of departments. Thirdly, without a credible performance measurement methodology, the scheme was difficult to operationalize. Finally, the RFD which had just been introduced in the Central Government was yet to take roots. It could, therefore, not be used as an anchor for the Scheme. For these

and a number of other reasons, PRIS was not operationalized by the departments. It was implemented in a modified way in the Department of Atomic Energy and Department of Space.

PRIS in Department of Atomic Energy and Department of Space

15.7 The Commission notes that as a pilot measure, the government approved the implementation of the PRIS in the Department of Atomic Energy (DAE) and Department of Space (DoS). While the general scheme of PRIS, as recommended by VI CPC, proposed that the performance awards be financed from budgetary savings of the concerned department, PRIS as implemented in Atomic Energy and Space is independent of budgetary savings. Payable as a cash incentive, PRIS in these two departments is non-additive and non-cumulative. Details of the scheme implemented in these two departments have been reflected in Chapter 11.2.

Bonus Schemes in the Central Government

15.8 Apart from DAE/DoS, there are bonus payments to Group 'B' (non-gazetted) and Group 'C' Central Government employees. The bulk of these employees are covered under the Productivity Linked Bonus (PLB) Scheme, which is implemented in Railways, Posts and Telecommunications, production units under the Ministry of Defence and other establishments.

15.9 The functioning of the PLB Scheme was reviewed in 1982-83 by a Group of officers. The Group of officers also considered the demands for grant of bonus made by those Central Government employees who were not covered by the PLB Scheme. The Group suggested evolution of a productivity linked bonus scheme for Central Government employees as a whole. Based on the recommendations of the Group, and pending evolution of a single scheme of bonus for employees, an Adhoc Bonus Scheme was evolved and the remaining employees, who were not covered by the PLB Scheme, were allowed ex-gratia payment. The Commission notes that the financial outgo on these two bonus schemes stood at ₹1847.08 crore for the year 2013-14.

15.10 These Bonus schemes have no clear, quantifiable targets and performance evaluation of any individual, therefore, is not possible in an objective fashion. The Commission notes that Ministry of Finance has been insisting on revision of the PLB Scheme. It has been suggested, inter-alia, that the PLB scheme should be on the basis of an input-output ratio, should be based on productivity and profitability and that productivity should be assessed on financial parameters based on profitability of the organisation.

15.11 The VI CPC too had recommended that all departments should ultimately replace the existing PLB Schemes with PRIS. The VI CPC further opined that in places where PLB is applicable and it is not found feasible to implement PRIS immediately, the existing PLB schemes may be continued in a modified manner where the formula for computing the bonus has a direct nexus with the increased profitability/productivity under well-defined financial parameters.

15.12 The Commission notes that since PRIS could not be implemented, it could not supplant the existing system of Performance Linked and Adhoc Bonus Schemes.

Analysis

15.13 Pay flexibility reforms are not a silver bullet, and involve trade-offs and risks. A study of the literature on the subject reveals that employee motivation and performance are not exclusively linked to Performance Related Pay (PRP) which may only enforce temporary compliance.

15.14 The Commission notes that it may be relatively easier to implement PRP in private sector organizations which are, generally speaking, guided by profit motives. Targets, thus, are often based on quantitative criteria making the assessment of performances easier. In the governmental context, on the other hand, the targets are more in the nature of social and public goods. These may not necessarily be tangible and discernible within a stipulated period. Proportioning credit for such a larger public good amongst various departments may not be possible so as to reward some and leave out others. There may be genuine difficulties in separating individuals from the collective, in terms of contribution made towards achieving results. The problem of PRP degenerating into routine entitlements also needs to be reckoned with.

15.15 Despite the potential difficulties with PRP, recognition for good effort and achievement through an incentive can, over time, energize the bureaucratic culture of the civil service into one that is focused on meeting citizens' and the government's expectations for speedy and efficient delivery of services.

International Experience

15.16 Countries that have made considerable progress on PRIS have managed these risks in a variety of ways. The successful ones have tried to develop objective criteria for results; several have improved the appraisal system and framework as a prior step. A few have linked PRP with a results based management system. Some countries follow a differentiated approach where an extensive and sophisticated framework is applied for senior civil service levels, while a simple results based approach is applied at the lower levels.

15.17 Many OECD and non- OECD countries have introduced PRP for their civil service. There is significant diversity in the design, coverage and implementation of their PRP schemes across countries. OECD countries such as UK, Australia, Canada, and Netherlands have considerable experience in operating PRP across their civil service, with a more nuanced one for senior civil servants. Korea, Chile, Malaysia and Philippines have implemented PRP in their civil services and have considerable experience in using this as a tool for boosting performance and accountability. Evidence from these countries indicates that pay flexibility contributes to management improvements, promotes an atmosphere of dialogue, rewards teamwork and is helpful in efficient task allocation. In Brazil and Indonesia, PRP has contributed to reducing staff absenteeism. They have also provided managers with the tools with which to redress and discipline poor performers.

Guiding principles

15.18 Any attempt to implement PRP in a governmental framework has to be preceded by proper understanding of the system, adequate planning and capacity building at various levels. The Commission feels that given the enormous size of the government and the wide diversity in the basic structures, sizes and patterns that are observed across ministries/departments/Divisions, it would be erroneous to recommend a one-size-fits-all model for PRP. The Commission is of the view that prescribing any particular model for PRP may not be sustainable. Ministries and departments should be given enough flexibility to design individual models suiting to their requirements.

15.19 The Commission would prescribe some broad guidelines:

- a. **Simple Design:** Performance Related Pay system must be simple, transparent and easy to implement.
- b. **Smart and Effective:** Performance Related Pay must be smart and should be effective in rewarding excellence and in managing poor performers in a targeted manner.
- c. **Consistent Across Departments:** PRP framework should be consistent across departments with enough autonomy to design context specific criteria, targets and indicators.
- d. **Non-additive Cash Increment:** The award for high performers may be a non-additive cash component of their current pay, given at the end of the financial year as one time incentive for the particular period.
- e. **No Linkage with Saving:** The monetary incentive should not be linked to savings.
- f. **Training:** Proper training and capacity building of the stakeholders is a must before launching PRP.

15.20 In addition to the guidelines suggested above, the Commission notes that introduction of Performance Related Pay should be done keeping in mind two important aspects. **First**, need to evolve proper criteria to measure performance along with setting a context where individual and organizational goals are clearly aligned, and **Second**, need to devise a performance appraisal system in which the objectives of the appraisal system match with that of the reward system.

15.21 The Commission opines that the Results Framework Document (RFD) can be used as the primary assessment tool for linking the targets of the organization with that of the individuals. Suitable changes in the existing Annual Performance Appraisal Report (APAR) can provide the necessary linkage between the targets of the appraisal system with those of the RFD document.

RFD: the Primary Assessment Tool

15.22 The 2ARC had recommended that annual performance agreements should be signed between the Departmental Minister and the Secretary of that Ministry/Head of department, providing physical and verifiable details of the work to be done during the financial year. The government accepted this recommendation in 2009 and put in the place the system of Results

Framework Documents (RFD) - consisting of a vision, mission, objectives, functions, inter se priorities among key objectives, success indicators and targets of a ministry/department - for evaluating and monitoring departmental performance. RFDs are being used as the primary assessment tool to measure performance of departments.

15.23 The Commission notes that the PRIS Guidelines based on VI CPC recommendations also based the performance measurement methodology on the RFD system. However, at that time, the RFD system was still being put in place and many departments were still adopting this system. The RFD system has taken firm roots now and has emerged as a powerful tool for evaluation of actual achievements of a department against annual targets. The Commission notes that presently 72 Central Government ministries/departments are implementing RFDs. This Commission is of the view that the RFD system can be harnessed as an anchor for PRP. It can provide the platform through which organizational and individual targets can be clearly aligned.

15.24 The financial rewards should be linked with the performance rating under the RFD, to be undertaken by independent experts, as is done under the MoU system for central public sector enterprises.

Linking RFD with APAR

15.25 The Commission observes that it is essential to have a linkage between Departmental RFD and APAR. The APAR methodology should be consistent with that for Performance pay. The Commission, however, notes that the performance evaluation methodology embedded in APAR system has some limitations. Some of the prominent limitations are:

- Lack of Linkage between Individual and Organizational Performance.
- Lack of prioritization: the activities in the APAR are not ranked on the basis of their importance.
- No ex-ante agreement on the targets.
- APAR is highly subjective.
- Emphasis on personality rather than results.

15.26 The Commission suggests the following modifications in the existing APAR system so that it can be used as another anchor for determining Performance Related Pay:

- A. **Alignment of Objectives:** At present, the linkage between individual and organizational performance is not clearly aligned in the APAR. The current APAR focuses more on the individual's performance compared to organizational performance. This results in a situation where individual officer can be rated excellent while the rating of the department could be lower. This is an anomaly which needs to be corrected. Conceptually, the Ministry's Vision/Mission needs to be translated into a set of strategic objectives for each department and these objectives need to be cascaded by the Department Head to his subordinates and subsequently down the chain.
- B. **Prioritizing Objectives, Assigning Success Indicators and their Weights:** Objectives reflected in the APAR should be prioritized and assigned weights along with success indicators or Key Performance Indicators (KPIs). This is required for evaluation of the

KPIs in the end. The current PAR system assigns 60 percent weight on personal attributes and functional competencies and only 40 percent weight to work output. It would be useful to devise the performance framework in such a way that it captures all the KPIs in a holistic manner: on work output, effectiveness of process adherence, management of tasks, other competencies—behavioral/leadership/functional. **The Commission recommends 60 percent weight on work output and 40 percent weight on personal attributes.**

- C. **No Ex-ante Agreement:** The indicators in the APAR of an officer/staff will need to be discussed and set with the supervisor at the beginning of the year. This will set the agenda for performance assessment on scientific lines, obviate the possibility of gaming during target setting exercise and facilitate midcourse correction, in case of requirement, in a transparent manner.
- D. **Timelines:** The Commission notes that timelines have been prescribed for drafting, reviewing and finalizing RFDs. The Commission recommends that these timelines may be synchronized with the preparation of the APAR so that the targets set under RFD get reflected in individual APARs in a seamless manner.
- E. **Online APAR System:** The Commission notes that 'Smart Performance Appraisal Report Recording Online Window' has been introduced for IAS Officers. Such a system ensures adherence to the prescribed timelines in filling up the APARs. The Commission recommends introduction of such online APARs systems for all Central Government officers/employees.

Conclusion

15.27 The Commission feels that any Performance Related Pay (PRP) for Central Government employees should provide a credible framework to drive performance across ministries/departments. Rather than a new system design, the favoured approach should be an incremental adaptation which can operate within the existing framework of rules with minor changes that can enable smooth implementation and operationalization of PRP.

15.28 In this backdrop, the Commission recommends introduction of the Performance Related Pay for all categories of Central Government employees, based on quality RFDs, reformed APARs and broad Guidelines, as enumerated above.

15.29 The Commission also recommends that the PRP should subsume the existing Bonus schemes. The Commission notes that there could be a time lag in implementing the Performance Related Pay by different departments. Till such time, the existing Bonus Schemes should be reviewed and linked with increased profitability/productivity under well-defined financial parameters