

# **Evaluating PRP - A case study of Thames Water.**

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**PhD Thesis**

**London School of Economics**

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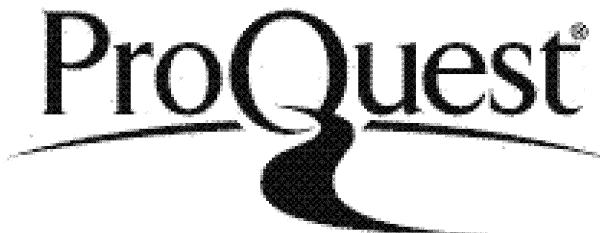
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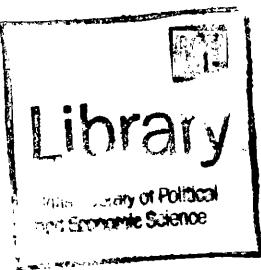
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## **ABSTRACT**

Performance Related Pay (PRP) explicitly links the level of pay an employee receives to that employee's performance. Intuitively, it would appear likely that employees would increase their work effort in order to maximise their earnings from PRP. However, there is now a substantial body of research evidence, which suggests that PRP is not particularly effective in increasing employee motivation in practice. Despite this research evidence, PRP continues to remain popular as a payment system amongst firms.

This Thesis uses a case study of Thames Water, a large utility company, to examine the paradox between the continuing popularity of PRP and its apparent ineffectiveness as a tool for increasing employee motivation. Evidence from an employee survey and interviews with key managers, together with information from internal company documentation, is brought together to explore five related questions:

- Why did Thames Water use PRP?
- How effective has PRP been in Thames Water as a motivator for employees?
- Why was PRP not more effective as a motivator for employees?
- How effective was PRP in delivering the other objectives it was originally intended to achieve?
- Why does Thames Water continue to use PRP?

The analytical approach adopted, using three theories of motivation as a framework against which to examine the motivational effectiveness of PRP, provides a new way of looking at the possible limitations on the motivational effect of PRP. This thesis touches on the question of whether and how PRP brings about cultural change; this in turn raises complex questions of causation, which call into question the effectiveness of PRP as a mechanism for bringing about cultural change.

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## Chapter 1

### The Puzzle of Performance Related Pay.

#### Introduction.

'Performance-related pay in the UK is a puzzle. There is overwhelming scepticism about its effects on performance, yet its progress seems unstoppable.'

The Financial Times (3/11/93)

Performance Related Pay (PRP) continues to be something of a puzzle. On the face of it, relating pay to performance would seem to be an effective way of motivating workers to work harder. Intuitively it might be assumed that workers would increase their work effort in order to increase their pay. ACAS (2003) in their guidance on pay systems put it quite simply:

"... the prospect of higher pay for increased output/quality often provides an incentive and many (incentive pay) schemes are introduced in the clear expectation that performance will thereby be improved."

It is therefore natural that managers should introduce PRP with increased employee motivation as a key objective (Kessler 1994, 2000 and Thompson & Milsome 2001). From a theoretical perspective, expectancy theory would seem to provide explicit support for PRP as a motivator, by

predicting employees will work harder to achieve an additional performance payment in the right circumstances.

Research, however, has shown that PRP is often not particularly effective at motivating workers (Thompson 1993, Marsden & Richardson 1994 and Marsden & French 1997). Nevertheless, PRP continues to be a popular mechanism for rewarding employees (Choat 1997 and Thompson & Milsome 2001). So it would seem, paradoxically, that a system of reward that at face value appears to be principally concerned with motivating employees to work harder, often turns out to be fairly ineffective as a motivator, and yet still remains generally popular with employers.

This thesis uses a case study of PRP in Thames Water to examine the paradox of the continuing popularity in the face of the evidence that PRP is not a particularly good motivator, by exploring five questions:

- Why did Thames Water introduce PRP?
- How effective has PRP been in Thames Water as a motivator for employees?
- Why was PRP not more effective as a motivator for employees?
- How effective was PRP in delivering the other objectives it was originally intended to achieve?
- Why does Thames Water continue to use PRP?

Each of these questions raises further issues in relation to the use of PRP

both to motivate staff and achieve other objectives. These other issues can be summarised as follows.

### Why did Thames Water introduce PRP?

Using qualitative evidence from structured interviews with those involved with the decision to introduce PRP and contemporary documentation it is possible to put together the original rationale for the introduction of PRP by Thames Water. The literature on pay and PRP, in particular, has highlighted three questions that may help shed some further light on the introduction of PRP by Thames Water and help place it in a wider context. Did PRP form part of some overall pay strategy? Was PRP part of a Performance Management strategy? Finally, to what extent was PRP part of a strategy for bringing about cultural change within Thames Water?

There is a debate in the literature about pay as to whether or not there is a new approach to pay emerging, sometimes termed 'new pay'; this is not about the introduction of a new pay system, but is concerned with the way in which pay fits with business strategy and organisational change (Kessler 2000). This thesis looks at how far the introduction of PRP fitted into Thames Water's other strategic and organisational goals. Thames Water undoubtedly had a number of objectives that they hoped to realise through the introduction of PRP. The extent to which different

objectives were articulated when PRP was introduced and the consistency and degree to which those objectives fit together and support each other, as well as the wider business strategy, is also clearly important to understanding how far the introduction of PRP in Thames Water can be said to be part of a strategic approach to pay or 'new pay'.

Performance Management has also played a part in respect of both the introduction and continued use of PRP in Thames Water. Performance Management can be viewed as an attempt to align individual performance objectives with wider organisational objectives, although the concept still maintains a degree of ambiguity (Bach 2000). PRP is not essential to Performance Management. Hendry et al. (2000) have criticised the use of PRP in Performance Management, terming it the 'dark side' of Performance Management, because it emphasises the controlling rather than the developmental aspects of Performance Management. Nevertheless, the ability to cascade organisational objectives and reward their achievement, through PRP, has in practice meant that PRP is widely associated with Performance Management.

Looked at from the perspective of PRP, it is Performance Management that ensures that PRP engages with the wider organisational issues necessary for PRP to bring about greater employee commitment and cultural change. In Thames Water PRP was intended to ensure managers and employees took responsibility for organisational

performance by getting them to focus on issues of performance management through the performance appraisal system. The question then is was the use of PRP in Performance Management part of an overall strategy or simply just another justification for adopting PRP? It is hypothesised that PRP will have been an essential part of the move of Thames Water from the public sector, as a nationalised industry, into the more commercially focused private sector, as suggested by Kessler and Purcell (1992).

#### How effective has PRP in Thames Water as a motivator for employees?

PRP explicitly focuses on performance it therefore seems pertinent to ask how far PRP can be said to improve performance. The evidence, as already noted, is that while managers by and large think that PRP acts as a motivator for employees, when you ask employees, they report not being motivated by PRP. Indeed the apparent ineffectiveness of PRP as a motivator has often been used as a point of departure for a critical analysis of PRP (Bevan and Thompson 1991, Thompson 1993, Marsden and Richardson 1994, and Marsden and French 1997). Kessler (2000) has observed that much of the evidence about the motivational ineffectiveness of PRP comes from the public sector where there are constraints regarding the nature of the workforce and the nature of the organisation which make it less likely that PRP will be an effective motivator. It is perhaps worth noting that this study looks at the

motivational effectiveness of PRP in a newly privatised company where many of the constraints that apply to the public sector do not apply. Irrespective of any constraints, the explicit link between pay and performance in PRP begs the question of whether that link has a causal effect on performance, or whether pay is simply being distributed contingent on levels of performance that would have been achieved irrespective of the use of performance payments.

It could be argued that if PRP is used to achieve a number of different organisational objectives it is not particularly important to know whether or not PRP increases employee motivation. Nevertheless, whether or not PRP is introduced with the objective, wholly or in part, of increasing employee motivation, the extent to which PRP is motivating employees is still an important issue in terms of the overall performance of the firm. If PRP is not motivating employees, then there is a danger that it may actually be de-motivating employees (Marsden and Richardson 1994). It is also argued in this thesis that PRP is more likely to be an effective mechanism for bringing about a positive change in organisational culture and as a tool for Performance Management, where it is successful in its own terms, that is to say where it motivates employees.

An attitude survey of the white-collar employees of Thames Water in receipt of PRP was conducted in 1995. On the face of it this survey provides the best evidence in a field setting of the additional effort

employees are prepared to make in return for the prospect of obtaining a performance payment. The problem with measuring actual performance in order to gauge motivation in a field setting is that performance is dependent on numerous other variables such as ability and environmental factors. Equally the employer's assessment of individual effort may be tainted by prior commitment (Brody, Frank & Kowalzyk 2001) or other considerations (Harris 2001). Therefore the simplest and most direct way of assessing motivation is to ask those whose motivation is being assessed. To put it another way:

'It is the fish who decide what is bait not the fisherman. We need to ask the fish what they would prefer to nibble on.'

(Derek Robinson quoted at p. 55 in Hendry et al 2000)

The results of that survey have been used to assess the motivational effectiveness of the Thames Water PRP scheme and also to explore why the Thames Water PRP scheme was not more effective in motivating employees.

### Why was PRP not more effective as a motivator for employees?

If much of the criticism of PRP relates to its lack of motivational effectiveness, one has to ask why PRP fails to motivate employees to work harder. Common sense would suggest that workers should improve their performance if that will lead to an increase in their earnings. Consequently, it is not immediately apparent why research has shown that PRP is not always effective as a motivator. One view would be that

it is simply a question of implementation and that if PRP were implemented in the correct way then it would be an effective motivator. Lawler (1981) says that for PRP to work the rewards must be important, capable of being varied in line with validly measured performance, where there are high levels of trust between employees and managers and employees accept the PRP scheme. Kessler (1994) has identified three elements in PRP which present problems of implementation; establishing performance criteria, assessing whether those criteria have been met or not, and the linkage between the criteria and the pay award.

However it may not simply be a case of changing the scheme to match the prescription for improvement. Marsden and Richardson (1994) found that there were deficiencies in the implementation of the Inland Revenue PRP scheme that tended to undermine its potential effectiveness. The Revenue changed the scheme in certain important respects following this research, but research by Marsden and French (1997) after the new scheme was implemented found that employees were still not motivated by PRP, the researchers suggested that the essential problem was the workers' lack of trust in both the scheme and the way that it was managed.

The revised Revenue PRP scheme built in a number of features, which reflected the principal theories of work motivation, namely expectancy theory, goal setting theory and equity theory (Marsden and French 1997).

This thesis is based on the general hypothesis that by applying theories of work motivation to a particular PRP scheme it should be possible to get a better understanding of why that PRP scheme is failing to act as a motivator for employees. This gives a framework within which to examine issues such as employee trust, which it is suggested is a critical element in PRP, both from the point of motivational effectiveness of PRP and also because PRP may actively undermine trust.

One of the first steps has been to identify those theories of motivation that seem most likely to explain the motivational effectiveness of PRP. Looking at the literature the three theories that have been identified as most relevant to PRP, are those Marsden and French (1997) refer to, namely expectancy theory, goal setting theory, and equity theory. Some commentators (Kanfer and Ackerman 1989, and Kanfer 1990) have attempted to build an overall theory of motivation, which encompasses all three theories. However that approach has been rejected, as it is argued in this thesis that goal setting theory and expectancy theory are essentially measuring different motivational drivers.

Looked at individually, each of the three theories of motivation highlights a different aspect of PRP. So that while goal setting theory and expectancy theory both emphasise the importance of the goal setting process, in goal setting theory the emphasis is on the specificity and difficulty of the goal, while in expectancy theory the emphasis is on the

nature of the reward and the link between goal achievement and reward. Potentially, this distinction between goal setting and expectancy theory offers the intriguing prospect that it is the goal setting process that is motivating employees rather than ability to earn a performance payment. If the performance payment really makes no difference to the motivational effectiveness of PRP, then PRP really needs to be judged on its other supposed benefits.

Equity theory on the other hand is concerned with the impact of the wider group on motivation, and this highlights issues such as procedural and distributive fairness. Equity theory predicts that individuals will take action to balance any perceived imbalance in their effort reward ratio compared to the effort reward ratio of comparator groups, but without specifying how the individual will bring about a re-balancing. Individuals may respond to perceived inequity through a range of reactions including increased or decreased motivation and cognitive dissonance. Consequently while equity theory may help to explain improved motivation in some cases, in others where employees feel hard done by and unfairly treated, it suggests that they may become disillusioned with the firm or even reduce their efforts at work. Thus by using these three theories of motivation as a framework of analysis against which to examine the motivational effectiveness of the Thames Water PRP scheme it is possible to highlight those areas of the scheme that are most important in relation to employee motivation.

## How effective was PRP in delivering the other objectives it was originally intended to achieve?

PRP outcomes are assessed against the original rationale for introducing PRP and the rationale for its continued use. PRP is like any other business tool; its value depends on its cost ratio benefit. Consequently it is perfectly feasible that PRP can fail to motivate employees and yet at the same time present a real benefit to the business. Looking at Thames Water, if for instance PRP is intended to motivate employees and bring about a change in organisational culture, then Thames Water may still feel that it is a worthwhile investment even if it fails to motivate most employees, provided it brings about the desired change in organisational culture. Nevertheless cost benefit may be difficult to measure without knowing precisely what value Thames Water puts on the benefits they derive from PRP. Even though Thames Water have used employee surveys to ask about employee views on PRP and have recently undertaken a review of their reward structure, the continued use of PRP has been taken as a given and there is no evidence of a complete review of its effectiveness. Most employers do not review the effectiveness of their PRP schemes (Cannell & Wood 1992).

Therefore it seems appropriate to ask not just about the benefits of PRP for Thames Water, but also to attempt to weigh those benefits against

those outcomes that can be seen as negative from the organisations point of view. Likewise the consistency of the original objectives and the extent to which those objectives are undermined by any unintended outcomes from PRP are important factors in weighing the success of PRP within Thames Water.

### Why does Thames Water continue to use PRP?

Finally why does Thames Water continue to use PRP? This question goes to the centre of the paradox about the continued use of PRP despite evidence that it is not particularly effective. The original reasons for the introduction of PRP may no longer be relevant or time may have proved them less compelling. How would Thames Water justify PRP some years after its original introduction? As already noted a current review of the Thames Water reward strategy contains no proposals to do away with PRP. What is the continuing attraction of PRP for Thames Water? Is PRP seen as the least bad option in terms of pay? Does it have iconic value, marking the company as a commercially focused organisation? Or does the payment of PRP to all employees help to justify larger much more substantial performance bonuses higher up the organisation? These issues have been explored through a structured interview with the current European Director of Human Resources.

## A case study approach.

Thames Water has been used as a case study partly because of its size; it is the largest water company in the UK and has introduced PRP for a substantial part of its workforce. At the time it introduced PRP Thames Water was publicly quoted on the stock exchange (it was subsequently purchased by the German RWE Group), which meant that there was a substantial amount of information about the company in the public domain. Also as a Water and Sewerage Company, it had been in public ownership until 1989, when the then Conservative government led by Margaret Thatcher privatised it. Water and Sewerage Companies are concerned with maintaining a secure and safe water supply and sewerage system. Privatisation posed a new challenge for the Companies to become commercially focused, so that they could meet their obligations to their shareholders and raise money in the market at advantageous rates. Thames Water under the Chairmanship of Roy Watts was in the forefront of water privatisation, anticipating the new freedom of operating in the private sector by, for instance, being the first water company to withdraw from national pay bargaining. Consequently Thames Water seemed to be an interesting case study, not only because of its size and the availability of information, but also because it was undergoing a process of change not unlike that being experienced by a number of Nationalised Industries which were privatised by the Thatcher Government making a change in organisational culture arguably very

desirable (Kessler & Purcell 1992).

Ideally, qualitative research would have been conducted with Thames Water in order to identify the key issues before any quantitative research was undertaken. However, there were problems over access for research, which may well initially have been exacerbated because the author is a full time trade union official. A number of different companies were approached all of them in the private sector, because the original intention was to examine a private sector company that was free of the sort of political constraints that apply in the public sector. After all, if the reason for introducing PRP is simply political, and there are political pressures in the public sector to use PRP, any discussion about the motivational effectiveness or overall cost benefit becomes otiose or at best less pertinent. At least one of the private companies approached, London Electricity, specifically said that they would not want to give access to a trade union official. In the end, research access to Thames Water employees was gained with the assistance of UNISON at the beginning of 1995, Thames Water initially refused to cooperate with the research. This necessarily limited the qualitative research that it was possible to carry out, to a trade union view of why Thames Water had introduced PRP, and a few published documents. From the point of view of quantitative research a survey of UNISON white-collar worker members employed by Thames Water in its utility business was conducted in May 1995 and that survey forms part of the core research

for this thesis. Subsequently, in 1999 Thames Water agreed to co-operate with the research paradoxically after the author became the principal trade union negotiator for the trade unions in Thames Water. This allowed greater access to material about the PRP scheme and the reasons for its introduction. The author was able to conduct qualitative research with some of the key players from the company's side regarding the processes which the company went through in deciding to introduce PRP and reasons for its introduction. However, the problems over getting access for qualitative research have imposed limitations on the quality of the quantitative evidence that it has been possible to gather, most notably in terms of the ability to give appropriate weight to the various elements of the rationale given by Thames Water for the introduction of PRP. In particular, with the benefit of hindsight Performance Management and changing organisational culture should have been given more emphasis.

### Structure.

The next chapter defines PRP, looks at its coverage, and explores some of the reasons put forward for the popularity of PRP and some of the criticisms of PRP by way of general context. The rest of the thesis breaks down into four parts. The following three chapters explain the theoretical framework used to explore the motivational effectiveness of Thames Water and its effectiveness as an engine of cultural change. Chapters 6

and 7 describe the qualitative research evidence and describe the research instrument used to gather the quantitative data. The quantitative data is then reported and analysed in Chapters 8-10. Finally, Chapter 11 brings together the research evidence in an attempt to answer the five questions posed at the beginning of this Chapter.

## Chapter 2

### **Why do firms use PRP?**

#### **Introduction**

In order to understand why Thames Water adopted and continues to use PRP it is important to look at the factors that may have influenced that decision including the approach that has been adopted by other firms. First of all it is important to be clear about what is meant by PRP and look at what distinguishes PRP from other performance based pay systems. It is also helpful to understand how far PRP has spread and why. There are a number of different surveys that give some idea of the extent to which the use of PRP by firms has grown. Firms have adopted PRP for a variety of reasons and a number of the benefits that firms commonly hope to achieve by using PRP can be identified from the literature and surveys. It is also important to consider the criticisms of PRP, that is to say the potentially negative factors that firms might take into account when deciding whether or not to adopt PRP. Finally there is the question of why PRP continues to be popular with employers? Taken together these different aspects of the extent and rationale for the use of PRP by firms in general give a background against which Thames Water's decision to introduce and continue to use PRP can be better understood.

## PRP Defined

PRP is one of a range of performance pay systems, that is payment arrangements where the amount being paid to employees depends upon specified outcomes being achieved (Performance Pay Trends in the UK, IPD Survey Report 1999). These outcomes can be in the form of inputs or outputs. In this context, inputs are how the employees perform their work or the level of competence or skill that they bring to their work. Outputs are a measure of the performance of employees, either individually or as a team or group, or of the workforce as a whole. The key feature of all such schemes is that pay is contingent on outcome.

Thompson and Milsome (p25, 2001) define PRP in the following terms:

'Individual performance-related pay links financial rewards for individual employees to the results achieved by that employee, usually through assessment of performance, summed up in an appraisal rating based on agreed objectives.'

The IPD Survey in 1999 defined individual PRP as covering merit pay or bonuses determined by agreed individual objectives (Performance Pay Trends in the UK, IPD Survey Report 1999). Armstrong and Murlis (p262 Reward Management 1994) define PRP as linking pay progression to a performance and or competence rating carried out at a performance review. They distinguish between schemes where the manager makes an assessment of the performance from those schemes where the performance is judged against predetermined targets and payment is in

the form of a lump sum or bonus. For the IPD survey bonuses are included as PRP, yet Armstrong and Murlis say that bonuses are not part of PRP. There is a lack of consistency in the definitions but for the purposes of this thesis the question of whether bonuses are included or not makes no real difference.

The key issues are captured by defining PRP as a payment scheme where:

- The individual employee's pay is at least in part contingent on performance.
- And the employee's manager assesses performance for the purposes of determining contingent pay against predetermined criteria.

The two points that are highlighted are that individual pay is linked to individual performance and that the manager assesses performance against predetermined criteria. A number of performance payment schemes are excluded by this definition. It does not cover group PRP schemes or payment by results (PBR) schemes or bonus schemes where the bonus is entirely discretionary, without any laid down criteria for payment.

This thesis is concerned with the paradox between the continuing general popularity of PRP and the evidence that it often turns out to be fairly ineffective as a motivator. This paradox is most evident in relation

to individual PRP schemes. Individual PRP Schemes appear to focus on the issue of motivation more acutely than group schemes do. This is because the link between the individuals, their performance and their pay, in individual PRP schemes, more closely reflects the key elements in the three theories of motivation in individual PRP than it does in group PRP.

### PRP and payment by results

The growth of PRP can be contrasted with the use of Payment by Results (PBR), which it appears is either static (Mason and Terry 1990, and Millward et al. 1992) or may even be in decline (Cannell and Wood 1992). The essential difference between the two payment systems is that in a PBR system the level of payment is determined objectively by predetermined and measurable output, while in a PRP system the level of payment is determined by a subjective assessment of performance against predetermined measures, which may include both output and input. A further important distinction between the two systems is that in PBR schemes performance payments are not generally incorporated into salary for future years, while PRP schemes frequently consolidate pay increases earned through performance in one year into salary for future years (Heneman 1994). One of the attractions for employers of PRP over PBR appears to be the ability to use the subjective nature of the assessment system to focus rewards on the achievement of less readily

quantifiable or tangible areas of performance, such as the quality of work done and customer service (Heneman 1994). Another reason why PRP is perhaps more attractive to employers than PBR is the well-established tendency of PBR systems to degenerate in their effectiveness as workers learn to play the system and regulate their own output (Roy 1952, Lupton 1963, Brown 1962, and Cannell & Wood 1992). It has been argued that PBR is particularly suited to large establishments with short tenure employees where essentially it is used as a substitute for supervision (Heywood, Siebert & Xiandong Wei 1997)

However, it is worth noting that much of the evidence on the motivational effectiveness of pay for performance schemes relates to PBR and bonus schemes, rather than PRP. Lawler and Jenkins (1990) reported that pay for performance schemes are producing productivity gains of between 1- 35%, but they found that PRP schemes were failing to establish a clear link between pay and performance and consequently failing to produce positive motivational results. Kahn and Sherer (1990) found in a longitudinal study of a company using both bonus pay and PRP, that, while the bonus scheme was motivating employees, the PRP scheme was not acting as an effective motivator for employees. Fernie and Metcalf's (1999) study of the performance effects of contingent pay over a fixed fee arrangement in horse racing is essentially measuring the motivational effectiveness of payment by results.

## The growth of Performance Related Pay.

"Reports of the death of IPRP [Individual Performance Related Pay] appear to have been greatly exaggerated"

(p. 280, Kessler 2000)

The evidence from surveys suggests that a large and increasing number of employers are using individual performance related pay (PRP), or merit pay as it is sometimes called, to pay workers. Annual statistics on pay, such as those in the New Earnings Survey, do not distinguish PRP from payment by results (PBR), consequently it is difficult to use annual statistics to gauge the use of PRP (Cannell and Wood 1992), although a recent attempt to use annual statistics to gauge the spread of PRP supported the notion that PRP is continuing to spread and suggested it may be forming a larger part of employees' salaries (Choat 1997). However, more precise evidence about the use of PRP comes from survey results. The 1990 Workplace Industrial Relations Survey (WIRS) showed that 34% of all employees covered by the survey received PRP; Millward et al (1992) suggest that this figure under-reports the use of PRP. By 1998, WIRS figures had not changed to any significant extent and Millward et al (2000) were suggesting that there may even have been a slight reduction in the use of PRP. However three things were clear from the 1998 WIRS; there was more use of PRP in the private sector than in the public sector, PRP was more common in manufacturing than elsewhere, and PRP tended to be used in larger workplaces.

Cannell and Wood (1992) found that 40% of the PRP schemes for non-manual employees reported in an IPM/NEDO survey had been introduced in the preceding ten years, with 27% of the schemes being introduced in the preceding five years. The IPM/NEDO survey showed hardly any evidence of PRP schemes being withdrawn (1% of schemes for non-manual employees), while 11% of the schemes had been extended and 20% had been revised in the preceding five years. The IPD surveyed some 5,000 firms in respect of performance pay trends in the UK (Performance Pay Trends in the UK, IPD Survey Report 1999) and got response rate of 23% covering some 1.5 million employees. They found that 40% of respondents had individual PRP, although it tended to be used more frequently for managers than non-management employees. Comparing the rate at which firms reported that they were abandoning PRP, with the rate at which firms were introducing PRP, the report concludes that the use of individual PRP is still increasing. Thompson and Milsome (2001) reviewing the survey evidence conclude that PRP is far from in its death throes, even though its advance is less rapid, and that it continues to be a prime and extending feature of the pay landscape for the majority of UK and US employees and it is increasingly in evidence in continental Europe. These survey findings support the view that the use of PRP is both widespread and may even still be growing.

## Reasons for the use of PRP.

There are a number of different reasons why firms have introduced PRP, and the reasons can be divided between those that produce immediate benefits, which will be termed 'hard', and those reasons that reflect a wider perspective in the firm's reward strategy, which will be termed 'soft'. Increased employee motivation, improved recruitment and retention, and better wage cost control are the hard immediate benefits of PRP. While using PRP because of the message it sends, or as a strategic approach to pay, or as part of Performance Management, or to bring about cultural change are the soft benefits of PRP. Looking at employers' perceptions of the hard benefits of PRP first, the most obvious benefit is the link between performance and pay.

### i) Motivation

There continues to be substantial support for the idea that incentive pay schemes will improve performance amongst employees.

"the prospect of higher pay for increased output/quality often provides an incentive and many (incentive pay) schemes are introduced in the clear expectation that performance will thereby be improved."

ACAS 2003

One of the key objectives firms have in mind when introducing PRP is to enhance employee motivation and productivity (Kessler 1994). Intuitively, it would appear that the link between performance and pay should

encourage employees to work harder and, indeed, expectancy theory (Vroom 1965) would seem to support this conjecture, subject to certain conditions being satisfied. Employers and commentators have long believed that this link will motivate employees to work harder. F. W. Taylor (1911) put it this way:

'it is impossible through any long period of time, to get workmen to work much harder than the average men around them unless they are assured a large and permanent increase in their pay.'

The motivational effect of PRP is claimed as one of its principal benefits in a number of the works on reward systems (Smith 1991, Armstrong 1993, Heneman 1994, and Armstrong and Murlis 1994). From the firm's point of view, increased employee motivation would, on the face of it, provide a straightforward economic justification for using PRP, as increased motivation should improve the employees' performance. Indeed it is the motivational effectiveness of PRP, which has often been used as a point of departure for a critical analysis of PRP (Bevan, Thompson & Hirsch 1991, Thompson 1993, Marsden and Richardson 1994, and Marsden and French 1998). The motivational effectiveness of PRP is also one of the central issues examined in this thesis.

## ii) Recruitment and retention and downsizing and costs

PRP is also seen as a mechanism for retaining good employees and losing bad employees. Good employees, that is to say those who are assessed

as performing well, will be better rewarded through PRP and thus encouraged to stay. Bad employees, that is to say those who are assessed to be performing badly, will either improve their performance or leave because they are receiving lesser rewards. Bodies like the Top Pay Research Group have argued (Top Pay Research Group 2003) that it is essential to pay those at the very top of organisations contingent pay in order to retain them. If the decision makers in organisations are being given rewards contingent on their performance, as a retention mechanism, they may well be attracted to the idea of cascading down similar mechanisms through the organisation.

Paying more to more productive employees and less to the less productive employees might also be thought to have the additional advantage of helping to control wage costs (Smith 1991). Increases in productivity help to fund the additional pay for the good performers, and poor performers no longer enjoy an automatic increase in pay through the incremental system or annual wage round.

Many firms have been downsizing since the 1980s by delayering, that is to say by getting rid of layers of management, which in turn reduces the promotion prospects for remaining employees. PRP may help to control wage costs and yet maintain employee morale amongst those employees who are judged to be better performers. It is argued that PRP became an attractive option for firms, as they sought to retain and motivate good

employees, whose traditional promotion routes had disappeared, by offering them the opportunity to increase earnings through performance (Baker 1990). Meanwhile poor performers would leave as they became dissatisfied with the level of PRP that they received, or so it was said (Dreher 1987).

### iii) PRP gives a message about the firm

Employers have also turned to PRP for longer term, more strategic, less immediate reasons, which have been termed soft benefits. PRP is sometimes said by employers to be a fairer system of rewarding employees, than incremental systems, in which pay increases as a result of length of service. PRP is said to be:

'A conscious move...to reflect a new perception of equity based on the developing view that it is fairer to reward in relation to personal contribution than for length of service in a job.' (page 18 Armstrong & Murlis 1994).

From the employer's point of view using what they perceive as a fairer system that relates reward to contribution, may be seen as sending some powerful messages about their organisational values.

In the 1980s PRP was promoted as part of the Thatcher revolution (ACAS 1993, and Kessler & Purcell 1995), firms saw the adoption of PRP as a step on the road to an enterprise culture (Armstrong and Murlis 1994).

PRP was officially promoted for the public sector in the Citizen's Charter (1991), which stated:

'Pay systems in the public sector need to make a regular and direct link between a person's contribution to the standards of the service provided and his or her reward.'

The plans for the public sector under the Labour Government continue to emphasise performance and the use of PRP as a mechanism for achieving improved performance, with a strong emphasis on benchmarking performance and the linking of teachers' pay progression to appraisal (Treasury 1998). The logic seems to be that if firms want to compete then they have to be performance driven and one way this can be demonstrated is by adopting a payment system that links the level of pay to the employee's performance. This became apparent in the newly privatised former nationalised industries (Kessler and Purcell 1992). Across both the public and private sectors in Britain PRP was also promoted, as part of the Thatcher agenda, as a move away from the collective to a more individualistic approach to the employment relationship (Kessler and Purcell 1995).

The use of PRP in the public sector in Britain reflected a wider move to use PRP in the public sector across many countries in the OECD, which Wood (1993) attributes to the cross-fertilisation of 'new managerialism' from the private to the public sector, as public sector agencies have moved away from simply using budgetary control, as their principal measure of effectiveness, to using more output measures to monitor

their effectiveness. The argument here seems to be that as controls become more output-orientated performance becomes more critical, which in turn makes a pay system that links pay to performance more attractive.

State promotion of PRP continues in Britain and the United States, and has spread to the rest of Europe (Milkovich 1991, Elliot & Bender 1997, and Marsden et al. 2000), despite research evidence that PRP has not been particularly effective at motivating employees in the public sector (Marsden & Richardson 1994, Marsden & French 1997, and Kellough & Nigro 2002). Indeed, Kessler (2000) has commented that much of the criticism of PRP is based on evidence from the public sector where as he says the character of the workforce and the financial and political constraints were always likely to make PRP more difficult to implement successfully.

#### iv) Pay strategy

The introduction of PRP may also be a response to arguments about the best type of reward structure for the organisation, in other words a strategic approach to pay, what has been termed 'new pay' (Kessler 2000). Some authors (Lawler and Jenkins 1990, and Armstrong and Murlis 1994) argue that the correct payment system for an organisation is contingent on a number of other factors, such as business strategy,

history, people, human resource strategy, culture, market and regulatory environment (Armstrong and Murlis 1994). What matters in order to get the best from the payment system is that there is fit between the pay system and organisation. Lawler and Jenkins (1990) comment that there is little or no evidence to support this assertion, but that it has face validity. However, firms may introduce PRP because they feel that PRP fits with other parts of their business strategy, so for example Cannell and Wood (1992) found that some firms in their survey felt that PRP helped to emphasise that they were results driven or performance orientated organisations.

The development of human resources management (HRM) has focused attention on the reward strategies used by employers (Tichy, Forbrun and Devenna 1982). Adopting a HRM approach includes ensuring that the reward system reflects the organisation's goals and engages line management in the reward process (Kessler 2000). PRP emphasises performance, which is a key organisational goal for many employers, and engages line managers in the reward system through the appraisal process, so that it is a natural choice as part of HRM.

#### v) Performance Management

Performance Management is perhaps one particular approach to pay strategy, but it warrants separate mention, both because of its popularity

and because it is sometimes seen by employers as linking pay into employee commitment and cultural change (Bach 2000). 'Performance Management has become massively popular in recent years' (at p. 52 Hendry et al 2000), yet there is a degree of ambiguity about what is meant by Performance Management. In essence Performance Management is about ensuring that the individuals' objectives at work are aligned with those of the organisation, in a measured and managed way. Performance appraisal is clearly a key part of Performance Management, but PRP is not an essential ingredient of Performance Management, and Hendry et al (2000) argue that PRP takes away from the developmental side of Performance Management and focuses too much on the 'dark side' or controlling element. While Performance Management clearly owes some of its growing popularity to an interest in the structured approach it offers to employee development as exemplified by Investors in People award scheme, PRP also fits into Performance Management by directly linking individual performance into overall organisational objectives. Indeed the growth in the use of Performance Management may help to explain some of the continuing popularity of PRP.

The use of PRP for Performance Management can be viewed on two levels. At one level PRP can simply be seen as a way of ensuring that performance appraisals get done, as Cannell and Wood (1992) found in their survey. At a less prosaic level, PRP reinforces the organisational objectives for individuals by tying the objectives into financial rewards;

this reinforcement may be particularly important if Performance Management is being used to increase employee commitment or bring about cultural change within the organisation (Bach 2000).

#### vi) Changing Organizational Culture

PRP can also be used, not because it fits the organisation, but because it fits the type of organisation that the firm would like to become. In other words PRP becomes a mechanism for achieving change in the organisational culture. Some employers have used PRP as a mechanism for achieving cultural change within their organisation (Kessler & Purcell 1992). It is not clear precisely how PRP acts as a mechanism for achieving cultural change in an organisation. Lawler and Jenkins (1990) assert that all pay systems influence organisational culture, but argue that PRP does this more dramatically than other pay systems, because it communicates norms of performance in the organisation. PRP can also be used to communicate organisational goals by cascading the goals down through the organisation, as those goals are translated into individual targets for each level within the organisation. However, while changing the pay system may be an important reinforcer of cultural change, the process of cultural change within an organisation is far more complex (Schein 1992).

Whether PRP is used because of the message it sends, or because it reflects the type of organisation the firm is, or wants to become, it is being used for longer term, perhaps less tangible benefits, which have been termed soft benefits. It will be argued in this thesis that these soft benefits are perhaps even more important to some firms than the hard benefits.

### Criticism of PRP

Criticism of PRP can be divided between general criticism of its impact on organisational effectiveness and specific criticism of its failure to motivate employees in practice.

#### i) Conservatism

Critics of the impact of PRP on organisational effectiveness argue that PRP is inherently conservative in its effect on the organisation. Demming (1982) says:

'Merit Pay rewards people that do well in the system. It does not reward attempts to improve the system'

Kanter (1989) also describes the system as conservative. The problem, for both Demming and Kanter, is that they see PRP as suppressing initiative and risk taking, by rewarding the achievement of predetermined targets. The setting of objectives, which have to be achieved in order to

get a performance payment, creates what has been called a pseudo contract (Pearce 1987) in the employment relationship. Lacking the advantages of a fully contracted out relationship, the pseudo contract nevertheless inhibits the organisation's ability to gain all the flexibility from employees that should flow from an employment relationship. Essentially the argument is that the employee focuses on achieving those targets or behaviours that have been identified as the targets or behaviours against which their performance will be assessed in order to determine the level of performance payment that they receive, at the expense of flexibility. For instance, a longitudinal study of PRP for U.S. Federal employees by Pearce and Perry (1983) found what they called 'gaming', whereby broader organisational goals were displaced as employees became narrowly focussed on achieving their PRP targets.

Potentially the flexibility of many PRP schemes allows employers to specify quite general criteria against which employee performance will be judged, so that for instance the Thames Water PRP scheme includes performance traits amongst the criteria against which employee performance is judged. On the face of it this should allow employers to specify performance for PRP purposes in such away as to avoid any undue rigidity. There is however a danger that the level of flexibility in the scheme depends upon the way in which individual managers operate PRP as well as the nature of the scheme itself. The evidence from the

Thames Water PRP scheme is that the quality of management of the scheme was highly variable.

ii) Adverse impact on internal relationships

Much of the criticism of PRP has focussed on the effect PRP has on the internal relationships within an organisation. Firstly, it is suggested that instead of being an aid to good management, PRP becomes a substitute for management. Rather than managers managing employees' performance, so that employees work hard at their jobs, it is said that managers rely on PRP to ensure adequate levels of performance from employees. Smith (1991) asserts that in many organisations PRP is the only effective control for the management of human resources and Kohn (1993) says that:

'In many workplaces, incentive plans are used as a substitute for management: pay is contingent on performance and everything else is left to take care of itself.'

At least some support can be found for this contention in the report of the IPM/NEDO survey (Cannell and Wood 1992), which found that paradoxically one of the reasons given by employers for using PRP was to ensure that assessments get done. In other words, some employers were saying that without PRP managers would not discuss performance with those employees that they managed. The criticism is that if managers are only discussing performance because of need to set

performance targets and assess performance, then they are abrogating their responsibility to manage the employees' performance, and relying instead on PRP.

The difficulty with this argument is that it reduces management to a question of managing employee performance. While this is no doubt an important part of the managers' role, it is only one part of a complex role. In any event, managing employee performance is not simply a question of talking to employees about their performance. Leadership and role modelling may be just as important in getting the best performance out of employees. On the other hand it may be that PRP is a very useful trigger for ensuring that managers take responsibility for managing employee performance. After all, if PRP is a trigger for good management rather than a substitute for it, PRP is fulfilling a useful function. However, the evidence from Thames Water is that the management of PRP is very variable in quality. It may be that good managers find PRP a helpful tool, and poor managers fail to use it effectively.

Secondly, it is argued (Kanter 1989, Kohn1993 and Pfeffer 1998) that the assessor role may undermine the relationship of trust which a manager needs with those employees they have to manage; as manager and employee focus on the assessment of prescribed tasks and targets, rather than identifying problems and solving them. Some PRP schemes, such as

the Thames Water PRP scheme, work on the basis that the appraisal will be an opportunity for the manager and employee to discuss problems. The Thames Water PRP scheme specifically provides for more than one appraisal a year to take account of changing circumstances and provide an opportunity to discuss problems.

The relationship between the manager and the employee may also be tainted by the financial element of PRP. If the employee's earnings are going to be determined by the employer's assessment of their performance, then the employee might quite rationally want to be seen as a very competent performer. The employee may be less likely to admit to any shortcomings if they believe that this may adversely affect their earnings. Put another way, an employee, who has customer care as a PRP target, seems less likely to admit to problems over delivering customer care, than an employee for whom such an admission would have no impact on their earnings. Effectively PRP may damage the trust between the employee and manager. Some commentators have said that trust between the employee and manager is a precondition to the effective operation of PRP (Lawler 1981, Siegall & Worth 2001). If trust is a precondition to the effective operation of PRP then PRP may have an inherent tendency to undermine its own effectiveness. As the PRP process erodes trust between the employee and manager so PRP becomes less and less effective. From a theoretical perspective trust may

well be important to the motivational effectiveness of PRP, both from the point of view of expectancy and equity.

A further widespread criticism (Demming 1982, Kanter 1989, and Kohn 1993, Pfeffer 1998) is that PRP damages teamwork between employees as they focus on their individual PRP targets at the expense of co-operative teamwork. The argument here being that if individuals are focussed on achieving their own individual performance targets, which carry a potential financial benefit, they will put the achievement of those targets before co-operation with other members of the workforce, which has no financial benefit for them. A number of PRP schemes try to tackle this last point by including team working as a PRP target, so that individual employees will know that their performance assessment will include an element to reflect the extent to which they have worked as part of a team.

Finally it is said that PRP schemes can demotivate employees who receive a poor appraisal or performance payment (Demming 1982, Kanter 1989, and Kohn 1993). Marsden and Richardson (1994) concluded from a survey of Revenue staff that the PRP may on balance have been demotivating employees. Clearly, if some employees are demotivated, then there is a danger that the demotivating effect of the PRP may outweigh its benefits as a motivator for other employees. Support for the idea that PRP might demotivate some employees comes from equity

theory (Adams 1965), which says that individuals will compare their ratio of inputs to outcomes with others and adjust their level of input to match what they perceive to be appropriate comparitor ratios. This means that someone who thinks they are underpaid for the work they do compared to others may simply work less hard or leave, although poor performers leaving may be what the employer wants. Clearly the employer is left with a problem if the poor performers respond to low levels of performance payment by reducing their level of performance further. Some employers specify that consistently poor performers will be dealt with under the capability procedure and may have their employment terminated.

#### iv) Fails to motivate

There is a considerable body of survey evidence that PRP is not effective as a motivator for individual employees. Heneman (1994) examined U.S. survey results and concluded:

'The results to date on the relationship between merit pay and subsequent motivation and performance are not encouraging.'

Armstrong and Murlis (1994) examined the survey evidence from Britain, including large-scale surveys by Bevan, Thompson & Hirsch (1991) and Thompson (1993), and found that none of the surveys showed that PRP works as a motivator for employees. Indeed, according to Cannell and Wood (1992) personnel managers, in the firms using PRP that they

surveyed, were themselves unclear about whether PRP had any motivational effect. Harris (2001) also found scepticism about the motivational effects of PRP in a survey of middle managers. More recently the Industrial Society found that fewer than half the personnel and human resources managers in a survey believed that their own PRP schemes were rewarding performance (Hague 1996). Kessler (2000) has said that much of the survey evidence regarding PRP's lack of motivational effectiveness comes from the public sector where the nature of the workforce, as well as the distinctive financial and political features of the sector are more likely to make PRP problematic.

The Inland Revenue perhaps best illustrates the problems over the motivational effectiveness of PRP. Marsden and Richardson (1994) surveyed Inland Revenue employees who were in receipt of PRP and concluded that, instead of improving employee motivation, the scheme might actually on balance have been demotivating employees. Subsequently, the Inland Revenue revised their PRP scheme. A further study of Inland Revenue employees was conducted by Marsden and French (1998), three years after the introduction of the new scheme; the survey found that there was little change in the motivational effectiveness of PRP in the Inland Revenue, despite the introduction of a new PRP scheme.

Evidence that PRP has any motivational effect is much more limited. An OECD study (Wood 1993) on the use of PRP in the public sector concluded that there was limited evidence to support the use of PRP. A number of other studies, which on the face of it show that PRP may have some motivational effect, have looked at incentive pay generally rather than just PRP (Guzzo and Katzell 1987, and Fernie and Metcalf 1995, 1996). However, as noted above, there are important differences between PRP and other forms of incentive pay, such as PBR, and there is evidence that PRP schemes are less effective than other incentive payment schemes (Lawler and Jenkins 1990, and Khan and Sherer 1990). Consequently the results of these studies, although concerned with incentive or, as they are sometimes termed, contingent pay schemes cannot simply be applied to PRP, which needs to be treated as a separate and distinct form of incentive pay.

### Why does PRP retain its popularity?

At first glance it seems somewhat paradoxical that a pay scheme which attracts so much criticism should be so popular with employers. There may be a number of explanations for this. Employers may not believe that the criticism of PRP is entirely valid, perhaps because it does not fit in with the employer's view of the world or it may be at odds with their own experience. It may be that the employer believes that the perceived benefits of PRP outweigh the potential disadvantages. Or it may be that

the employer sees PRP as the least bad alternative compared to other pay schemes. Each of these scenarios raises the question of how far the employer's assessment is based on an analysis of PRP and in particular of their own PRP scheme.

The survey evidence (Cannell & Wood 1992) suggests that any assessment of the effectiveness of PRP within individual firms seems to rely, more often than not, on the subjective views of managers and anecdotal evidence. Cannell and Wood (1992) found that many of the managers who had been surveyed were unsure about how a proper evaluation could be done. Without a proper evaluation, it is not difficult to imagine managers concluding from their own informal assessment that their PRP scheme is working satisfactorily or at least not wanting to rock the boat by suggesting that there may be problems.

Employers may also be sceptical, about the criticisms of PRP as a motivator for employees, because a number of texts suggest that PRP schemes will work as a motivator provided they comply with specific prescriptive rules. In other words, the suggestion is that the problem over motivation does not lie with PRP per se, but rather with the design and implementation of the PRP scheme. Armstrong and Murlis (1994), for example, say that there are five basic rules that have to be observed, if a PRP scheme is going to be an effective motivator for employees:

- i) There must be clear targets

- ii) Employees must receive feedback
- iii) Employees must be able to influence their own performance
- iv) Employees need to be clear about the rewards for improved performance
- v) Rewards must be meaningful and positively communicated

For the rewards to be meaningful, Arstrong and Murlis say that the amount of salary increase needs to be at least 3% of salary, and that arguably 10-15% is needed for a significant increase in motivation.

Heneman (1994) on the other hand, says that the critical component for the success of PRP is the adequacy of the performance measures, the criteria must have:

- i) Content validity - they must be relevant to the job
- ii) Convergent and discriminant validity - they must measure different constructs
- iii) Reliability - they must be consistent
- iv) Accuracy
- v) Correction for rating error - that is they must recognise problems like the halo effect
- vi) Relevance - they must be relevant to the goals of the organisation

For Heneman (1994) the amount of the performance payment is determined by the 'just noticeable difference', that is the minimum amount necessary to improve the employees performance, which he says will depend upon the individual employee and the circumstances. No one

element of PRP is identified as being the critical determinant of the motivational effectiveness of PRP:

'While the goal is to be able to pinpoint which characteristics of merit pay plans are associated with which desirable behavioural or attitudinal outcomes, it is not possible to do so at this stage.' (Heneman 1994)

It is perhaps not surprising that both Armstrong and Murlis (1994) and Heneman (1994) highlight different aspects of PRP schemes as being critical to the success of PRP as a motivator for employees, as neither approach is explicitly grounded in any theoretical framework or based on any substantial research evidence. Lawler and Kessler on the other hand take an approach implicitly more grounded in expectancy theory. Lawler (1981) says that for PRP to work the rewards must be important, capable of being varied in line with validly measured performance, and that there must be high levels of trust between employees and managers, and employees accept the PRP scheme. Kessler (1994) has identified three elements in PRP which present problems of implementation; establishing performance criteria, assessing whether those criteria have been met or not, and the linkage between the criteria and the pay award.

However, for some employers the perceived benefits of PRP may be more diffuse and less specific than simply increasing employee motivation. Kessler (1994) has argued that employers are often principally concerned with the use of PRP as a mechanism for strategic and cultural change than with its motivational effectiveness. Some employers have focused

on the Performance Management aspects of PRP, as a way of ensuring organisational and strategic fit between pay and organisational objectives. Although there is a degree of ambiguity about Performance Management, essentially it links individual appraisal in with organisational objectives and strategy in a measured and systematic way (Bach 2000, Hendry et al. 2000). For employers who are concerned with strategic and cultural change, the link between PRP and a more motivated workforce may be more indirect than that suggested by the motivational theories such as expectancy, equity and goal setting theory.

The decision of so many firms to stick with PRP may also be a matter of choosing what is perceived to be the least bad pay system. While PRP has been criticised, the choice of PRP has to be set by the employer against the available alternatives. The rate for the job or an incremental progression system, both pay a set rate for the job done irrespective of the employee's ability or commitment or effort. Payment by results pay systems are only really appropriate for those employees whose outputs can be readily and non-controversially measured and, in any event, payment by results systems are subject to manipulation and may soon become degraded as employees learn to 'play the system' (Roy 1952, Lupton 1963, and Brown 1962). The problem with profit related pay is that the employee may have little or no influence over whether the firm makes a profit or the size of that profit, so that the employee may be rewarded irrespective of their ability, effort or commitment. Skill based

pay systems are expensive to introduce and maintain and it is far from clear whether the benefits outweigh this additional cost (Armstrong 1993). Employers will also be aware that any differentiation in pay between employees doing the same work or work rated of equal value has to be objectively justifiable, otherwise such differences may be illegal (Danfoss ECJ 1989). Consequently PRP may appear to some employers as on the face of it the least bad pay system available to them.

Despite the explicit linkage between performance and pay, which is made by PRP schemes, the literature reviewed above suggests that organisations use PRP to obtain a range of objectives. Increased employee motivation is only one of the benefits employers identify. Kessler (1994) has argued that political and cultural drivers are likely to be more important considerations than increased employee motivation, especially for a company, which has been recently privatised. If Kessler's analysis is correct it would help to explain the growth in PRP at a time when there is increasing evidence to suggest it does not increase employee motivation (Bevan, Thompson & Hirsch 1991, Thompson 1993, and Marsden and Richardson 1994). Similarly, it is argued that the growth in Performance Management (Hendry et al 2000) may have also fostered the growth in PRP, as firms use PRP to ensure employees take on wider organisational objectives. The research for this thesis was done with Thames Water a privatised utility; this provided an opportunity to explore Kessler's argument about the reasons for the introduction of PRP.

The competing arguments in the literature about the reasons why firms use PRP have been tested using qualitative analysis to test the following hypothesis:

Hypothesis 1.

*'Thames Water introduced PRP in order to achieve a number of objectives, but principally in order to achieve a change in corporate culture following privatisation.'*

## **Chapter 3**

### **Three theories of motivation.**

#### **Introduction**

This thesis draws on three theories of motivation to produce a theoretical framework, which can be used to explore how PRP motivates or fails to motivate employees. The rationale for focusing on three particular theories in order to explain the motivational effects of PRP is explained below. The three theories are put into the broader context of theories of motivation in general, firstly by putting the theories into a broader context and then by examining an 'integrationist's' approach (Kanfer & Ackerman 1989, and Kanfer 1990). Finally, expectancy theory is then examined and a model of expectancy theory, together with an elaboration on that model, are identified as the first part of the theoretical framework.

#### **The fit between expectancy, goal setting and equity theories and PRP.**

Expectancy theory (Vroom 1964) is frequently quoted as providing a possible theoretical justification for the use of PRP (Pearce & Perry 1983)

and consequently is sometimes used as a point of departure for critical analysis of PRP (Kahn & Sherer 1990). As noted in the last chapter there is a natural congruence between a payment system that links additional payment to performance and a theory that predicts that individuals will be motivated to work harder to achieve goals that produce a valued outcome for the worker. Similarly some commentators have noted that the essential elements for goal setting theory are also present in PRP, in so far as the individual worker is set specific targets to achieve in order to get a performance payment (Cannell & Wood 1992).

The third theory that is considered in this hypothesis is equity theory (Adams 1965). Expectancy and goal setting theories are concerned with the mechanisms that affect individual worker's motivation to achieve the targets that have been set. One weakness with this approach is that it ignores the wider social context, in particular the perceptions that individuals have about the way in which they have been treated compared to other workers. Yet one of the fundamental claims made for PRP is that it is a fairer system of rewarding employees (Armstrong and Murlis 1994). Fairness is a question of how the individual is treated in both absolute and comparative terms, that is to say it engages both individual feelings of fairness and the wider social context. Equity theory has often been used in the literature in order to capture the wider social aspects of PRP (Brown 2001, Brown & Benson 2003, Isaac 2001, and Kahn & Sherer 1990).

Taken together expectancy theory, goal setting theory and equity theory provide a framework against which the motivational effectiveness of PRP can be examined (Richardson 1999 and Arrowsmith et al 2001). The three theories highlight different aspects of the PRP process. Some commentators have tried to develop an overarching theory of motivation that attempts to bring together the theories of motivation. The problem with this approach is that it assumes that the various theories of motivation can be reconciled, so that they fit together to form a coherent whole. However, it is far from clear how at least two of the theories, which are tested in this thesis, can be reconciled. Indeed it is argued that Goal Setting theory and Expectancy theory are counterposed, because each of them assumes that motivation is a function of different variables. On the one hand, Goal Setting theory predicts effort will be related to the difficulty of achieving the goal. While on the other hand, Expectancy theory predicts that effort will be related to the expectancy of a valent outcome. As expectancy and goal difficulty are not necessarily correlated, it is difficult to see how the two theories can be reconciled in one overarching theory of motivation. This issue is considered in more detail in a subsequent chapter.

However, although it is argued that the two theories cannot be readily merged in one overarching theory of motivation, that does not mean that the two theories are seen as being mutually exclusive. Indeed one of the

central hypotheses of this thesis is that each of the three theories, which have been used to examine PRP, can give an insight into different aspects of the motivational effectiveness of PRP. It is hypothesised that each theory might shed some light on a particular aspect of the scheme, because each of the theories looks at a particular aspect of PRP. It is helpful in this context to look at the place each of the theories has in the broader context of motivational theories.

### The theories of motivation in context.

Two different approaches to a categorical framework for theories of motivation are helpful. Deci (1992) has suggested a framework for the theories of work motivation based on the development of the concepts underlying those theories. Ruth Kanfer (1990), on the other hand, has suggested an analytical approach focusing on the key structural differences between the theories of motivation as step towards reconciling the various theories of motivation in a unified approach. Both approaches produce a similar broad distinction between the theories of work motivation, and it is that distinction which illustrates why expectancy theory and goal setting theory in particular seem apposite for an analysis of PRP.

Deci (1992) suggests that the theories of work motivation can be put into one of five clusters built around organising concepts of; responses,

physiological needs, psychological needs, goals, and social forces. The first three of these organising concepts are concerned with what it is individuals are motivated to do by various stimuli. Thus response theories, such as operant theory, are concerned with behaviour modification through the use of behavioural reinforcement. Operant theory predicts that behaviour can be directed through positive reinforcement. Theories clustered around physiological needs focus on the various physiological drives, such as the need to reproduce, that are said to explain behaviour. Similarly, theories based on psychological needs suggest that individuals experience pull which directs their behaviour to meet certain psychological needs, like self-esteem and self actualisation. It has been argued that physiological and psychological needs form a hierarchy of needs, and that when lower order needs were satisfied individuals will be motivated by the need to fulfil higher order needs. These three clusters of theories are concerned with identifying what will motivate individuals by describing what will be of value.

PRP schemes implicitly assume that workers will increase effort in order to achieve greater financial reward, in the form of a performance payment, and what distinguishes different PRP schemes is the mechanism for achieving that financial reward. The underlying assumption in PRP, about the attraction of a financial reward for workers, matches the prediction in the three clusters of theories about stimuli, that individuals are hedonistic and will respond to positive stimuli. What is

less clear is to what extent any particular individual will perceive a performance payment to be a positive stimuli. Maslow's hierarchy of needs suggests that once basic physiological needs are met, individuals will be stimulated by psychological pulls such as the desire for self-actualisation. On the face of it, this suggests, applying just these first three clusters of theories identified by Deci, that not every one will be motivated by PRP, because not all individuals will find performance payments attractive, and all PRP schemes are predicated on a monetary reward for better performance. However, in order to understand why one PRP scheme is better at motivating employees than another PRP scheme, it is necessary to consider not what motivates individuals but how they are motivated. In other words in order to compare the effectiveness of different PRP schemes it is necessary to accept the basic premise of all PRP schemes that a performance payment is a valued outcome for employees.

Deci distinguishes those theories about what will be of value from goal theories, which are concerned with cognitive processes, that is to say how motivation is directed, rather than what motivation is directed to achieving. There is a logical connection and fit between goal theories, which describe motivation in terms of the establishment of goals, and PRP where the emphasis is on relating pay to the achievement of goals. Two goal theories, goal setting theory and expectancy theory, are particularly relevant to PRP and appear to have an inherent congruence

with the goal setting processes used in PRP systems. According to goal setting theory (Locke and Latham 1984), motivation will increase with goal difficulty, when individuals are committed to achieving specific achievable goals. While expectancy theory (Vroom 1964) states that motivation is a function of the individual's expectancy that achieving a particular goal will be instrumental in producing a valent, that is to say valued, outcome for them. Both theories are concerned with goals and how an individual's motivation to achieve those goals can be increased.

Deci says there is a fifth cluster of theories around the concept of social and group influences. These theories are concerned with the way in which individuals adapt to their social environment by adopting the norms of the social group or informal organisation in the workplace in an effort to achieve social approval. Another aspect of this cluster is the concept that individuals will seek balance or consonance in their perceptions of how they are being treated. According to equity theory (Adams 1965) this means that individuals will adjust their behaviour in order to ensure that they feel their ratio of inputs to outcomes at work is comparable to the ratio of inputs to outcomes for others, who they see as comparators. One of the arguments advanced for PRP is that it is a more equitable system of pay, because it looks at individual inputs and outputs rather than simply paying people the rate for the job (Armstrong and Murlis 1994). Potentially workers in receipt of PRP might work harder on the basis that it is only by increasing their inputs that they can justify

their pay levels. However, equity theory works on the individual's perceptions and there is a danger that individual workers will simply adjust their perceptions of their own contribution, rather than increase their inputs. Equity theory seems likely to be a better predictor of demotivation, where the individual feels that they are being treated unfairly. A number of commentators (Demming 1982, Kanter 1989, Kohn 1993, Marsden & Richardson 1994 and Brown & Benson 2003) have suggested that PRP may have a demotivating effect on those employees who receive a poor performance appraisal or performance payment. Consequently equity theory has been used in this thesis both because it looks at the social aspects of PRP as a payment system, and because it predicts both the motivating and demotivating effects of PRP.

Ruth Kanfer (1990) adopts a different approach to the categorisation of the various theories of work motivation, but comes to a similar distinction between the various theories. Kanfer describes three streams of research that she says can be brought together in a 'unified perspective of motivation'. Firstly she identifies need-motive-value research which focuses on person based determinants of behaviour. The theories which have developed from this research are concerned with the activation of intrinsic motives, that is to say determinants of action that are based on that individual's own innate value system, such as equity theory, or the arousal of needs, as for instance in the case of Maslow's hierarchy of needs. The second stream of research, cognitive choice research, is

concerned with how choices about goals are made. The dominant framework for this paradigm is expectancy theory (Vroom 1964). Thus, if need-motive-value research tells us what is valuable or valent for an individual, cognitive choice research seeks to explain the basis on which the individual chooses the goal that leads to that valent outcome. The third stream of research is contained in the self-regulation metacognition theories, these theories are concerned with the self-regulation of the mechanisms that transform motivational force into behaviour and performance.

According to Kanfer the first two streams of research are concerned with distal theories of motivation, that is to say they set the stage for task engagement, by determining goal choice and the level of intended effort. Self-regulation and metacognition theories and to a lesser extent cognitive choice research, on the other hand, are proximal theories of motivation explaining the mechanisms that control task engagement. PRP assumes that money, which is the distal motivator according to Kanfer's framework, will be a motivator and consequently it is the proximal theories, goal setting and expectancy, which should explain the effectiveness of different PRP schemes.

In this thesis each of the three theories of motivation used in the framework has been used to highlight particular aspects of the PRP process. Each of the theories makes a prediction about motivation based

on the operation of specific psychological mechanisms. By examining the way in which PRP engages each of those psychological mechanisms it is hypothesised that the weaknesses in PRP or at least in the Thames Water PRP scheme can be identified. Consequently the approach adopted has not been to try and integrate the three theories of motivation in the framework, but to use each of them to highlight different aspects of PRP.

### Expectancy theory

Vroom's Expectancy theory (1964) or valence-instrumentality-expectancy theory, as it is sometimes called, assumes that individuals makes choices between alternative courses of action in order to maximise the benefit to themselves. Vroom posits that there are three key elements in this process. Valence is the individual's perception of affective value of a particular outcome. Valence can be positive or negative, depending on whether the outcome is perceived by the individual as being of benefit or disbenefit. Vroom distinguishes between first order and second order outcomes. So effort may lead to a first order outcome of performance. Performance may be a positively valent first order outcome, because it in turn leads to a valent second order outcome, such as a performance payment. The outcome does not have to be financial in order to be valent, but PRP offers the potentially valent outcome of a performance payment. Whether a performance payment was positively valent for any particular individual would depend upon their perceptions about its

affective value to them, and the valence of any other outcomes from the PRP scheme.

The individual's choice of behaviour will be determined by the instrumentality of a first order outcome leading to a second order outcome. Thus for the individual, the first order outcome of performance is only likely to be valent if it in turn is believed to lead to a valent second order outcome, and this causal link is described as instrumentality.

Vroom expresses instrumentality in terms of probability, that is to say on a range from 1, where the individual believes one outcome will necessarily follow from the other, to 0, where there is no likely relationship between the outcomes, and -1, where the individual believes that the second order outcome will only happen without the first order outcome. In PRP terms, this means that performance payment can only be a valent outcome where performance is believed to be instrumental in obtaining a performance payment.

The third element of the theory is the individual's belief that a particular outcome is achievable; this is termed expectancy. Expectancy is a measure, expressed as a probability between 0-1, of the individual's expectation that a particular outcome will be achieved through a behaviour or action. Thus if performance at a particular level is the first order outcome that an individual needs to achieve, to get a valent second order outcome, then expectancy is a measure of their belief that they can

perform at that level. That belief will be determined by a number of different factors including the individual's skill and confidence, as well as their perception about intervening factors that may help or hinder them in performing to that level.

According to Vroom the strength of an individual's intention to act in a certain way is determined by the valence, instrumentality, and expectancy which would result from that action. Vroom stated:

'the force on a person to perform an act is a monotonically increasing function of the algebraic sum of the products of the valences of all outcomes and the strength of his expectancies that the act will be followed by the attainment of these outcomes.'

This theory is expressed as the formula:

$$F_i = f \sum_{i=1}^n (E_{ij} V_j) \quad \text{and} \quad V_j = f \left[ \sum_{j=1}^n I_{jk} V_k \right]$$

Where  $F_i$  = the psychological force to perform an act /

$E_{ij}$  = the expectancy that the act will be followed by the first level outcome  $j$

$V_j$  = the valence of the individual first level outcome  $j$

$I_{jk}$  = the instrumentality of the outcome for attaining the second level outcome  $k$

$V_k$  = the valence of the second level outcome  $k$

Vroom's model has been elaborated on by a number of commentators but the basic multiplicative model, where effort is seen as the product of

expectancy and valence still lies at the heart of expectancy based cognitive choice theories. Although there has been some suggestion that the effects of expectancy and valence on motivation may be additive rather than multiplicative (Kanfer 1990), it is still possible to view expectancy theory in a simple diagrammatic form, as shown in figure 3 a.

Porter and Lawler (1968) have elaborated on the basic model by arguing that both valence, or the value of the rewards, and expectancy, or the perceived effort/reward probability, comprise a number of distinct elements. The value of the reward will be determined by the anticipated level of satisfaction, which results from the combination of the extrinsic and intrinsic rewards and their perceived equity. The perceived effort/reward probability is determined by perceptions about performance, which will in turn be determined by effort, abilities and traits, and clarity of role. Both the value of the reward and the perceived effort/reward probability are informed by a feedback loop from previous organisational experience. Porter and Lawler's model is shown in figure 3 b.

Deci (1972) has challenged the assumption in Porter and Lawler's model that intrinsic and extrinsic motivation is cumulative, arguing instead on the basis of laboratory experiments that contingent rewards reduce intrinsic motivation. This raises the question of whether firms that use PRP may in fact be reducing intrinsic motivation amongst employees.

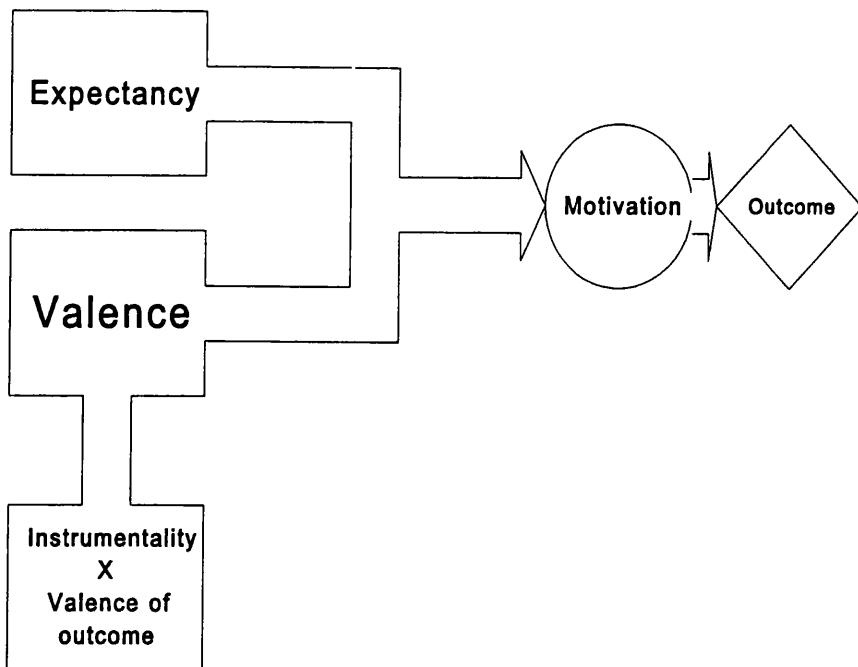


Figure 3 a

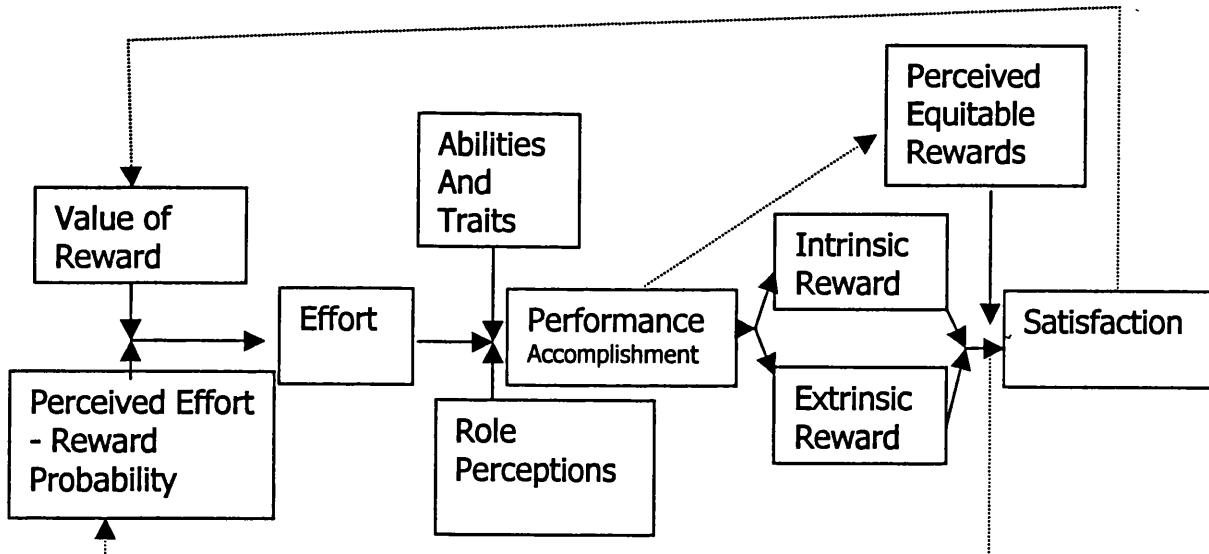


Figure 3 b.

In this thesis Vroom's basic expectancy model has been used in the first instance to test the hypothesis that expectancy theory helps to explain the motivational effects of PRP for two reasons. Vroom's model has the

advantage, over other models such as Porter and Lawler's model, that it is parsimonious. This makes it easier to specify the constructs necessary to operationalise the theory. It is then possible to elaborate on the basic model by adding in elements suggested by Porter and Lawler's model. However, some of those elements provide conceptual and practical difficulties in a field setting.

According to Porter and Lawler's model performance is said to be a function of effort, ability and traits, and role clarity. In practice there are likely to be a number of other variables that affect performance. Organisationally an individual's performance may be interdependent with the performance of others, indeed in larger more complex organisations, it would be unusual for an individual's performance to be completely independent from other members of the organisation. Equally environmental factors, such as the market in which the organisation operates, are likely to have an impact on performance. It is therefore difficult to specify ability and traits in an organisational field setting.

Perceptions about the outcome are fed back in a loop to inform current expectations about the value of the reward and the effort /reward probability or expectancy, in Porter and Lawler's model. Feelings about the outcome are the product of both extrinsic and intrinsic rewards, together with equity considerations. The focus of this thesis is on the motivational effectiveness of expectancy theory in the context of PRP and

not the wider issue of the validity or otherwise of expectancy theory. Consequently the basic assumption has been made that it is the performance payment which is the valent outcome from the employee's point of view, and consideration of the intrinsic rewards of the PRP system have been put to one side. However, Porter and Lawler's model highlights both the equity considerations surrounding PRP and previous satisfaction. This suggests that employees are more likely to be motivated if they perceive the PRP system to be operating fairly, and if their approach to performance is enhanced by positive feelings about their previous experience. The issues of fairness and satisfaction have therefore been looked at as part of the elaboration on Vroom's basic expectancy model.

Some of the most cogent criticism of expectancy theory suggests that it is over-simplistic, and implies that a more rounded approach is needed to understand motivation. Expectancy theory has been criticised on the basis that it is essentially concerned with straightforward choice, while human behaviour is determined in situations where simple choices play little part in determining individual motivation. Benkhoff (1996) characterises expectancy theory as a calculative approach to individual decision making. Benkhoff argues that every day work behaviour often comprises impulsive or habitual behaviour that is not susceptible to a calculative approach. Similarly it has been argued that expectancy theory provides an episodic model of behaviour which does not provide a good

explanation of changes in repetitive behaviour where the variables remain constant (Kanfer 1990). These criticisms suggest that expectancy theory may not paint the complete picture, when it comes to understanding motivational processes. Hence the appeal of a more integrative approach to motivation. Expectancy models such as Porter and Lawler's go some way to addressing this problem by proposing a more complex model of behavioural determinants.

However, in order to understand to what extent and how a particular motivational technique, such as PRP, is working it is important to be able to distinguish the motivational effects of the various elements of the scheme. It is possible to look at the various elements of a PRP scheme by using each of the relevant theories individually, in a way that is not possible using an integrative approach. Expectancy theory focuses on the reward element of PRP, goal setting focuses on the performance targeting, and equity theory looks at the questions of fairness. Using each of these theories in turn allows each of the issues associated with the particular theory to be examined separately.

### Hypotheses

In this Chapter it has been argued that expectancy theory provides at least part of the explanation for the motivational effect of PRP. From this general hypothesis about expectancy theory it is possible to identify a

number of specific hypotheses that address the different models of expectancy theory described in this chapter. Adopting the simplified approach to expectancy theory described above and set out in figure 3 above it is hypothesised that:

Hypothesis 2(a)(I)

*'Individual employee motivation will tend to increase as a result of PRP, where the employee has an expectancy that improved performance will be instrumental in leading to a valent outcome.'*

This hypothesis can be further elaborated, in line with Porter and Lawler's model, by hypothesising:

Hypothesis 2(a)(ii).

*'The explanatory powers of expectancy theory in respect of the motivational effectiveness of PRP will be improved by factoring in Equity considerations'*

And

Hypothesis 2(a)(iii)

*'The explanatory powers of expectancy theory in respect of the motivational effectiveness of PRP will be improved by factoring in feedback.'*

Each of these three hypotheses is tested in a later Chapter using regression analysis to see how far the key elements of expectancy theory identified in the hypotheses go to explain the motivational effectiveness of the Thames Water PRP scheme.

## Chapter 4

### **Goals and Rewards.**

#### **Introduction**

The approach adopted in this thesis has been to distinguish between goal setting and expectancy theory. The importance of the distinction between the key elements of goal setting and expectancy theory from a practical viewpoint is explained in this section. Then the various elements of goal setting are described and the goal setting model, which is used to test the motivational effects of PRP in this research, is identified. Finally, the various attempts to reconcile expectancy theory and goal setting theory are considered.

Goal setting is a theory that comes from the USA, and Locke and Latham (1990) did much of the formative work on it. The author is aware of only one goal setting study done in the UK, (Early 1986), although there have been a number of studies in Israel (Erez 1986). There is however a considerable body of research to support the motivational effectiveness of goal setting theory. Guzzo and Katzell ( 1987) used a meta analysis to compare the effect size from various studies of employee incentive schemes; they found that the variance in effect size for employee incentive schemes was so large as not to be statistically significant; but the same meta analysis

found that goal setting had a strong and significant effect size. Potentially this has important practical implications for PRP. If it is goal setting, rather than the financial incentive, which explains the motivational effects of PRP, then it may be possible for an employer to get the same motivational effects without the need for a financial incentive. In other words, if it is the appraisal system in the PRP scheme and specifically the target setting part of the appraisal system, which affects motivation, then the performance payment may be unnecessary.

Consequently the distinction between goal setting theory and expectancy theory is vital to an understanding of the importance of two key elements of PRP, namely the target setting process and the financial incentive. Cognitive theories of motivation, such as expectancy and goal setting theory, describe the thought processes that affect an individual's effort to achieve a particular outcome. Expectancy theory focuses on the effect that the individual's perceptions about the value of second level outcomes has on that individual's effort to achieve a first level outcome. In contrast, goal setting theory focuses on the process by which an individual determines to achieve a specific achievable outcome or goal, and describes a correlation between the individual's effort and goal difficulty.

Goal setting provides an explanation for individual performance which is related to the individual's intention to achieve a particular goal, and is based on the hypothesis that if goals regulate performance then more difficult

goals will lead to a higher level of performance than easy goals (Locke 1968). As goal setting is concerned with intentional behaviour, it also follows that goal difficulty will only improve performance where the individual has formed the intention to achieve the goal, that is to say where the individual has accepted the goal. The relationship between goal difficulty and performance distinguishes goal setting from other cognitive theories, such as expectancy theory (Vroom 1964), in which performance is related to the expectation of a beneficial outcome.

The first part of this chapter examines two key elements of goal setting, namely goal difficulty and goal acceptance, and the relationship of those two key elements to performance, and identifies feedback as mediating both the relationship between goal difficulty and performance, and goal acceptance and performance. The relationship between goal setting and expectancy theory is then examined in more detail, including specifically the attempts to integrate the two theories.

The approach taken in the literature to goal setting has changed; initially goal setting was portrayed as a technique, as Edwin Locke (1978) put it:

'The concept of goal is not the most fundamental motivational concept, it does not provide an ultimate explanation of human action. The concepts of need and value are the more fundamental concepts and are, along with the individual's knowledge and premises, what determines goals. Goal setting is simply the most directly useful motivational approach in a managerial context'

Goal setting was said to be 'a motivational technique that works!' Evidence to support this contention came from interventions in the American logging industry by Locke and Latham, who proposed goal setting as an inexpensive technique to improve employee motivation and productivity amongst loggers and truck drivers (Locke and Latham 1984). There was a focus in the literature on those facets of goal setting which had a resonance in organisational theory and practice, such as participation (Latham, Mitchell & Dossett 1978, and Dossett et al. 1979), feedback (Hall & Foster 1977, Matsui, Okada & Kakuyama 1982, Locke & Latham 1984, and Pritchard et al. 1988) and the supervisory relationship (Oldham 1975, Locke 1978, and Earley 1986), and the way in which those facets mediated goal difficulty and particularly goal acceptance and goal commitment.

The work on the different aspects of goal setting, such as goal difficulty (Erez & Zidon 1984), highlighted the importance of goal commitment, and the emphasis in the literature shifted from examining goal setting purely as a technique to a more theoretically based examination of the determinants of goal commitment (Hollenbeck & Klein 1978, and Locke, Latham & Erez 1988). The introduction of control theory concepts into the debate on goal setting (Garland 1985, and Hollenbeck & Williams 1987) has in turn led to a move, away from the concentration on goal commitment as the key variable, to the hypothesis that self-efficacy and goal importance are the key variables in the relationship between goal difficulty and performance (Garland 1985, Hollenbeck & Williams 1987, Eden 1988, and Locke & Latham 1990). The

treatment of goal setting in the literature has changed from viewing goal setting purely as a technique or motivational approach to a view of goal setting as a theory of motivation. A number of differing theories of goal setting are explained and compared in the second part of this review. Finally goal setting is contrasted with valence-instrumentality-expectancy theory (expectancy theory) and the attempts to both integrate and distinguish the two theories are reviewed.

### 1. The Key Elements of Goal Setting.

#### a) Goal specification and difficulty.

The relationship between goal difficulty and performance is central to goal setting theory, as it provides a mechanism whereby increased effort can be obtained through external stimuli, namely the setting of specific difficult goals. Locke (1968) found that there is a positive linear relationship between goal difficulty and performance in respect of achievable goals and that specific hard goals produced a higher level of performance than the 'do your best' type of goals; similar results have been found in numerous other studies. For example Dossett, Latham, and Mitchell (1979) found in a field study of clerical workers that there was a significant correlation between goal difficulty and performance ( $r = .53$ ,  $p > .001$ ). Tubbs (1986) in a meta-analysis of previous studies of goal setting concluded that the evidence from previous studies of goal difficulty and specificity was generally so consistently positive that there appeared to be little need to conduct further studies

which looked solely at the issues of goal specificity or goal difficulty. However, there is some evidence that the nature of the goal, in particular the complexity of the goal, may moderate the effect of goal specificity and goal difficulty. Where the goal is simple the effort-performance relationship may be clear; but where the goal is more complex, perhaps involving qualitative targets, a multiplicity of paths to the goal may be presented which will in turn necessitate the selection of a strategy for choosing the correct path, so that the link between effort and performance is mediated by strategy selection. It has been argued by Terborg and Miller (1978) that the majority of the evidence about the effectiveness of goal setting relates to the setting of simple quantitative goals, and that the relationship between goal specificity, goal difficulty, and motivation may not be the same for more complex goals as it is for simple quantitative goals.

Earley, Connolly, and Ekegren (1989) hypothesised that in the case of more complex problems, which required strategy selection, specific difficult goals would impede strategy selection and consequently prove dysfunctional. The hypothesis was tested in a laboratory experiment in which students ( $n=34$ ) were asked to predict the performance of fictitious companies from information provided to them, their predictions were then assessed against performance levels which were generated using a formula. Some of the students were given specific and difficult goals, others were simply asked to do their best. The results showed that those students who had been asked to do their best tried fewer strategies and did better overall at predicting

results, than those students with specific difficult goals. The authors concluded that being given specific difficult goals had resulted in subjects testing more of the possible strategies for predicting the results of the fictitious companies, but that this was dysfunctional because the search for a single best strategy was likely to prove futile, as there were an infinite number of possible strategies. Therefore, they argue that specific and difficult goals will improve performance where either the goal is simple and requires no strategy selection, or where there are a limited number of strategies which can be used to perform the task, so that selection of the correct strategy improves performance, but that in those cases where there are an indefinite number of strategies to choose from specific and difficult goals impede performance. However, given the small number of subjects used in the experiment and the laboratory conditions, these results ought to be treated cautiously. In particular, the time constraint imposed in the laboratory experiment is likely to have limited the time that could usefully have been spent searching for the appropriate strategy far more rigidly than might have been the case in a work environment, so that whilst the search for a strategy may prove dysfunctional against a tight laboratory time limit, it does not necessarily follow that the same would be true in a work environment. In any event there is clearly scope for further examination of the extent to which the nature of the goal moderates the effect of goal specificity and goal difficulty on motivation.

**b) Feedback.**

Feedback appears to moderate both the relationship between goal difficulty and performance, and the relationship between goal commitment and performance. There is evidence that feedback leads to improved performance through three distinct mechanisms, the first of these relates directly to goal difficulty. Locke and Latham's early work on goal setting (1984) suggested that goal setting would be more effective if subjects were given feedback on their performance. Indeed logically it would appear to be a necessary precondition for goal setting to be effective that the individual for whom the goal had been set should have some means of assessing their performance against that goal. Individuals may of course have their own perception of how their performance matches up to a particular goal or they may depend upon informal sources of feedback. Tubbs' (1986) meta-analysis of the evidence from previous studies of goal setting found that feedback did increase the effectiveness of goal setting as a motivational technique, and that goal difficulty was less effective in increasing the motivational effects of goal setting in those cases where there was no feedback.

Secondly, where there is positive feedback, commitment to achieving future goals may be increased by the individual's perceptions of their own ability, that is to say by increased self-efficacy. Hall and Foster (1977) used path analysis on the work of students ( $n = 66$ ) on an 'introduction to business course' to test their hypothesis that there is a psychological success cycle in

which performance leads to psychological success, self esteem, and involvement, thus increasing goal commitment. Student attitudes and performance were measured at two different stages in the course and the results were cross-lagged. Hall and Foster found that their suggested psychological cycle of success was not fully supported by the results, which showed no significant link between effort and performance. However, by using cross lagged correlations Hall and Foster were able to show that good performance leads to increased involvement. These findings support the proposition that positive feedback can affect future goal commitment.

The third way in which it has been shown that feedback can lead to improved performance is where individuals with high achievement needs set higher goals after they receive feedback. Matsui, Okada, and Kakuyama (1982) conducted a laboratory experiment ( $n = 91$ ) where subjects were first assessed for achievement need, and then asked to carry out a simple perceptual task for which they had been asked to set a goal, the task was then interrupted halfway through the allotted time and the subjects were given feedback and allowed to revise their original goal. Those subjects with a higher achievement need performed better after the feedback than those subjects with a lower achievement need, even though there had been no significant difference before the feedback was given. Matsui, Okada and Kakuyama found that the difference in performance was accounted for by the higher goals which were set by the subjects with high achievement needs after they received feedback.

It is not clear how important feedback is in goal setting. Pritchard et al. (1988) found that feedback increased productivity by 50% in a field study they conducted with units of the United States Air Force. The field study started by establishing a baseline performance and then used first feedback, then goal setting, and then incentives, to see how far these interventions increased productivity. The results showed that productivity increased to 50% over the baseline assessment when feedback was introduced, then 75% when goal setting was introduced, and finally 76% when incentives were introduced. However, productivity was measured using subjective assessments and feedback was given through computer generated reports, which included information about the effectiveness of performance against what had been achieved in the past and what was being achieved by other units. The authors point out that this may mean that the feedback system was itself operating as an informal goal setting process, because the information contained in the feedback report in effect gave targets which might be used as goals. Consequently the 50% increase in productivity needs to be treated with caution both because of the way in which productivity has been measured, and because there is a danger that the results are conflating the effect of goal setting with the effect of feedback. Nevertheless, what evidence there is suggests that feedback plays an important role in goal setting and works in a number of different ways.

c) Goal acceptance and commitment.

Goal setting depends upon the individual's acceptance of and commitment to a goal, it has been argued that commitment to a goal includes acceptance of that goal and that it may be better simply to refer to goal commitment (Locke, Latham, & Erez 1988). On the other hand, there is evidence that goal acceptance is a boundary condition for goal setting, that is to say a dichotomous variable, and it is therefore possible to distinguish the effect of goal acceptance from the effect of goal commitment, which is said to be a continuous variable (Hollenbeck & Klein 1978, and Locke, Latham, and Erez 1988). Erez and Zidon (1984) found in a laboratory test of technicians and engineers ( $n = 120$ ), who were asked to carry out a perceptual speed test, that the level of goal acceptance decreased with goal difficulty, but that provided the goal was accepted, the decrease in the level of acceptance did not affect performance which continued to increase with goal difficulty. However in those cases where the goal was rejected the relationship changed to a negative linear relationship between goal difficulty and performance, so that performance decreased as goal difficulty increased. The results obtained by Erez and Zidon suggest that goal acceptance is a boundary condition for goal setting, and that it is of critical importance that the goal is accepted, both to ensure that goal setting improves performance and to ensure that increasing goal difficulty does not become dysfunctional.

A goal may be accepted because it is the individual's own, or because the individual has participated in the setting of that goal, or because it is an

assigned goal, which the individual has accepted. There have been debates both about whether the conditions under which an assigned goal is given affects performance, and about whether participative goal setting improves performance. Goal assignment may influence performance, firstly by increasing the likelihood of a goal being accepted, secondly by creating an environment in which harder goals are set, and finally through increased goal commitment. The nature of the relationship between the person who assigns the goal and the person to whom the goal is assigned may be important; Locke (1978) suggests that the employment relationship may facilitate the assignment of goals, because the employee's mental set will be 'what do you want me to do?', so that the ease with which an assigned goal will be accepted will depend on the perceived legitimacy, fairness and difficulty of the goal and the level of trust with which the employee views the manager. If Locke is right then the nature of the employment relationship may increase performance by facilitating goal acceptance. In a laboratory experiment ( $n = 48$ ) to test the importance of supervisory characteristics in determining the effectiveness of goal setting, Greg Oldham (1975) found that the individuals' perception of the legitimacy of the assignment of the goal and the trust with which the supervisor is viewed affected reported goal commitment, but not the performance. However, Earley (1986) found in a field study of workers ( $n = 120$ ) in the United States and England that workers in England who received goal related information from their shop steward showed a higher level of goal acceptance and performance, than those English workers who only received goal related information from their

supervisor, Earley attributed this to the greater level of trust the workers had in their shop stewards. The findings from Earley's field study suggest that the level of trust may effect performance and can be contrasted with Oldham's findings (1975); it seems likely that the field study results are more reflective of real life than the experiment, particularly in relation to the effect of trust. However, it is unclear from Earley's results whether the greater level of trust workers had for shop stewards led to improved performance because there was a higher rate of goal acceptance or because the level of goal commitment was increased.

Participative management systems are said to improve organisational performance by increasing commitment (McGregor 1957, Lawler 1986), participative goal setting might therefore be thought to result in higher goal commitment, which would in turn lead to improved performance. However it turns out that the bulk of the evidence suggests that participative goal setting leads to improved performance because harder goals are set through participation in the goal setting process, and not because participation increases goal commitment. In a longitudinal field study of engineers and scientists working for a research and development department in a large international corporation, Latham, Mitchell and Dossett (1978) found that participative goal setting tended to result in harder goals being set than those that were assigned. There was a positive linear relationship between goal difficulty and performance ( $r=.79$ ,  $p<.001$ ), consequently those subjects with participatively set goals performed significantly ( $p< .01$ ) better

than either those subjects who had been urged to do their best or the control group, while those subjects with assigned goals did not perform significantly better than the control group or subjects who had been urged to do their best. These results were equivocal on the question of the importance of participation, because it was not clear how far goal difficulty, which was greater for those with participatively set goals than for those with assigned goals, had influenced the results. The same authors conducted a further longitudinal field study (Dossett, Latham & Mitchell 1979) this time using female clerical staff comparing the effects of participative goal setting to assigned goals. When goal difficulty was held constant, there was no significant difference in performance between subjects with assigned goals and those subjects whose goals were set participatively. These results lend support to the authors' contention that the differential results obtained in the field study of engineers and scientists may well have reflected the harder goals set through participative goal setting, further support for this proposition can be found in a meta-analysis of previous goal setting studies undertaken by Mark Tubbs (1986), although there were only six previous studies in which goal difficulty had been held constant.

Erez and Arad (1986) argue that the results from studies of participative goal setting are inconsistent and that participation in the goal setting process can increase the motivational effects of goal setting in certain circumstances. They point out that the results obtained by Latham and his colleagues from Washington University are based on a dyadic process of participation, which

may not capture some of the effects of group participation particularly the information sharing associated with group participation. Erez and Arad argue that the improved information available to individuals through group participation differentially affects quality and quantity of performance. Their hypothesis that group participation would lead to improved performance was tested using a laboratory experiment where goal difficulty was held constant, and performance was analysed in terms of quantity and quality, the results showed a significant main effect for group participation both in terms of quantity and quality of performance and that quantity and quality of performance was significantly correlated ( $r=.23, p<.05$ ) for subjects whose goals were set participatively. It is interesting to contrast these results with those obtained in the other studies, a distinction can be drawn between the previous work which has focused on goals being participatively set in a one to one environment and this study which has looked at goals being set in a group environment.

## 2. Goal Setting Theories.

### Theories of goal commitment.

A number of these elements of goal commitment have been brought together in a theory of goal setting by Locke, Latham & Erez (1988), who argue that performance is the product of two independent variables, goal content and goal commitment, and that goal commitment is the result of both external, interactive and internal factors. In this model of goal

commitment, the external factors which determine goal commitment are the authority of the person assigning the goal, peer group pressure, and the promise of rewards and incentives; the interactive factors which determine commitment are participation and competition; the internal factors which determine commitment are self-efficacy and self-administered rewards such as self-generated feedback. The authors argue that participation does increase commitment, and that previous studies have tended to underestimate the effect of participation, both where the procedures used have limited the range of goal commitment amongst the experimental groups and where the assigned goals have been 'sold' to participants.

Locke, Latham, and Erez's model draws on existing material on goal setting and the authors do not provide any further evidence to support their model. A somewhat different approach has been adopted by Hollenbeck and Klein (1978) who argue that commitment is a key variable, which moderates the relationship between goal difficulty and performance, and is the product of the attractiveness of goal attainment and the expectancy of goal attainment, where both the attractiveness of goal attainment and the expectancy of goal attainment are determined by both personal and situational factors. This expectancy theory model of the goal commitment process was not tested by Hollenbeck and Klein, although they speculated that it could be used to reinterpret inconsistencies in previous goal setting studies. Klein (1991) has subsequently carried out further work on integrating expectancy and goal setting theories using students (n=252) in a classroom setting, and the

results from that study show that expectancy and attractiveness are inter-correlated with goal commitment, although only attractiveness accounted for a significant increment of variance in goal commitment. These results provide only limited support for the expectancy model suggested by Hollenbeck and Klein (1987).

#### Goal importance and personal goals.

The use of control theory concepts in goal setting, and greater emphasis on self-efficacy and personal goals are evident in some of the more recent theories of goal setting. These theoretical models are based on the premise that goal setting improves performance in a number of ways (Earley & Lituchy 1991). First of all goal setting gives a sense of purpose and direction to performance, in addition the process of goal setting conveys a normative expectation of what can be achieved. Secondly the gap, between what the individual does and that individual's goal, acts as an incentive as the individual seeks to reconcile the two in order to avoid feelings of self-dissatisfaction. The improved performance resulting from the goal setting process will further enhance the individual's feelings of self-efficacy, which will in turn mediate the goal setting process. Central to this understanding of goal setting is a move away from goal commitment as the key variable in the goal setting model, to personal goals and self-efficacy.

Hollenbeck and Williams (1987) argue that not all goals will be given the same importance and that performance is determined by goal level, self-

focus and perceived goal importance. In their model of goal setting, the individual is motivated through a negative feedback loop to seek to reduce the discrepancy between the goal that has been set and actual performance, and this motivation will be stronger the more important the goal is perceived to be and the more self-focused the individual is. Goal importance is the level of importance the individual attaches to a particular goal relative to that individual's other goals and self-focus is the measure of how far an individual is focused on self rather than the external environment. In a longitudinal field study of sales staff employed by a department store, conducted by Hollenbeck and Williams (1987), the interaction between goal level, goal importance, and self-focus was found to be statistically significant ( $p<.05$ ) and together with the main effect of goal level explained 17% of the variance in sales level. Goal levels in this study were set by the sales staff themselves and the selection of goal level turned out to be a function of the individual's perceptions of past performance, self-focus, and perceived goal importance, so that goal importance and self-focus also improved performance because they led to more difficult goals being set.

Earley and Lituchy (1991) have tested three models of goal setting which use self-efficacy and personal goals to mediate the relationship between assigned goals and performance. In the first model, proposed by Locke and Latham (1990), self-efficacy and personal goals fully mediate the relationship between goals and ability, and performance. In the second model Garland (1985) suggests that self-efficacy and performance valence fully mediate the

relationship between personal goals and performance. Performance valence is the anticipated satisfaction with performance and Garland argues performance valence will decrease the more difficult the goal, so that there is a negative relationship between performance and performance valence. The third model, suggested by Eden (1988), hypothesises that it is assigned goals and trait efficacy, rather than ability, which are mediated by self-efficacy and personal goals. Trait efficacy refers to the more generalised feelings that an individual has about their ability, than the specific expectancy about performance that is described by self-efficacy. Earley and Lituchy (1991) subjected each of the three models to two laboratory experiments, using tasks of varying complexity, and a field study in a classroom environment. The data from the tests was analysed using hierarchical regression, path analysis, and three tests of fit; namely chi-square, goodness of fit, and parsimonious goodness of fit. The results show that Locke and Latham's model and Eden's model were better predictors of performance than Garland's model in each of the tests, and that Locke and Latham's model was the most parsimonious of the three models. The studies also consistently found that performance valence added no significant variance to the prediction of task performance. On the other hand, while trait efficacy was not supported by the results of regression analysis, it was supported by path analysis, from which Earley and Lituchy concluded that trait efficacy may be playing some more subtle role in predicting performance level. Overall the comparison appears to lend most support to Locke and Latham's model of goal setting, which explained 78%,

35% and 21% respectively of the variance in performance for the first, second and third studies, as compared to Eden's model which explained 65%, 22%, and 27%, and Garland's model which explained 62%, 34%, and 9%.

### Hypothesis

It is not practical to investigate all of the intricacies of goal setting in a survey based, cross-sectional study of PRP, consequently a simplified model has been adopted. The key question so far as PRP is concerned is does goal setting theory provide an explanation of the motivational effects of PRP, and if that is the case is Performance Management without the financial element of PRP a more robust motivational system than PRP? For the purpose of this research the key elements of goal setting theory have been reduced to the following hypothesis:

#### Hypothesis 2 (b)

*'In so far as goal setting theory explains the motivational effectiveness of a PRP scheme, individual employee motivation will be directly and positively related to goal difficulty for specific goals to which the employee is committed.'*

Unless there is a relationship between goal difficulty and motivation, goal setting theory can not help to explain the motivational effectiveness of that particular PRP scheme. That is not to say that the particular PRP scheme could not be improved by applying the principles of goal setting. However it

does mean that in so far as the scheme is effective at motivating employees it is other elements of the scheme rather than goal setting, which will explain this.

It can be seen from the preceding chapter that goal setting is not simply about goal difficulty, a number of other points have emerged which may have a bearing on the effectiveness of the PRP scheme from a goal setting perspective. Employees clearly need to be committed to achieving the goals that are set for them, but there is some suggestion that participatively set goals may be more effective than assigned goals (Erez & Arad 1986). The number of goals set may also mediate the effects of goal setting, with fewer goals allowing for easier strategy selection, which in turn appears to make goal setting more effective (Earley, Connolly & Ekergren 1989). Finally, feedback appears to be another key element in the goal setting process, giving cues about appropriate levels of performance and enabling employees to focus on goal achievement. Each of these three issues regarding goal setting will be examined in addition to the goal-setting hypothesis.

### Goal setting and expectancy theory.

Intuitively, there appears to be a fundamental difference between goal setting and expectancy theory. Goal setting theory postulates that effort will increase in direct relation to the increase in goal difficulty for specific achievable goals. Consequently it is goal difficulty that is the driver which

increases motivation. In contrast, expectancy theory states that motivation is a product of valence and expectancy. So that for expectancy theory it is the perceptions about the effort/reward relationship and the value of the reward which drive motivation. This in turn means that goal setting theory focuses on issues around the goal setting process, such as goal commitment and goal specification. Whereas, expectancy theory is concerned with the effort/reward relationship and specifically the instrumentality of that relationship, that is to say the link between increased effort and reward. Sometimes it is suggested that goal choice and goal commitment are affected by valence instrumentality and expectancy. Whether this is true or not, does not affect the fundamental distinction between goal setting and expectancy theories, both theories still depend upon different drivers and focus on different aspects of the task setting process.

There have been several of attempts to reconcile the expectancy and goal setting theories, which fall into two camps. Some commentators have tried to reconcile the conflicting evidence about the explanatory power of the two theories. Other commentators have tried to reconcile the two theories as part of a wider search for an overall theory of work motivation. Looking first of all at attempts to reconcile the evidence about the explanatory effects of the two theories, it is apparent that the arguments concern methodological issues rather than the fundamental differences in the two theories. Locke and Latham (1990) argue that there are two ways of reconciling the evidence about goal setting theory and expectancy theory. First of all, they

show that the positive correlation between goal difficulty and performance, and the negative correlation between expectancy and performance, is the result of the flawed methodology used in a number of studies. The difficulty with these studies is that they conflate group and within group results for both expectancy and goal setting. Subjects are allocated different goals and then they are asked to rate their expectancy of goal attainment. Locke and Latham (1990) argue that the problem arises because the data analysis does not distinguish between the groups which have been allocated different levels of goal difficulty. They say that this between group level of analysis captures the effects of goal setting, because the level of goal difficulty distinguishes the groups. But it fails to give a true picture of the effect of expectancy, as the expectancy data is distorted, because comparisons are being made between individuals who have been assigned different levels of goal difficulty. They show that for subjects with the same level of goal difficulty, expectancy is correlated to performance. Effectively Locke and Latham are able to show that it is possible to get a positive correlation between both goal difficulty and performance and expectancy and performance from studies which had previously shown a negative relationship between performance and expectancy, by using within group studies for groups that have been assigned the same level of goal difficulty.

The second approach adopted by Locke and Latham is to substitute self-efficacy for expectancy in the studies. The essential difference is that this effectively allows subject's assessments of their likely performance to cover a

range of different levels of goal difficulty. This methodological change also creates a positive relationship between performance and both goal difficulty and expectancy. However, this second approach also involves a conceptual change from expectancy to self-efficacy, a concept developed by Bandura (1986), that does not resolve the fundamental theoretical differences between expectancy and goal setting. So that while Locke and Latham's attempts to reconcile goal setting and expectancy theories raise some interesting methodological issues in respect of studies which attempt to compare both theories, they do not provide any satisfactory reconciliation of the underlying concepts in the two theories.

On the other hand, attempts to integrate goal setting and expectancy theories into one overall theory of work motivation have been concerned more with the structural and theoretical issues, than problems over methodology. One approach to integrating the various work motivation theories has been to simply combine the theories together, in what Kanfer (1990) describes as the amalgamation approach. Potentially amalgamation improves the predictive ability of the theories and should allow for the identification of redundant constructs. Amalgamating goal setting and expectancy theory does not reconcile the fundamental differences between the theories. Other attempts to produce an integrated model of work motivation theory have involved the construction of new models, which draw on established theories of work motivation. Kanfer (19..) describes this as the new paradigm approach. Kanfer and Ackerman (1989) suggest a model

which includes both expectancy and goal setting elements. These two elements of the model help determine the resources the individual allocates to task performance at different stages in the motivational process. Thus expectancy which Kanfer and Ackerman divide into effort-utility and performance-utility, is both a distal and proximal process. Goal setting on the other hand is a proximal process determining the immediate allocation of resources to the task, in their model. The distinction between proximal and distal affects of the constructs from the two theories shows that it is possible to build a model utilising concepts from goal setting and expectancy at different stages in the model; it does not reconcile the fundamental difference between the two theories.

Notwithstanding the arguments advanced to unify expectancy and goal setting theories, it is difficult to see how they can be reconciled, given the fundamental difference between the focus on the outcome of goal achievement and the difficulty of achieving the goal. Indeed the findings from a study by Lee, Locke and Phan (1997) suggest that PRP type incentives may reduce the effectiveness of goal setting. The extent to which goal setting and expectancy theory can be reconciled has been examined in this thesis using the data from the research into the Thames Water PRP scheme. The data has been analysed to see how far goal setting and expectancy theories have a cumulative explanatory effect. If the two theories are, as Locke and Latham suggest part of the same process, with expectancy explaining goal choice and commitment in what is essentially a

goal setting model of motivation, then they should have a cumulative explanatory effect. The cumulative effect will arise because one theory, expectancy, explains goal choice and commitment, and the other uses goal difficulty to explain the additional effort utilised to achieve goals to which the individual is committed. Likewise, if goal setting and expectancy theories are proximal and distal parts of amalgamation theory, their explanatory powers should also be cumulative. In this thesis it is argued that there is no cumulative effect because these are distinct theories of motivation which focus on different drivers.

#### Hypothesis 2 (c)

*'Goal setting and expectancy theory will not be cumulative in the extent to which they explain the motivational effectiveness of the Thames Water PRP scheme.'*

This research attempts to utilise the fundamental differences, between goal setting and expectancy theories, to see whether it is possible to identify which elements of a particular PRP scheme are most effective in motivating employees. From a practical point of view by highlighting those elements of the process that are motivating, for at least some employees, it should be possible to suggest areas where the PRP scheme might be improved. Expectancy and goal setting focus on the financial rewards and task setting process. The next chapter looks at broader issues of fairness and organisational change.

## Chapter 5

### **The impact of the wider work group.**

#### **Introduction**

The theories of motivation that have been considered so far focus on the individual and their approach to goals and rewards, the next step is to consider the impact of the wider group on motivation at work. This starts with an examination of equity theory and then goes on to describe other aspects of group motivation such as corporate culture. A model for cultural motivation is suggested.

The two work motivation theories which have been described in detail so far, goal setting and expectancy theory, are both concerned with the individual's relationship with task and outcome. Goal setting theory predicts an association between goal difficulty and individual effort. Expectancy theory is based on the relationship between an individual's effort and that individual's perceptions about the value of the reward for task performance. It has been evident from some of the earliest studies of work motivation<sup>1</sup> that there may, however, be wider social influences on the level of effort individuals commit to a particular task.

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<sup>1</sup>e.g. the Hawthorne studies show how group norms can regulate productivity (Roethlisberger & Dixon 1939).

In the workplace PRP has clear social implications, firstly because it purposefully differentiates the reward given to employees doing the same job, where it is judged that there is a difference in their contribution. This differentiation is intended by the employer to provide a clear message about the value that the employer places on the employee's contribution. Employees are likely to compare the level of reward they receive, for their effort, to the level of reward received by others, whom they feel are in a comparable position. If the employee believes that the relative performance assessments are fair, then that might have an incentive effect, either because employees try to do better than other work colleagues, or because the performance of other work colleagues inspires them to work harder. However, employee perceptions about the relative merits of the contributions made by them and their colleagues may not be the same as those of the employers, or they may believe that the system is in some way unfairly fixed. In either case there is a danger that the PRP scheme might have unintended consequences in terms of work motivation because it is believed to be unfair.

Equity theory provides an explanation of how an individual's perceptions about the fairness of a reward system might affect motivation. In addition, any doubts an individual has about the fairness of the system are also likely to affect the individual's belief in the effort reward relationship and, consequently, the motivational effectiveness of the reward.

Secondly, PRP is frequently used as part of a programme of cultural change (Kessler 2000). It is not clear precisely how PRP can change corporate culture, or indeed whether it is effective in doing so. But the underlying assumption appears to be that by aligning the cultural norms within the organisation to the achievement of organisational goals individuals will improve their performance in order to achieve those organisational goals. The issues surrounding this process are considered in more detail later in this chapter and a model for cultural change is suggested. But first of all equity theory is considered in more detail.

### Equity theory

Equity theory (Adams 1965) is essentially an exchange theory (Brown 1986). It is based on the premise that people expect that the outcome from a particular input will be comparable to the outcomes enjoyed by social comparitors from similar inputs, but unlike many economic exchange theories, it recognises that the individual's judgement may be based on imperfect knowledge. Thus it is individual perceptions about the inputs and outcomes for themselves and others that determine the judgement that individuals then make about the comparative value of the input/outcome ratio for themselves and others.

Equity theory focuses on the comparison of the ratio between inputs and outcome. It is not concerned with the objective assessment of the value of outcomes against inputs. Adams expressed the theory by postulating that there was equity when:

$$\frac{O_p - O_o}{I_p - I_o}$$

But not when  $\frac{O_p}{I_p} > \frac{O_o}{I_o}$  or  $\frac{O_p}{I_p} < \frac{O_o}{I_o}$

Where: O=outcome and I=input

According to equity theory the individual will act to remedy inequitable comparison with a referent group in one of a number of different ways. Individuals may seek to vary the inputs or outcomes, or cognitively distort the inputs or outcomes, or they may quit, or act in relation to referents. Choices about which course to take are made depending on the strength of the perceptions about injustice, situational and individual constraints on action, and individuals' perceptions about the choices open to them. Clearly motivation comes into play when individuals seek to alter their inputs. However, the individual is not restricted to simply varying inputs in response to inequity, and they may make cognitive changes to the comparative ratio of inputs to outcomes, which do not affect motivation.

The two principal difficulties in applying equity theory are, firstly determining who constitutes the relevant referent group for any individual, and secondly predicting what counterbalancing action an individual will take to remedy an inequitable situation. Individuals may have quite different perceptions about who they ought to compare themselves with for reward purposes. One person may feel that the relevant group is their colleagues at work, while for someone else it may be a circle of friends from school or college. Intuitively it might be assumed that the principal reference group for most employees is likely to be colleagues working for the same firm and doing similar work. However, Dornstein (1988) found, in a study of blue and white collar employees in Israel, that the most important referent group tended to be others in similar occupational categories working for other firms.

Nevertheless, in relation to PRP and any assessment of the motivational effectiveness of PRP, it is reasonable to use other work colleagues as the relevant comparitor. PRP purposefully differentiates pay for individuals, doing the same work, where those individuals' performance is judged to be different. Some researchers have suggested that PRP may in fact demotivate employees, presumably because the employer's assessment of performance is felt to be unfair in some way (Marsden and Richardson 1994, Isaac 2001, Kellough & Nigro 2002, and Brown & Benson 2003). Equity theory provides an explanation of how differences in pay might demotivate employees. It also provides a mechanism for testing the impact of pay

differentiation, based on performance assessment, on individuals, particularly where their judgement about the relative merits of their performance, compared to that of other work colleagues, is different from their employer's. It is clearly relevant to have regard to individual perceptions about the input to outcome ratio of work colleagues when looking at PRP because that distinction is a direct and intended consequence of PRP.

The problem over what counterbalancing steps an individual might take to remedy a perceived inequity is somewhat more difficult to resolve. If the perceived inequity is responded to by varying inputs this has a clear motivational effect. But if, on the other hand, a perceived inequity leads to cognitive distortion, the individual's own performance may not be affected, that is to say there may be no impact on motivation. This makes it difficult to predict the response that an individual will make to a perceived inequity. Indeed one of the criticisms of equity theory is that the theory can be interpreted flexibly to fit whatever research results are produced (Locke & Henne 1986) because it does not provide a clear cut prediction about the individual's response to inequity. In addition, the research evidence suggests that individuals do respond to what they consider to be underpayment (Berkowitz et al. 1987), but they are less likely to respond to overpayment (Mowday 1991). In other words the research shows that employees who think they are being underpaid are likely to work less hard,

but that employees who think they are overpaid are less likely to increase their work effort.

Two assumptions have been made in order to generate a workable hypothesis about the impact of an individual's perception concerning the distributive equity of a particular PRP scheme on motivation. The first one is that the employee will use as a comparator group other employees employed by the same employer who are in receipt of PRP. This assumption reflects the fit between equity theory and pay differentiation in PRP. The second assumption is that employees will change the level of input they are making in response to any perceived inequity. Essentially the thesis is concerned with the motivational effectiveness of PRP. If the employee responds to inequity in the pay system by cognitive distortion or other action in respect of the referent group, that does not affect their motivation. On the other hand, if the inequity in pay is reconciled through a variation in the level of input, then that means that it is having a direct impact on motivation. The effects of employee perceptions about distributive equity on motivation can be hypothesised as:

Hypothesis 2 (d)(i).

*'Where employees believe that other employees of the same firm are being paid comparatively more for their effort, they will be demotivated.'*

## Procedural Equity

Adam's equity theory is concerned with individuals' perceptions about the level of benefit of the input outcome ratio to them, or what is termed distributive equity. Greenberg (1987) has argued that in addition to distributive equity individuals are also concerned about procedural equity, that is to say the fairness of the procedure, which is used to determine what outcome is going to be. Indeed it has been suggested that procedural fairness may be as important as distributive fairness (Cropanzo and Folger 1991). The evidence from Greenberg suggests that where the individual is receiving a medium to high level of reward, compared to others procedural equity will not be particularly important: where however the rewards are comparatively poor procedural equity becomes much more important in determining the individual's perceptions of inequity. In other words, employees who are well paid are less likely to be concerned about the fairness of the payment system than those who are not well paid. On face value the approach of highly paid corporate executives and city traders to pay does not seem to support this proposition. These highly paid individuals appear to be very sensitive to pay comparisons.

Procedural fairness is an important issue in PRP systems, because PRP depends upon a subjective assessment of the individual's performance and the reward that performance should attract. The obvious danger is that the assessment will be tainted by considerations other than the

individual's work performance. PRP could, for instance, foster a 'blue eyed boy syndrome' or halo effect, where an employee who is viewed favourably for some other reason, perhaps because of their readiness to agree with their manager, is unfairly assumed to perform well without any objective justification. Many PRP schemes include specific rules about the criteria which should be used in assessing an individual's performance, and indeed it is common for assessments to be subject to review or ratification by another manager within the organisation; this manager is sometimes termed the 'grandfather'.

Once an individual's performance is assessed, the other danger is that the level of payment might be influenced by external considerations. One of the fears expressed by revenue staff about PRP (Marsden and French 1998) was that their assessments were being overridden by more senior managers in order to comply with an imposed quota for the number of employees who should receive additional payments. In fact, some schemes specifically impose a quota distribution on the number of staff who can be assessed as falling into each category (eg London Docklands Development Corporation had such a scheme). From the employer's point of view a quota system helps to control wage costs and acts as a check on managers, who might otherwise tend to be too extreme, one way or the other, in their assessment of their employees' performance.

These procedural equity issues also impact on the employee's expectancy that an improved performance will lead to an increase in pay. The research evidence suggests that procedural equity affects employee perceptions about the PRP outcomes (St-Onge 2000, and Siegall & Worth 2001). From a theoretical perspective this may be the result of direct equity consideration and also the perceived instrumentality of the PRP process. If the assessment is thought to be influenced by factors other than the individual's performance, or if the payment is determined by a quota system, then that breaks the expectancy link between performance and pay. Consequently there is a twofold impact on motivation where there is procedural inequity. Firstly, according to expectancy theory the motivational effects of the performance payment will be nullified. Secondly, procedural inequity will itself demotivate employees or cause other adverse effects amongst employees (Brown & Benson 2003).

It is therefore hypothesised that:

Hypothesis 2 (d)(ii).

*'Where employees perceive that there is procedural inequity in the PRP scheme they will be less motivated.'*

### PRP and Cultural Change

There is a view that if a firm gets its corporate culture right, that will improve the firm's performance. It is unclear whether or, indeed, how firms can improve their performance by changing their corporate culture.

Nevertheless numerous organisations have introduced cultural change programmes in order to improve their performance. PRP is often introduced as part of a cultural change programme (Kessler 1994). In order to understand how PRP could act as a catalyst for cultural change, a number of issues need to be addressed. Firstly, what is meant by corporate culture? How can having the right or appropriate corporate culture improve an organisation's performance? How can culture be changed and what part can the introduction of PRP play in changing culture? And finally how can these processes be measured?

Corporate culture is a complex issue and there is a considerable body of literature on this subject. In a thesis primarily concerned with PRP and motivation, it is not practical to do justice to the extensive research on this subject. Instead the focus in this thesis is on producing a model explaining how the issue of corporate culture and performance interact.

### Defining corporate culture

Schein (1992) sees corporate culture as a set of psychological predispositions, which are evidenced by multiple layers within the organisation. At the top layer there are the artefacts, that is the visible signs of organisational culture; under that there are the organisation's perspectives, that is socially shared rules for dealing with common problems. The bottom two layers of organisational culture comprise

shared values and the assumptions employees make about themselves and others within the organisation, as well as the organisation itself. Looked at in this way culture appears to be a complex web running through the organisation. Schein says that one of the key factors in determining corporate culture is top management.

Some commentators have focused even more closely on culture as the product of management activity. Denison (1990) for instance defines corporate culture as: 'the underlying values, beliefs and principles that serve as a foundation for an organisation's management system as well as the set of management practices and behaviours that both exemplify and reinforce those principles.'

The emphasis in this definition is on management and management systems. Yet culture can be seen from a number of different perspectives, so that a shopfloor perspective on culture may be different from a management perspective. The differences in approach have been characterised (Martin 1992) as integration, differentiation and fragmentation. Integration is concerned with a single cohesive corporate culture. Differentiation argues for a number of different cultures in one organisation to accommodate the sub-cultures, whether they are rooted in different parts of the organisation or different levels of hierarchy. Fragmentation is a reflection of a lack of consensus and complexity in organisational culture. In looking at culture and pay systems it is logical

to adopt an integrationist approach on the basis that pay as a mechanism for cultural change is part of a top down or management approach to cultural change.

### Improving organisational effectiveness

Some management writers like Peters and Waterman (1982) have suggested that firms simply need to copy successful organisations in order to succeed. The assumption seems to be that successful firms all have the same culture. The difficulty with this inductive approach to the question of cultural effectiveness is that it has proved notoriously difficult to identify firms that will succeed in the long term. Some of the firms identified by Peters and Waterman as successful, subsequently proved to be less successful; IBM was one example. The selective basis on which firms have been chosen has also been criticised. By focusing on only some successful firms, Peters and Waterman omitted other firms, which have been successful with a different approach to organisational culture. More importantly, as Brown (1995) points out it is possible to identify successful firms that have a very weak culture and firms that face serious problems despite having a very strong culture.

Denison (1990), on the other hand, adopts a deductive approach to cultural effectiveness and hypothesizes that the effectiveness of an organisation will be determined by the extent to which the organisation's

policies, practices, beliefs and values mesh together and fit the business environment. As Denison puts it:

'Effectiveness is a function of the interrelation of core values and beliefs into policies and practices, and the business environment of the organisation.'

Denison argues that there are four mechanisms or hypotheses that an organisation needs to utilise in its cultural strategy in order to succeed.

The first hypothesis is that employees need to be involved, that is to say committed to the organisation that they work for. Involvement leads to consensus about core values, which in turn lowers transaction costs as employee action is intuitively guided by core values, thus minimising the need for rules and regulations. This leads on to the consistency hypothesis, which predicts that an organisation will benefit from better co-ordination and communication of shared values, provided those shared values are congruent with the business environment. These first two hypotheses are characterised as internal, that is to say they are concerned with how the organisation deals with internal cultural issues. One, involvement, is about how change is brought about, and the other, consistency, is about how stability and direction are achieved.

Effectively, Denison's internal hypotheses are concerned with creating and maintaining organisational commitment. Commitment is a complex concept which can be seen from a number of different perspectives (Swales 2002) however for the purposes of this thesis Kanter's definition has been adopted:

'the willingness of social actors to give their energy and loyalty to social systems, the attachment of personality systems to social relations which are seen as self expressive.' (Kanter 1968, p499)

If employees believe in the same values as their employer, and those values are co-ordinated and communicated through the organisation, as Denison suggests, employees will believe in that organisation, because it shares the same values as them, and that means that they will be committed to that organisation. Employees, who are committed to their employer and the employer's values are not only going to reduce transactional costs of internal communication, but may also be intrinsically motivated to work harder for the employer (Brown 1995, and Gallie, Felstead & Green 2001). Commitment not only means that the organisation needs fewer rules because employees intuitively understand what the organisation wants them to do, it should also mean that employees will be motivated to work harder because they identify more closely with the employer and the employer's objectives.

Denison's other two hypotheses are concerned with how the organisation deals with the external environment. Change and flexibility are maintained by adapting to the changing business environment by responding to both internal and external customers. According to Denison it is important to be able both to restructure and re-institutionalise. In other words whilst the ability to adapt to change is important, it is also important to avoid the so called balkanisation of an organisation. This seems to be somewhat akin to Schein's (1978) idea of

cultural change being a process of unfreezing and refreezing the organisation's culture. Finally, Denison argues that stability and direction are given to the organisation by its mission, that is some statement of what the organisation is about and where it intends to go.

Brown (1995) argues that an organisation with a strong culture will not necessarily be a successful organisation. Organisational effectiveness depends on cultural fit, that is to say the fit between the organisation's culture and its business environment. This is similar to Lawrence and Lorsch's (1967) hypothesis about the contingent nature of successful corporate strategy. There is no one right culture; culture should be appropriate to the nature of the organisation and the business environment that it is operating in. Brown says that culture can affect organisational effectiveness by increasing employee commitment, because employees are more likely to work harder for a firm they identify with.

Each of the three approaches to organisational effectiveness identified above is concerned with increasing the organisation's performance. Peters and Waterman leave the precise mechanism by which this is achieved is opaque; their approach is simple, copy the best. Denison and Brown both suggest a theoretical framework to explain how corporate culture can improve effectiveness. In effect both focus on commitment to explain how organisational culture can improve performance internally,

that is to say through the contribution made by employees. Commitment cuts down on the costs of communicating within the organisation, minimising the need for bureaucratic rules. At the same time, employees working for an organisation which reflects views that they subscribe to will be more intrinsically motivated to work for that organisation.

### Cultural change

Schein (1992) suggests that cultural change is a process of unfreezing corporate culture, learning a new culture and refreezing. Some commentators have suggested that cultural change comes about as a result of some organisational crisis, which throws the existing order into doubt. The problem it is argued is that the existing culture has a certain amount of inertia that makes it difficult to displace. Generally cultural change is seen as a top down process, sometimes starting with a change in leadership at the very top of the organisation. The actual mechanisms used to achieve cultural change often draw heavily on the various levers of change generally associated with HRM. Brown (1995) emphasises the need for consistent cues, as with HRM the focus is not on one particular policy, but on an overall strategy. The difficulty is in predicting the precise outcome of a particular strategy. As Brown (1995) puts it:

'if you want to create a culture of, for example, highly competitive entrepreneurs, then make sure your reward system rewards competitive and entrepreneurial behaviour... while this strategy may sound simple and obvious it is in fact neither. In the first place it is extremely

difficult for organisations to correctly analyse the full implications of, for example, a reward system'

### PRP as a mechanism for achieving cultural change in an organisation

Pay is widely recognised as an important tool in bringing about change in organisational culture (Drennan 1992, Kessler 1994, and Brown 1995).

PRP sends a particularly strong message to employees about the importance that the employer places on performance because it specifically relates pay to performance. As Kessler and Purcell (1992) observe, PRP has been widely used amongst newly privatised companies in order to create a more market orientated culture. However, the precise effects of PRP and its effectiveness as a means of achieving cultural change are less clear. As Kessler (at p.490, 1994) puts it,

'It is notoriously difficult to isolate and assess the impact of any pay system'. An effective PRP scheme might logically be assumed to send a clear message about the importance that the employer attaches to performance. Furthermore, if the PRP scheme cascades the firm's key objectives down through the organisation, as key targets which need to be achieved in order to earn a performance payment, then that should reinforce those objectives for employees.

On the other hand, a PRP scheme that failed to motivate employees might have a different effect. If employees see no benefit in working harder to achieve the performance targets that they are set, it seems

unlikely that they will attach much importance to the messages that are associated with those performance targets. Consequently it can be hypothesised that a PRP scheme that failed to motivate employees might have unintended and unattractive consequences in terms of cultural change. Given that so much of the UK evidence is that PRP schemes are not particularly effective at motivating employees this is an important point.

### Measuring cultural change and its effectiveness

Much of the work done on organisational culture has been qualitative in nature comprising detailed case studies. Denison (1990) uses quantitative methods to test his hypothesis, but the level of analysis used is the firm. On the face of it, this would seem to be the natural level of analysis at which to study the overall effectiveness of a particular organisational culture or programme of change. Looking at the firm as the unit of analysis makes it difficult to disaggregate the effects of the various elements of cultural change programmes and assess their effectiveness separately.

However, there are a number of issues that have been identified above which would appear to be susceptible to analysis at the level of the employee. Firstly, while culture is a complex concept, cultural change is essentially about changing employee beliefs about the firm and their

relationship to it and their values. Secondly, for cultural change to be effective it should increase employee commitment. Thirdly, employee commitment should lead to improved employee motivation. Finally, if PRP is a mechanism for achieving cultural change, it is more likely to be successful in changing culture in those instances where it is also successful in increasing employee motivation. This in turn means that the PRP scheme should be more likely to increase the motivation of employees who become more committed to the employer, through the programme of cultural change.

This three-stage analysis of cultural change can be tested using three hypotheses. Firstly, if cultural change is achieved by changing employee attitudes in such a way that their commitment to the firm is increased, it can be predicted that changes in employee attitudes, in line with the programme of cultural change, will be associated with increased employee commitment. This can be expressed in the following way:

#### Hypothesis 3(a)

*The Thames Water programme of cultural change will have brought about a change for some employees in their view of the relationship with their employer, and that will in turn have increased the commitment of those employees to the employer.*

Secondly, according to the model being suggested, employee commitment should lead to greater employee motivation. Clearly

this is predicated on the assumption that employees who are more committed to their employer will be more motivated than those who are not so committed. This can be hypothesised as:

Hypothesis 3(b)

*'Employees who are more committed to their employer will be more highly motivated by PRP than employees who are less committed to their employer.'*

Finally, if PRP is used as a mechanism for achieving cultural change, by changing employee attitudes, it would follow that it is more likely to have worked as an agent of cultural change in those cases where it has also been successful in its own terms. In other words, PRP is more likely to be effective in changing corporate culture where it also works to increase employee motivation. Thus it is hypothesised that:

Hypothesis 3(c)

*'PRP will be more effective in changing organisational culture where the PRP scheme is also successful in motivating employees.'*

## **Chapter 6**

### **Thames Water and PRP.**

#### **Introduction**

This thesis has looked at PRP using both qualitative and quantitative research to examine why PRP was introduced in Thames Water, how successful it has been as a motivator for employees, and why Thames Water continues to use PRP. This chapter specifies the research approach adopted, explains why Thames Water was chosen for this research and describes the nature of the Thames Water PRP scheme.

While some of the theories being tested have been developed using both laboratory and field research, there is a clear advantage to be gained from using a field test to see how far those theories go to explain the motivational effectiveness of PRP. Although it might be possible to simulate PRP in a laboratory setting, there is a danger that a laboratory setting would fail to capture all the different aspects of a working environment that influence the effectiveness of PRP. The advantage of a field setting is that it brings into play a number of environmental elements that would be difficult to replicate in a laboratory study. By the same token this means that field studies may be criticised on the basis that they fail to capture or allow for important environmental influences. Kessler (2000) for instance has pointed out that much of the critical evidence about the motivational effectiveness of PRP

comes from the public sector where there are constraints regarding the nature of the workforce and the nature of the organisation, which may undermine the effectiveness of PRP. Consequently it is important to bear in mind the environmental constraints that might impact on PRP in Thames Water when considering the results of the research.

Effectively, by focusing on one firm the individual employee becomes the unit of analysis. Some studies have used the firm as the unit of analysis (Bevan, Thompson & Hirsch 1991, Thompson 1993), and although they have managed to get an overall picture about the motivational effects of PRP within the firms studied, a more detailed quantitative analysis of the individual PRP scheme is needed in order to understand the motivational effectiveness of that scheme. Marsden and Richardson (1994) and then later Marsden and French (1998) conducted quantitative research into the Inland Revenue PRP scheme, which gave a more detailed picture of the effectiveness of a particular PRP scheme. That process has been taken one step further in this thesis by looking at the effects of PRP on individual employee's motivation and correlating the level of motivation with specific facets of the PRP scheme and other aspects of the employee's relationship with the firm and other employees. By using the individual as the unit of analysis in this way it is possible to explore the Thames Water PRP scheme and identify those aspects of the scheme which are most important in motivating employees.

## Quantitative and qualitative research

Both qualitative and quantitative research methods have been used in the thesis (see Appendix A.i). Qualitative research gives a general background to the scheme and specifically helps to explain the reasons why Thames Water introduced PRP. Quantitative research methods are particularly useful for testing the hypotheses about the motivational effects of PRP. By using the individual employee as the unit of analysis it is possible to examine, first of all to what extent PRP is motivating employees, and then to analyse how far particular facets of the PRP scheme can be associated with the motivational effectiveness of the PRP scheme. In so far as those facets of the PRP scheme which are associated with the motivational effect of PRP are consistent with any of the three theories of motivation being examined in this thesis, it will then be argued that theory gives an insight into the mechanisms by which PRP is motivating employees. This analysis is pertinent even if only a minority of the employees surveyed is motivated by the PRP scheme. Indeed, by utilising those facets of the PRP scheme that are germane to the theory or theories that are identified by the analysis, it may be possible to improve the motivational effectiveness of the PRP scheme.

There is now a substantial body of evidence, largely from the public sector (Kessler 2000), to show that PRP is not a particularly strong motivator (Bevan, Thompson & Hirsch 1991, Thompson 1993, Marsden and Richardson

1994, and Marsden and French 1998), yet PRP continues to be a popular payment system, and it is therefore pertinent to ask why a firm chooses to use PRP. Cannell and Wood's (1992) survey suggested that firms use PRP for a number of reasons, and that motivation is only one of those reasons, indeed they found some scepticism amongst personnel managers about PRP's effectiveness as a motivator. It is hypothesised that Thames Water may be more concerned with other benefits of PRP, than they are about its effectiveness as a motivator. Qualitative research has been used in order to contextualise Thames Water's decision to use PRP, and examine the reasons for that decision.

Qualitative research has also been used to look at cultural change within Thames Water, and the extent to which PRP has been used as a tool to achieve cultural change. Although PRP can be an important tool for changing an organisation's culture (Kessler 1994), it is only one of a number of possible levers of cultural change. It is therefore important, if PRP has been used as a lever for cultural change, to understand why PRP is being used and to understand the objectives of the cultural change programme. Qualitative analysis has been used to examine the extent to which Thames Water were pursuing a programme of cultural change and how far PRP was a part of that programme. The effectiveness of Thames Water's programme of cultural change and PRP as a mechanism for achieving cultural change has then been tested using quantitative analysis. It is thus possible to bring together both qualitative and quantitative research in an area of research

where the use of purely qualitative analysis has been criticised for giving too narrow a perspective on the subject (Denison 1990, Milkovich 1991).

### Why Thames Water?

Thames Water presents an interesting opportunity to explore PRP because of its size, history and approach to the future. Taking size first of all, the Thames Water area comprises the Thames basin, stretching from Cirencester in the west to Erith in the east, up as far north as Banbury and down as far south as Godalming. Thames Water supplies clean water to over 7 million people and treats waste water for over 11 million people<sup>1</sup>. In 1995, when the survey of Thames Water employees was conducted, the Thames Water Group employed a total of 10,473 people of whom 6,673 were employed by the utility part of the Group, the bulk of the rest were employed on international work (1,135) and in products and services (2,603), which included subsidiaries, such as the Brophy Group, engaged in non utility work (Annual Report and Accounts 1995). There were therefore sufficient number of people employed in the utility part of the business to make it possible to conduct quantitative analysis, which would provide useful results.

This thesis has focused on the utility part of the Thames Water PLC for four

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<sup>1</sup> The difference is accounted for by the supply of clean water by smaller Water Companies to some households in the Thames Water area – these Water Companies only supply clean water.

reasons. Firstly and decisively, it was only the utility part of the Thames Water PLC group that used a standard PRP scheme, some of the other parts of the Group did not even have PRP. But it is also worth noting that the utility part of the Group represents a reasonably heterogeneous employment environment, with a substantial number of employees being engaged in the continuous processes necessary for water production and waste water disposal, which in turn tends to moderate the environmental differences between subjects within the utility. In addition, the historical development of the utility part of the business from a nationalised industry into the private sector presented a further dimension to the study, which did not apply to other parts of the Group, such as Brophy, which was acquired from the private sector and had always been in the private sector. Finally, while Thames Waters status as a Public Limited Company (PLC) means that its annual reports and accounts are publicly available, those reports also give utility specific information, which makes it possible to focus on the utility business and still get relevant PLC information.

The development of Thames Water as a private company ought to be seen in the context of the water industry in the late 1980s. In England and Wales the water industry prior to privatisation comprised a number of large publicly owned Water Authorities; Thames Water was one of these Authorities. The Water Authorities were responsible for the provision of clean water and disposal of waste water in their areas, although there were also a number of statutory water companies, which provided clean water. The Water

Authorities were bound by government rules on public sector borrowing and, by the end of the 1980s, they were widely perceived to have been under-investing in the water infrastructure. This made them an ideal target for privatisation, especially by a Conservative government ideologically committed to privatisation. However water supply and waste water treatment are natural monopolies, at least in terms of ownership and deployment of the assets.

In 1983 the government appointed Roy Watts as chairman of Thames Water; he had previously worked for the newly privatised British Airways. Roy Watts shared the Thatcherite enthusiasm for privatisation and believed that the Water industry should be privatised. In 1988 Thames Water was the first Water Authority to leave national pay bargaining and put its managers on personal contracts. This was seen as a precursor to a move into the private sector, representing as it did a break with the old nationalised industry commitment to national pay bargaining. It is perhaps interesting to note that Thames used a change in personnel policy to signal its commitment to water privatisation. Then in 1989 Thames Water and the other Water Authorities were privatised. The privatisation followed the same pattern as privatisation of the other utilities had, but in the case of the new water companies the standard pricing formula of  $RPI - X$ , which had been applied to the other privatised utilities, was changed to  $RPI + K^2$ , to provide more money for investment. This pricing formula allowed Thames Water to

increase its capital programme from £247m to £392m in 1990 (Annual Report and Accounts 1990/91) and by 1998 the company's capital investment programme had increased to £485m (Annual Report and Accounts 1998). Utilities other than water on the other hand were faced with a decline in income and the prospect of competition in the future.

While Thames Water was not faced with the same pressure on price as the other utilities, it wanted to increase efficiency for a number of reasons. Firstly, increased efficiency improved shareholder value. Secondly, Thames were keen to become a major international water company with subsidiaries around the world and, in order to win contracts abroad, they needed to be seen as an efficient operator at home. Thirdly, the formula itself was subject to periodic review and the outcome of any review was likely to be more advantageous if the company could show that it had increased efficiency without regulatory pressure. Privatisation was seen as giving Thames Water the managerial freedom to adopt a more efficient and more market-orientated approach to its business. Reporting a 15% increase in earnings per share, Roy Watts said in the 1990/91 Annual Report;

'I question that such results and improvements could have been achieved but for privatisation. Managerial and financial freedom have been a stimulus.'

The impact of the so-called managerial freedom brought about by privatisation was particularly evident in the field of industrial relations. Prior

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2  $K = -X + Q$  where X= efficiency expectations and Q= quality obligations

to privatisation the industry had conducted national pay bargaining in respect of three distinct groups of employees; namely manual, craft and staff. This meant that each group had separate terms and conditions agreed both nationally and locally. Thames Water broke away from national pay bargaining in 1988 a year before privatisation. Then after privatisation, Thames continued reorienting its personnel policies to reflect the new commercial environment. In September 1990 the company announced the Employee Project. This new initiative aimed to:

'Support the modernisation of working practices and continued efficiency improvements by establishing common basic terms and conditions for all employees, greater opportunities for training, and the introduction of a single negotiating forum.'(Annual Report and Accounts 1990/1991)

Essentially, the company was embarking on a programme of change, moving away from job demarcation to a unified and more flexible approach to working practices. Job evaluation and PRP were both introduced as part of the employee project. Overall the aim was to change the culture of the organisation from a public sector organisational culture to a more commercially focused organisational culture. For Thames Water that meant that in the field of industrial relations there needed to be greater flexibility so that managers and employees would feel that they had the freedom to respond to commercial pressures. In particular it meant that employees and managers had to take responsibility for delivering the business aims and to see performance as key to the success of the business. PRP was a central part of this because it allowed Thames Water to cascade down the business

aims through the process of objective setting. At the same time it required managers to address the issue of employee performance.

### The Introduction of PRP.

In 1990, the year after privatisation, Thames Water launched the 'Employee Project' with the aim of revisiting the relationship between the Company and its employees. This project encompassed a range of different policies, including training, employee communication, and payment systems. One of the underlying intentions was to simplify the employment relationship, by for example moving towards single table bargaining. PRP was one of the new policies, which was introduced as part of the Employee Project. One of Thames' Personnel Managers<sup>3</sup> (Appendix A.i) described the aims and objectives of PRP as:

'...a mixture of things. Really a recognition that we needed to be able to reward good performance and, I guess, penalise poor performance, and reflect that in money terms. ...a very broad kind of motivational approach. ... we could use the performance related pay scheme to make clear to employees what we felt were the important issues in the Company, so that for example, the criteria that we ended up with in this scheme, things like team working, things like adaptability, we felt were important values to encourage amongst employees in recognition of the way that the company itself was changing and moving. Certainly since privatisation, the company has gone through so much change, we felt we ought to be actively encouraging that kind of approach amongst our employees, ...a way of getting a message to employees. Trying to use PRP to support cultural change...'

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<sup>3</sup> Extract from an interview with Thames Water Personnel Manager - 9.11.94.

PRP for white-collar staff in Thames Water was agreed in the 1991 pay settlement and implemented with effect from July 1992. The Thames Water PRP Assessor's Training Manual (1995) says that:

'The Company's pay strategy is designed to reward people for their contribution to the business. This means paying a fair rate for the job, recognising and rewarding individual effort and achievement and allowing employees to share in the success of the Company. The three elements of pay which enable the Company to achieve this strategy are described below:-

- Basic Pay - This is based on the appropriate grade for the job as determined through Job Evaluation.
- PRP - Allows an individual's pay increase to be determined by their performance at work.
- Profit Sharing - Enables employees to share in the financial success of the Company providing certain profit targets are achieved.'

A more detailed statement of the objectives of the PRP scheme was given to the Trade Union Side of the Thames Water Company Council when the scheme was revised in 1994. The objectives of PRP were summarised in the presentation given to the Trade Union side of the Council, as being:

'- to recognise differing levels of performance, and by rewarding better performance to encourage and motivate employees to contribute to the best of their ability;

- to ensure a fair salary is paid which takes account of effort and achievement;

- to achieve a fair pay system in which equal pay is given for work of equal value carried out to equal levels of performance.'

Similar objectives are suggested by the introduction to the Thames Water leaflet 'Performance Related Pay - A guide for employees' (circa 1992) which says:

'Thames believes that people should be rewarded for their contribution to the business. This means paying a fair rate for the job, recognising and rewarding individual and/or team achievement and allowing employees to share in the success of the Company.'

The emphasis in these documents is on ensuring the pay system is fair by rewarding performance. The motivation of employees is identified as one of Thames Water's objectives in using PRP only in the company's statement to the Trade Union Side of the Company Council. PRP is not presented in these documents as being a mechanism for achieving changes in the organisational culture. Yet PRP was originally introduced as part of a broader programme of cultural change within Thames Water, the Employee Project. This contrast is perhaps indicative of the difficulty in identifying a single objective as the sole reason why an employer has introduced PRP, and tends to confirm the view that there may be a number of different objectives (Cannell and Wood 1992).

### The Thames Water PRP scheme.

The Thames Water PRP scheme depends upon annual assessments of performance in the year running from the 1st April to the 31st March. These assessments are normally carried out in the following May by supervisors or managers, who are trained Assessors. The assessment is separate from the

Thames' Staff Performance Review (SPR), but the Assessor's PRP Training Manual advises Assessors to look at the SPR, when carrying out the assessment, and says that there should be 'a sensible degree of consistency in the messages given through each scheme'. The SPR scheme is intended to ensure that supervisors and managers communicate and agree clear objectives with their subordinate staff and give feedback on progress towards achieving those objectives. Supervisors and managers should have an SPR interview with those employees they are responsible for at least once a year, sometimes more frequently, although there is no set timetable for SPR interviews. The objectives identified at the SPR should also be used as one of the criteria for judging staff performance for the purposes of PRP. So that while the SPR and PRP schemes are formally separate, the PRP assessment is both, based in part on SPR objectives, and should also reflect the SPR assessment.

There are seven criteria which Assessors use in order to assess employees for PRP in Thames. They are Key Tasks, Targets and Objectives, Motivation and Commitment, Working Relationships, Adaptability, Customer Services, and Managing Others. Key Tasks comprise those tasks in the Job Profile, which need to be done in order to achieve the main purpose of the job. The Job Profile is effectively a job description for each post, which is produced so that the post can be evaluated using the Thames job evaluation Scheme 'JET'. The Job Profiles 'describe jobs in such a way that the different demands of the job can be properly recognised and evaluated but without

including any unnecessary references to specific functional activities' (JET Guidelines for Managers 1994). Assessors first look at the Job Profile, then determine what are the Key Tasks in the profile, and then assess performance of those tasks as either: excellent, very good, good, acceptable, or unacceptable. Each of these categories or Performance Indicators, as they are called, is defined; ranging from excellent, which means 'Far exceeds the requirements and demands of the job', to unacceptable, which means 'Consistently fails to meet the basic requirements of the job in most key tasks'.

Achievement of Objectives and Targets is a criterion, which can be based on an individual assessment or team assessment as appropriate. The objectives and targets are those that are set by management and communicated through local discussions with employees, either individually or collectively. 'The objectives and targets will include such items as SPR objectives, operational performance indicators, quality standards etc.' (Assessors PRP Training Manual 1995) and assessors are required to have regard to documented objectives and targets when assessing employees against this criterion. Essentially this criterion ensures that employees are assessed against the objectives and targets they have been specifically given by their managers. Assessors are told to consider any special circumstances outside the employees' control, which have significantly influenced performance either positively or adversely. The assessment uses the same five Performance Indicators as does the Key Tasks criterion, but the definition of

those Performance Indicators is adapted to the specific criterion; so that for example for this criterion excellent means:

'Targets and standards are frequently exceeded. Exceptionally difficult circumstances overcome without dropping standards or targets. Makes a significant contribution to the achievement of the department beyond established performance standards.'

Four of the five other criteria are concerned with behavioural traits and so can be distinguished from the two already considered, both of which are concerned with performance against specific criteria which have been set and documented in advance. Motivation and Commitment looks at drive and determination that is to say the employee's attitude towards the company and job. Working Relationships relates to the employee's ability to work as part of a team, that is their attitude to other employees that they work with. Adaptability attempts to measure employee ability to initiate change and respond to it positively. And Customer Service looks at the employee's approach to both internal and external customers, to see how far they are focused on identifying customer needs and providing a service. It can be seen that for each of these four criteria, whilst employees will know in broad terms what behaviour is expected of them, they do not normally have any specific targets to work to. Finally, those employees who have responsibility for managing others are also assessed on their ability to achieve the best performance through effective motivation, delegation, and development of employees under their control. All of the criteria are assessed against the same five Performance Indicators, but the definition of each of the

Performance Indicators varies between the different criteria in order to reflect the different attributes that each of the criteria are concerned with.

Once each of the seven criteria has been assessed, an overall assessment is made of the employee's performance based on an overview of performance against the seven criteria. The relative importance of each of the criteria will vary from job to job and 'the balancing of the criteria, and their contribution to the single overall performance assessment is ultimately a matter of management judgement' (Management Presentation to the Company Council 1994). The overall assessment is expressed in the same terms as the Performance Indicators; so that an employee's overall performance may be rated as excellent, very good, good, acceptable, or unacceptable. Potentially one of the problems with the scheme is that employees may be unsure about the relative importance of the seven criteria for their particular job. Indeed it could be argued that seven criteria against which to assess performance are too many. From the employer's point of view, it may look as if they have captured all the different aspects of performance that they might want to reward. From the employees' point of view having a plethora of targets may make it more difficult to understand what is expected of them and how they can achieve a performance payment.

The overall assessment made by the Assessor is countersigned by the Assessor's manager and that assessment is recorded centrally, so that Personnel can monitor the assessments. Personnel monitor managers'

assessments first of all to see if there is a normal distribution of ratings, that is to say whether they correspond to the normal bell curve distribution, in practice the distribution is skewed to the right with a tendency for assessments to peak at very good. The assessments are then broken down according to gender and ethnic origin and then analysed to see whether the figures suggest that there is any bias in the assessments. If the monitoring process highlights any anomalies, these are discussed with the manager concerned. Some PRP schemes apply a forced profile or quota to the managers' assessments either before or after they are made, so that the number of employees who are rated in each category is limited. This helps ensure there is a distribution of the various category ratings and consequently helps to control salary costs, by ensuring that not everyone is in the highest category. Thames Water do not use a quota system or apply a forced profile, although presumably managers are aware that their assessments will be looked at by Personnel to see how far the distribution of assessments differs from others. Only the overall performance rating is used to determine the individual employee's entitlement under the PRP scheme.

The performance assessment is translated into a pay increase by applying the overall performance rating or assessment category to the relevant salary matrix. Each grade has a salary matrix which contains a scale salary range going from a scale minimum of 85% of the mid point of the salary scale to a scale maximum of 115% of the mid point of the salary scale, so that if the mid point of the salary range was for example £20,000, the range would go

from a minimum of £17,000 to a maximum of £23,000. Each performance assessment category has what is termed a Natural Level within the salary matrix. The Natural Level for excellent is 115%, for very good it is 107.5%, for good it is the scale mid point, for acceptable it is 92.5% and for unacceptable it is 85%. Where an employee's salary is above or below the Natural Level for their performance, when their performance is assessed, the level of their performance payment should progress their salary towards their so called 'Natural Level', which is the level of salary that reflects their level of performance. So, for instance if employees are paid more than their natural level then their salary should increase by less than the movement in the salary band, so that as the salary band moves up their position moves closer to their Natural Level. Alternatively, if an employee is paid less than their Natural Level then they can expect an increase higher than the overall movement in salary bands. The further the employee is away from their Natural Level on the salary matrix the larger the movement in their salary relative to the general movement in the salary band.

Each employee's assessment is known before the annual pay negotiations. The annual pay increase is agreed between the Company and trade unions. Historically the trade unions have sought to protect the earnings of employees who are earning in excess of the salary paid for that employee's natural level on the salary matrix. An employee can be above their Natural Level on the salary matrix for a variety of reasons. For instance when PRP was introduced the salary scales were changed and employees were job

evaluated onto the new scales, in some instances new grades attracted a lower salary than the employee's current grade, but the employee's salary was protected.

The speed with which an employee progresses towards their Natural Level depends upon how far they are away from that Natural Level on the salary matrix, so that the largest increase achievable would be paid to an employee, who was on 85% of scale and who was rated excellent. Equally, someone who was paid 115% of scale, but rated as unacceptable would move down through the matrix, because although they will not have their pay cut, their pay will not increase at the same rate as the matrix so that they will still effectively be moving down through the matrix. Anyone whose assessment category matched their current position on the salary matrix would already be at their Natural Level and so would not move on the salary matrix, although they would still benefit from any annual pay increase. One effect of this is that, in any one year, an employee whose previous performance has been poor might get a bigger salary increase, than an employee who has consistently performed very well, even though the difference in absolute salary levels would reflect the consistent performance.

Progress through the matrix has also been affected by the low level of inflation since PRP was introduced, which in turn has meant that the level of pay increases has been relatively modest. As the Personnel Manager<sup>4</sup> said:

'the first year we settled at something like 4.5%, the second year 2%, and this year just under 3%, so given we are talking about 30% wide scale, it is really very difficult to make a lot of progress, so I think inflation is a problem.'

Another personnel manager commented that the problem with the scheme is that salary increases were driven by the employee's position on the salary matrix rather than the employee's performance. In 1994, International Survey Research Limited conducted an employee opinion survey for Thames Water. Thames published a summary report of the results of the survey for employees in 'Viewfinder 94', an internal employee communication publication. The survey showed that 54% of Thames' employees were satisfied with their pay and benefits, according to the report this contrasts with only 40% in Companies generally, although this may reflect comparatively high levels of pay in Thames Water. Surprisingly, perhaps given the complexity of the Thames Water PRP scheme, some 51% of those surveyed claimed to understand how their performance was judged for the PRP scheme. However the scheme was not thought by respondents to be rewarding good performance, only 15% thought PRP penalises poor performance and only 13% thought PRP rewards superior performance. The report comments:

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<sup>4</sup> Interview with Personnel Manager - 9.11.96

'Performance -related pay is one particular cause for concern. Although people appreciated the scheme has some useful points - for example it helps prompt discussions on performance with managers - many question whether its usefulness is reflected in pay. Few of you feel it sufficiently rewards good performance, or that it penalises poor performance. Perhaps for these reasons PRP isn't motivating you as much as you'd like it to.'

Clearly on Thames Water's own evidence the PRP scheme was not achieving their published objective of rewarding individual achievement. Commenting on this a Personnel Manager<sup>5</sup> observed:

'I think there has been a recognition that it doesn't achieve a great deal in terms of motivation in its current form, that's for sure. I think the results of our internal review has demonstrated that people don't feel turned on by PRP and so from that point of view,...I guess we maybe parked that objective a bit. I certainly recognise that it is not one that's operating or has been achieved particularly well, but I think that the one about the cultural message is important to us.'

Notwithstanding these concerns about the motivational effectiveness of PRP, Thames Water continued to use a PRP scheme to pay the bulk of their staff, although they discontinued use of the salary matrix to determine the level of increase in salary for a given level of performance in 1998. Instead the employee receives an increase in pay determined by their performance assessment and expressed as a percentage increase in pay. So that all employees who receive the same performance assessment will receive the same percentage level increase in their pay. At the same time Thames Water reduced the number of assessment levels from five to four. The number of levels of assessment was reduced partly because managers were perceived to be over using the middle assessment too much and it was felt

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<sup>5</sup> Extract from interview with Personnel Manager - 9.11.94 -

that four levels of assessment would force a more honest assessment of performance to be made. One manager explained the continued use of a PRP scheme on the grounds that it focuses managers attention on the performance of the employees they are responsible for managing. Managers have to discuss targets with their staff and then assess how far those employees have progressed towards achieving those targets and the other criteria specified by the Company. That assessment is then translated into a payment. Consequently managers have to talk to their staff about performance and make a meaningful judgement on that performance. In other words PRP forces managers to manage. Thames Water see PRP as a fundamental part of the Performance Management because it forces managers to manage performance and by focusing managers on performance the company believes that PRP will help to bring about a change in culture within the company to a more commercially driven performance orientated culture.

## Chapter 7

### **Why Thames Water introduced PRP?**

In order to get a deeper understanding of the reasons why Thames Water introduced PRP, key managers who were involved in its introduction were interviewed (see Appendix A.i for description \of the key players interviewed and the structured interview approach adopted). This, together with the documentary record (Thames Water documents referred to are listed in Appendix A.i), provides a qualitative insight into Thames Water's objectives in introducing PRP. The interviews were primarily intended to give an understanding of why Thames Water introduced PRP. It soon became clear that the introduction of PRP in Thames was tied up with the whole process of water privatisation. Kessler and Purcell (1992) have argued that one of the reasons for the spread of PRP has been the privatisation of the nationalised industries, as these industries have used PRP to try to create a more commercially focused culture. Consequently the approach adopted in this chapter has been to look at the privatisation process in Thames Water and then to examine the specific reasons for the introduction of PRP in Thames Water.

### Thames Water in the run up to privatisation

In order to find out what Thames Water hoped to achieve by introducing PRP it is first of all useful to look at the history of the company. As a Water Authority, Thames had a strong public sector ethos. Derek McManus described the change from the public to the private sector as having started before privatisation.

'We were very much a local authority based organisation as Thames Water Authority. When the changes came about in the Water Act 1983, I think there was a view that that was a precursor to privatisation, although I don't think the word was actually mentioned at the time... Chairman and Personnel Director made the decision to position the Company or Authority in such a way as to take advantage of privatisation as soon as it came round.'

The Chairman of Thames Water, Roy Watts, drove the whole process from the top. Roy Watts had previously been Deputy Chairman of British Airways, where he had been involved in pushing through a major programme of change. Roy Watts was seen as a leading advocate of water privatisation.

In 1988 Thames Water was the first water authority to pull out of national pay bargaining. This was partly the result of frustration with a national system that meant that pay and conditions for the 9,000 to 10,000 Thames' employees were dictated by a body that Thames Water could not control. But it also reflected the drive to position the company for privatisation. It is worth noting that one of the first steps taken publicly to get Thames Water ready for privatisation involved a change to employees' terms and

conditions. According to Steve Jay, the company saw the move as 'a matter of principle', a move to bring decision making closer to home.

Steve Jay had joined Thames Water three years before privatisation, 'not quite knowing if they were to be privatised, but being quite interested in the whole privatisation process'. His feeling was that there was not a specific strategy for privatisation, but that the prospect of privatisation informed the company's agenda for change.

'My recollection of those early years in the run up to privatisation was that the agenda was more about cultural change and it was less about being specific as to what the strategy was.... It was about changing the way the organisation thought about itself, so one of the things that was critical was to start getting people in what was the Thames Water Authority to think of themselves as being in a commercial entity.'

In addition to the move away from national bargaining, some 60 or 70 of the top management team were taken off collectively agreed terms and conditions and given personal contracts. Once again the company chose to use an alteration of employee terms and conditions to communicate a broader cultural change message about a transformation in the nature of the company. This top management team was taken off to Templeton College, Oxford for a week-long course, not on any particular management theory or strategy, but to listen to people from outside the company talk about privatisation. Steve Jay described the course:

'It was quite transformational exercise because most of the people there, apart from two or three of us from the private sector had grown up within the water industry. They were confident in their own areas of expertise but had never really considered themselves as part

of a commercial entity and so didn't have a clear picture of a broad managerial agenda.'

The company then cascaded some of these changes down to the next level of management, a group of about 200 to 300 people. New managers were brought in from the private sector, but long serving water industry managers were also retained to give the company what Roy Watts referred to as 'the strength of the mongrel'.

At the same time that Thames Water was trying to introduce changes in management attitudes in the run up to privatisation, the opportunity to introduce technological changes in the way that the industry operated was opening up. Although the fundamental operation of water supply and waste water treatment had not changed very much, it was felt that after many years of under investment there was a need to invest in some quite major projects such as the London Ringway and in new technology like remote control systems.

'so that instead of having people pushing levers and pressing buttons, it was all done in a central location. That had been tried in the water industry before, but was not reliable for whatever reason. Coincidentally, I think about the time of the managerial type changes the technology began to become more reliable and accessible.'<sup>1</sup>

In the run up to privatisation, Thames Water was being led by a Chairman, Roy Watts, who not only believed in privatisation, but wanted to position the company so that it was ready for privatisation. Fundamental to this move to position the company for privatisation was a drive to change attitudes.

Firstly, by taking Thames Water out of national pay bargaining and so getting control of employee pay and conditions. Then by giving top managers individual contracts, and then training them in operating the company as a commercial organisation. The drive to change employee attitudes did not stop with privatisation, nor did privatisation diminish the role played by changes in pay and conditions as a mechanism for achieving changes in attitudes.

### Post privatisation

Thames Water introduced the Employee Project in 1990, the year following privatisation, to bring about a fundamental change in the way in which employees' terms and conditions were discussed and the way in which employees were paid. Steve Jay described the origins of the employee project.

'There was a small group... this agenda wasn't handed down to us by Mike Hoffman (Chief Executive) or Roy Watts...it really came from that group. We had a brainstorming session...we had a whole cross section of managers in the operational area... and we asked two questions. One was if you had a blank sheet of paper as far as people are concerned, terms and conditions, the whole agenda, what would you do? The other question, which was the other side of it, was, if you look at what we now have, what's stopping you from managing the business what are the obstacles, the things that are getting in the way? And there were five or six things that just emerged. ... We summarised the five or six things and got some personnel people and some line managers in teams to work in those five or six areas for several months and then we pulled it all together and we presented that agenda to Mike Hoffman who was the Chief Executive...'

Mike Hoffman then outlined the objectives that had been agreed to the whole of the top management. A small project management group was established to deliver the objectives. The group did not know how they were going to deliver these objectives and they spent some time working out what the practicalities were with line managers.

The project group then talked to the trade unions. One of the principal objectives of the project group was to create a single table for bargaining, as that was seen as a pre-condition for progress in other areas. Previously, employee terms and conditions had been discussed in one of three negotiating machines, depending on whether the employees were white collar staff, manual workers, or craftsmen. Thames Water wanted a simpler more straightforward system for determining pay and conditions. A feature of the discussions with the trade unions was that the project group did not have a definitive view of how the objectives that they wanted to achieve should be delivered. So for instance, when the project group suggested reducing the number of trade unions who were recognised by Thames Water, and the Thames Water trade unions said that they could work together through single table bargaining, the project group believed that delivered the key objective of single table bargaining.

Single table bargaining was introduced in Thames Water in 1992. Single table bargaining was just one of a range of changes which was introduced as part of the Employee Project. PRP was another aspect of the Employee

Project. The introduction of PRP for white collar Thames Water staff was agreed in principle in the 1991/1992 Staff Pay and Conditions Settlement which states: 'Joint Discussions to be held on criteria for the introduction of performance related pay from the 1<sup>st</sup> July 1992.' Following more detailed discussions during the PRP 1992/1993 pay negotiations PRP was introduced for Thames Water white-collar staff with effect from the 1<sup>st</sup> July 1992.

There was no formal statement of the objectives that Thames Water had in introducing PRP. As the Personnel Manager put it when she was interviewed:

'I am not sure that there were any aims and objectives formally written down at the beginning of the scheme, which is quite interesting for itself, but in reality I suppose it is a mixture of things.'

PRP did not appear in Thames Water as part of a well-defined written strategy nor as part of an overall reward strategy for the company. If it had done, that might have led to a different PRP scheme being introduced, perhaps one that would have been more effectively focused on achieving the company's objectives.

Nevertheless it is possible to identify Thames Water's objectives from the company's overall objectives, the documentation, and the evidence of those who were involved at the time. Clearly PRP was part of the broader agenda, described by Steve Jay, which aimed to change peoples attitudes, in other words it was part of a programme of cultural change. But before looking at PRP in more detail as an agent of cultural change within Thames Water, it is

worth considering some of the other objectives Thames Water intended PRP to achieve.

### Wage reduction.

The Thames Water Company Proposals issued in response to the 1992/1993 Trade Union Side Pay and Conditions Claim made it clear that Thames Water believed that they were more than competitive in the pay market. Indeed the minutes for the Thames Water Company Council Pay Negotiating Meeting held on 29<sup>th</sup> May 1992 record the Company's position as follows.

'Salaries and wages are the largest single item of cost. For 1990/91 we had the highest pay per employee in the industry. Our average pay totalled £22,000 - £4,000 or 24 % more than the industry average. Our profit per employee stood at £26,800 and is nearly the lowest (8 out of 10) in the industry.'

Managers were naturally concerned about this situation.

'considerable management discussions about the rates of pay that we had inherited from various local authorities and indeed the increase because of normal pay rises, and there was a statistically demonstrated view that we paid 20% more than other water companies. I think there was an understanding that some 10% to 12% of that was due to London Weighting and other geographical factors, but the remaining 10% to 8%, depending on how you like to describe it, was felt to be payment which was in excess of the going rate that other water companies were paying for any particular job. And I think there was a decision taken, partly due to outside pressure, that we would need to reduce the gap to get our general level of earnings, salary back by about 10% overall.'<sup>2</sup>

PRP was seen by Thames Water as a mechanism by which they could control excessive wage costs. The expectation was that the differential movement of individual employees pay would allow those employees who were

overpaid to be held in check, while others progressed through the salary bands. Derek McManus estimates that about 40% of employees were paid in excess of what was described as their natural scale position, that is to say what the company thought was the rate for their job. Realistically, PRP only offered an opportunity to manage down these excessive wage costs if the level of pay increase in the years following its introduction gave enough headroom to allow for that to happen. As Derek McManus explained:

'we introduced a new seven grade structure to replace what was a thirteen grade structure...It had the effect of squeezing a number of jobs into grade bands with a lower maximum. Since many, if not most, of our employees were at the maximum of the old scale, we had a large number of people who were overpaid in terms of the new scales. We thought we could control that through the application of performance related pay and it was not an unreasonable expectation because inflation rates were running at about 12% or 10%, which gave sufficient head room in the make up of the successive pay awards, annual pay settlements, to make some inroads into the so called overpayments. Almost immediately we introduced that system of performance related pay, inflation crashed, and we found ourselves on 3%, 4%, and 5% pay awards and even less in some areas, which meant there was no effective way to control the overpayments.'

PRP has not proved to be particularly successful as a mechanism for reducing excessive wages, largely because wage increases generally followed inflation downwards in the period following the introduction of PRP. Equally by using PRP to manage wages downwards Thames Water have tended to undermine the effectiveness of PRP as a motivator. Firstly because employees may have perceived PRP to be a mechanism for reducing wages, as one respondent said in response to the open question in the survey of Thames Water employees conducted for this thesis:

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<sup>2</sup> Derek McManus

'PRP was not introduced for the benefit of employees, but with the intention of reducing the pay bill for Thames Water.'

Such perceptions are likely to undermine any feelings of procedural equity, and as has been argued above that would in turn detract from the effects of any performance payment as a motivator. In addition, there was by definition a substantial body of employees (Derek McManus put the figure at 40%), who because in the company's view they were overpaid, would not receive any real benefit from PRP. For these employees PRP had a negative effect. The way in which this works was explained in one of the answers to the open question in the survey.

'If a person was over salary scale when PRP commenced there is no way, no matter how hard you work or how dedicated your performance is, that you will get anything other than the PRP%. This is soul destroying when you find that another person, perhaps only N/A (not acceptable), because they are lower down on the scale, in fact receives a higher percentage overall. Surely there is something wrong with such a system?'

Nevertheless wage control was clearly an important issue for Thames Water and it was always going to be difficult to manage wages downwards. While PRP may not have delivered a solution as quickly as Thames Water had hoped, it did give the company a mechanism for moving wages towards the 'natural salary scale point'. It is not clear whether the advantages of wage control outweighed the potential damage to the motivational effectiveness of the PRP scheme. Nor is there any evidence that Thames Water considered these competing concerns when they introduced PRP.

## Fairness.

The published justification for introducing PRP was set out in a leaflet Thames Water issued to employees entitled 'Thames Water Utilities - Performance Related Pay - a guide for employees'. The first paragraph of the leaflet states:

'Thames believes that people should be rewarded for their contribution to the business. This means paying a fair rate for the job, recognising and rewarding individual and/or team achievement and allowing employees to share in the success of the company.'

The central message to employees is that reward should be linked to their contribution to the business, and that this link between reward and achievement is a fair mechanism for paying employees, which enables them to share in the success of the company. Clearly the link between pay and performance was fundamental to Thames Water's thinking about PRP on a number of different levels, some of which might be viewed by at least some employees as contradictory. For example, an employee whose wages are being managed down is unlikely to feel that they were having their achievements recognised or being allowed to share in the success of the company, indeed there is a danger that they might view the system as being somewhat less than fair. Equally it could be argued that they might be less susceptible to some of the other objectives the company had in introducing PRP. Nevertheless PRP was a powerful tool for communicating with employees.

## Cultural change.

First and foremost linking pay to performance sent a clear message about the company's priorities. In other words it was part of the cultural change process aimed at changing Thames Water from a nationalised industry into a commercial organisation. It was about focusing employees and managers on performance. All four of the managers interviewed in the research for this thesis believed that PRP had an important role to play in bringing about cultural change.

'we were very keen to make a differentiation between the company that we had been, as a nationalised industry, to the company that we wanted to become, and we saw pay as a very significant factor in how we could achieve that. By putting in new systems, new organisation, new management structures and by adjusting pay, we thought we had a real lever on changing the culture of the organisation.'<sup>3</sup>

'There was a view that the new pay system which included performance related pay was necessary to change the culture of the company. I don't think it was particularly published at the time.'<sup>4</sup>

It is difficult to know how far companies can engineer cultural change, because of the problems over measurement and causality, particularly where, as in this case, the employer uses a number of different mechanisms to achieve cultural change. Most of the work that has been done on cultural change has relied on qualitative research rather than quantitative research (Dennison 1990). Some of the items in the survey questionnaire have been designed to measure cultural change and the results are dealt with in

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<sup>3</sup> Malcolm Carr

<sup>4</sup> Derek McManus

subsequent chapters of this thesis. Certainly Steve Jay thought that PRP had played a part in changing the corporate culture in Thames Water:

'Trying to describe exactly the part it (PRP) played in any change of culture and attitude was just about impossible, but I think it's got the issue, even if it's in a fairly contentious sort of way in some places, of performance into the language... the bloodstream'

Derek McManus thought that PRP had probably contributed to about 10% of the cultural change in Thames Water.

### Performance Management.

However, PRP was not just about changing individual employee attitudes to performance, it was also about getting managers to talk to their staff about performance. There was a very real concern about the ability of managers to manage. Steve Jay put it this way:

'We felt we had management and supervision generally who didn't manage people and were generally poor man managers and indeed hadn't been expected to manage people. It was quite common for managers to talk about... the authority doing this or the Authority doing that and abdicating responsibility for managing people, so we thought it would bring the linkage with employees and their performance right into the centre of the stage.'

For Thames Water PRP was both about changing employee and management attitudes, and also bringing about structural changes in the relationship between managers and employees that would encourage good management. This was a major departure from what had happened in the past. Derek McManus contrasted it with the previous incremental system.

'the concept of personal performance was something that was quite new to Thames. The concept of a manager actually assessing and

marking an individual's personal performance was unique as far as Thames Water was concerned. Previously increments had been paid on a regular basis and to have an increment stopped, it was necessary for the employee to be quite hopeless at the job he or she was doing, and even then the stoppage could only be for a limited period and after about 3 or 6 months the increment would automatically be paid. So performance pay is thus seen as a method of involving management in the assessment of employees and in determining the level of pay that a particular employee should have and I think this was a major departure from what had gone before.'

Thames Water clearly hoped that by embedding performance in the relationship between the manager and managed, both would focus on performance. Steve Jay was sceptical about how far PRP had affected the performance of very good or bad managers, but he believed it had helped to underpin the relationship the majority of managers had with their employees by making discussion about performance a legitimate and key part of that relationship. Two comments from the replies to the open question on the questionnaire illustrate the different experience different managers and employees have of the PRP process, as a mechanism for communication between management and employees. In one case the respondent thought that PRP was used by managers as a 'substitute' for feedback; while in the other the respondent commented that 'the words and feedback given are nearly as important as the pay'.

### Motivation.

Linking pay to performance allowed Thames Water to reward good performers and penalise poor performers. This is as the Personnel Manager

put it 'a very broad kind of motivational approach'. Thames Water did not have a particular motivational model in mind, but there was a belief that linking money to performance would stress the importance attached to performance and that employees would work harder to achieve a better performance payment. However the difficulty for Thames Water was that PRP was only ever intended to be a small part of pay. As Steve Jay explained:

'we never thought it (PRP) ought to be a large chunk of pay, not in this kind of cultural setting and also we were dealing with an industry which was the opposite of volatile, a long term industry where we didn't want a kind of lottery mentality developing amongst our workforce. We were more about making a point and so we never, ever thought that performance related pay would contribute a great slice of pay.'

PRP was kept as a relatively small element of pay in Thames Water by virtue of the fact that PRP was part of the consolidated annual pay increase. Even though the salary range in the Thames PRP scheme goes from 85% to 115%, so that potentially the difference in pay between a poor performer and an excellent performer could be 30%, the actual difference in any one year was determined by the level of pay increase. As has already been noted, the level of pay increase in the years after the introduction of PRP was relatively low, largely because inflation was relatively low.

'the pay increases that we could afford to pay even to the excellent performers was quite limited and was not motivating and indeed was almost de-motivating, because it was not very helpful to describe somebody as an excellent performer and only be able to pay 3% for that privilege, so it was a a sort of reverse motivation. But certainly motivation was one of the things that was claimed at

the time. I think part of it was jargon at the time. I think that's the claim for all PRP, but we did actually believe we could deliver against that criteria.<sup>5</sup>

In hindsight motivation has not been viewed as one of the benefits of PRP for Thames Water.

'It is noticeable that the issue about reward motivation, those sort of comments were dropped quite early on from our justification for it and we concentrated and still do concentrate on the management employee relationship, as being the thing that has improved during the currency of this scheme.'<sup>6</sup>

Nevertheless motivation and indeed de-motivation are important issues for any pay system. There is a very real paradox in Thames Water using a payment system because it focuses employees and managers on performance, while at the same time the company does not know whether the payment system is motivating employees to improve their performance.

### Hypothesis 1.

The first hypothesis that this research was intended to test is that:

### Hypothesis 1.

*'Thames Water will have introduced PRP in order to achieve a number of objectives, but principally in order to achieve a change in corporate culture following on from privatisation. Increased employee motivation will have been only a subsidiary consideration in the decision by Thames Water to introduce PRP.'*

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<sup>5</sup> Derek McManus

<sup>6</sup> Derek McManus

Both the documentary evidence and the interviews with those involved show that there were indeed a number of objectives that the Company was seeking to achieve through the introduction of PRP. There is however a difference between the documented reasons for the introduction of PRP and the principal reasons for the introduction of PRP that emerge from the interviews. 'Performance Related Pay – a guide for Employees' and the Performance Related Pay Assessors Training Manual (1995) both give the following rationale for PRP:

'Thames believes that people should be rewarded for their contribution to the business. This means paying a fair rate for the job, recognising and rewarding individual and/or team achievement and allowing employees to share in the success of the Company.'

The emphasis here is on fairness. This explanation seems to be distilled from the presentation given to the trade union side in 1994 pay negotiations where the company said that PRP was intended:

- '- to recognise differing levels of performance, and by rewarding better performance to encourage and motivate employees to contribute to the best of their ability;
- to ensure a fair salary is paid which takes account of effort and achievement;
- to achieve a fair pay system in which equal pay is given for work of equal value carried out to equal levels of performance.'

While the emphasis is again on fairness it can be seen that PRP is also seen to be a tool for increasing employee motivation.

This can be contrasted with the views expressed by Steve Jay and Derek McManus, both important players at the time that PRP was introduced. It is

clear from what they say that the principal driver for the introduction of PRP was the Employee Project, which was a programme of corporate cultural change aimed at giving Thames a greater commercial focus following privatisation. Indeed all the managers interviewed for this thesis expressed some scepticism about the usefulness of PRP as a mechanism for increasing employee motivation. And while greater fairness was clearly one of the objectives the company had in introducing PRP, it has to be said it was fairness from the Company's perspective. Thames Water was equally happy to use PRP as a mechanism for reducing wages.

Thames Water also used PRP to ensure that managers, and the employees they were responsible for, entered into a dialogue about performance. It was about getting managers to manage. As Steve Jay put it:

'We felt we had management and supervision generally who didn't manage people and were generally poor man managers and indeed hadn't been expected to manage people. ...so we thought it would bring the linkage with employees and their performance right into the centre of the stage.'

Cannell and Wood ( 1992) found an element of this when they surveyed employers to find out why they had introduced PRP, a number of their respondents referred to PRP as a mechanism for improving communication between managers and employees. Essentially the evidence from Thames takes that one step further and shows PRP being used to improve managerial skills.

The evidence supports the first hypothesis. Thames Water did have a range of objectives that went beyond improving motivation, which led them to introduce PRP. It would appear that the principal reason for introducing PRP was to bring about cultural change. This supports the arguments put forward by Kessler and others (Kessler & Purcell 1992, Kessler 1994, and Kessler 2000) about the importance of cultural change in certain contexts as a reason for the introduction of PRP. The programme of cultural change was in turn driven by the perceived need to make the company more commercially focused following privatisation. Thames Water also saw PRP as a way of focusing managers on performance in their dealings with the employees that they managed. Employees were told that PRP was a fairer pay system, at the same time it was clearly being used to manage down wages, which for some employees made it a less than fair pay system. Perhaps the least important objective appears to have been to increase employee motivation. Certainly there is some evidence that this was one of the objectives at the time PRP was introduced, but subsequently there has been some scepticism about the effectiveness of PRP as a motivational technique.

Nevertheless the important question remains does PRP increase employee motivation and if so how? And can the motivational effectiveness of PRP be improved? After all if employee motivation can be increased then the company's overall performance should improve. Equally it is important to

understand whether or not the PRP scheme is demotivating employees and, if so, whether that outweighs the benefits of the scheme.

## **Chapter 8**

### **The effectiveness of PRP in Thames Water.**

#### Introduction

This chapter examines the results from the survey of Thames Water employees (see Appendices A.i & A.ii for details) conducted as part of this thesis to see how far the Thames Water PRP scheme can be said to have been a success from the employer's perspective. It is the success or failure of the Thames Water PRP scheme which contextualises the results of each of the hypotheses being tested in this thesis. It does this, firstly, because the effectiveness of any one motivational theory needs to be judged against the overall motivational effect of the PRP scheme. Secondly, by looking at success criteria other than the motivational effectiveness of PRP, it is possible to make an assessment of whether the PRP scheme can be judged to be successful by Thames Water against criteria other than simply whether or not it motivates employees. After all, from the employer's point of view success can be judged against a number of different criteria (Cannell & Wood 1992) and motivation of the workforce is only one of those criteria. It is important to note, however, that not all of the possible success criteria are susceptible to measurement from the results of an employee attitude survey. Where the survey results shed light on the success or otherwise of the Thames Water PRP scheme, those results are reported. Equally, it is

important to examine the potentially negative effects of PRP, which might on balance outweigh its positive effects. And where the survey results shed light on the negative effects of PRP, those results are reported.

Thames Water commissioned International Survey Research Limited to conduct a survey of the opinions of employees in Thames Water Utilities in 1994. The survey was conducted on a confidential basis, with the overall results being communicated to employees in a report entitled 'Viewfinder 94'. The 1994 survey is interesting, firstly, because it is unusual for employers to evaluate the effects of PRP schemes (Cannell & Wood 1992) and the 1994 survey does this, if only to a very limited extent. The fact that the survey was conducted and its results reported to employees suggests that Thames Water were perhaps more open and rigorous in their approach to PRP than the majority of employers (Cannell & Wood 1992). Paradoxically, it also shows that even though Thames Water were aware of some of the deficiencies of their PRP scheme, they chose to continue to use PRP to pay employees. In addition, the results of the Thames Water survey provides a point of comparison for some of the results obtained from the survey conducted for this thesis. The results of the Thames survey in Viewfinder 94 are reported where relevant.

Results from other surveys of employees in receipt of PRP are also reported in this chapter for comparison. The results from the survey of Thames Water white collar employees are broadly consistent with the results of

similar surveys of employees in receipt of PRP, both in terms of the opinions expressed about the PRP in principle and the motivational effects of the individual's own PRP scheme. Respondents were generally favourably disposed towards the principle of PRP, but felt less positive about their employer's PRP scheme.

Finally, the data has also been analysed to see how far the gender of the survey population has influenced the results. Any difference in the way in which PRP is applied to men and women may be discriminatory and therefore unlawful. The European Court of Justice decided in the *Danfoss* (1989) case that:

"the quality of work carried out by a worker may not be used as a criterion for pay increments where its application shows itself to be systematically unfavourable to women."

Consequently, it is important that any PRP scheme should not be systematically unfavourable to women. In this chapter the results of the survey are examined to see whether there is any significant difference between the way in which the performance of men and women are assessed in Thames, whether there is any evidence that they are performing differentially, and whether the results of the performance assessment are reflected in the position of men and women on the salary matrix.

## Attitude to PRP

The majority of respondents thought that PRP was a fair way of paying staff, 66%, thought that performance related pay was a fair way of paying staff, while only 18% said that they did not believe that it was a fair way of paying staff (Appendix B.1). This opinion was also reflected in some of the comments made in reply to the open question:

"There are a lot of different claims made for performance related pay, for instance it is sometimes claimed that performance related pay motivates employees to work harder, but on the other hand it is also said that performance related pay may cause jealousies between staff and damages teamwork, could you summarise your own experience of performance related pay in Thames Water in your own words?"

Even when respondents were critical of PRP in their response to the open question, many prefixed their comments with statements such as 'PRP is good in theory...' or 'PRP is a good idea in principle...' or 'PRP sounds fine'.

The level of support for the principle of PRP amongst Thames Water employees can be compared with that found by Marsden and Richardson (1994) and Marsden and French (1998), when they surveyed of Inland Revenue staff in receipt of PRP. Inland Revenue staff were asked whether 'The principle of relating pay to performance is a good one.', the results in each year were similar:

Table 8 i – IRS PRP fair payment system

	<b>1991</b>	<b>1996</b>
<b>Agreed</b>	57%	58%
<b>Disagreed</b>	40%	37%

At 66%, the level of support for the principle of PRP, among Thames Water employees, is closer to the 70% support reported for the civil service as a whole (Marsden and Richardson 1994), so it would appear that Thames Water employees were more favourably inclined towards PRP than Inland Revenue staff.

#### Union membership and PRP

Intuitively, it might be thought that the trade union members surveyed would be more strongly associated with opposition to PRP than the population in general, either because trade unionists could see PRP as antipathetic to long cherished trade union principles, such as 'the rate for the job', or because the focus on the individual in PRP would run counter to the collectivist values of trade unions. Comparison with the Inland Revenue results suggests that this is not the case. The 1991 survey of Inland Revenue staff (Marsden & Richardson 1992) was conducted with the assistance of the Revenue and included both union and non-union employees. The 1996 survey of Inland Revenue staff (Marsden & French

1998) was conducted without the assistance of the Revenue and encompassed only union members. The two survey results for Inland Revenue staff in 1991 and 1996 are similar, which suggests that there is little difference in attitude between union and non-union members towards PRP in the Inland Revenue. Likewise the comparatively strong support for PRP amongst Thames Water employees responding to the survey, suggests that there is little innate hostility amongst the trade union members surveyed towards PRP.

#### PRP and fairness

On the face of it, support for PRP as "a fair way of paying staff" amongst the majority of respondents gives credence to the argument advanced by some employers, including Thames Water, that PRP is a fairer way of rewarding employees, reflecting new perceptions of equity (Armstrong & Murlis 1994). However, respondents' support for PRP in principle contrasts with what respondents felt about the Thames Water PRP scheme in practice, a clear majority (72%), did not believe that they had been paid more fairly as a result of the introduction of PRP; while only a minority (11%), thought that they had been paid more fairly (Appendix B.fii). An even higher proportion of respondents (82%) felt that their employer failed to adequately reward hard work (Appendix B.fiii). So, while a majority of respondents thought that PRP was a fair way of paying staff in theory, in practice, an even larger number of respondents thought that it not increased the fairness of their

pay. On this evidence, even if Thames Water felt that they had introduced a fairer payment system when they brought in PRP, this was not a view shared by the majority of their white-collar employees.

Thame's own survey in 1994 found that only 15% of employees thought that PRP penalised poor performance and only 13% of employees thought that PRP rewarded superior performance. These results support the survey finding that employees did not believe that the PRP was fair in practice. They also show that Thames were aware of employee perceptions about the fairness of the PRP scheme.

Looking at other surveys, Mark Thompson (1993) found in a study across three organisations in food retailing, finance, and local government, that employees were uncertain as to whether PRP rewarded them fairly or not. However, on further analysis Thompson found that high performers tended to see PRP as being a fairer way of recognising individual contribution than low performers did. One explanation for the different perspectives of high and low performers is that the level of performance was defined by the performance rating for PRP purposes, which in turn determined how much performance payment individuals received. An employee who received a larger performance payment might, after all, view the PRP system as being fairer than an employee who received a lower performance payment. From the employer's point of view, this raises the question of whether it is the absolute salary level compared to other employees or the increase on

previous salary which influences respondents' perceptions of fairness. If it is the former, then high performers who have reached the top of the salary scale may feel they are being treated fairly even if they do not receive a large year on year increase. If it is the latter, then high performers will be looking for a large increase in salary, year on year, even when they are at the top of the scale.

The thesis survey results for fairness reported in Appendix B.fii have been crosstabulated with the frequencies for the respondent's last performance rating and their last salary position against scale salary, to see whether the results are similar to those found by Thompson. The results have been tested using the chi-square statistic to see whether the null hypothesis could be rejected on basis of the variance between observed and expected counts, and to consequently establish whether more highly rated or paid staff were more likely to find the PRP scheme fairer. The chi-square statistic is used because it is robust for testing categorical data. However, if more than 20% of the cells in the crosstabulation have expected values of less than 5, or if the minimum expected frequency is less than one, then the observed significance level based on the chi-square distribution may not be correct (J.Healey 1990). The expected values of the cells were increased in this case by combining values using the recode procedure to ensure that these parameters were so far as practical not exceeded.

Crosstabulating the respondent's performance assessment with their reported views on whether or not they had been paid more fairly as a result of the introduction of PRP, produced the following results:

**Table 8 ii – Crosstab Performance/views**

		Fairness/ Assessment			
		Count (Expected Value)	Not paid more fairly	not sure	Paid more fairly
Chi-square Pearson	Value 46.01452	needs improvement	14 (11)	1 (3)	0 (2)
		Acceptable	240 (216)	45 (52)	14 (32)
		good	94 (121)	37 (29)	37 (18)
Significance	.00000				

This suggests that there is a significant relationship between the assessment that individuals receive and their perceptions about the fairness of PRP. Looking at the observed count in each of the cells and comparing it to the expected count, it can be seen that the observed count exceeds the expected count in relation to a belief that respondents are being paid more fairly only where respondents are also assessed as good performers. This is hardly surprising, as intuitively it might be assumed that respondents whose performance was judged to be good would believe that the system was operating more fairly. But more critically, the number of respondents who

were rated as good by their manager who felt that they were not paid more fairly as a result of the introduction of PRP, is more than twice the number who did feel they were paid more fairly. This may mean that it is not just poor performers who become alienated by PRP. One of the benefits claimed for PRP is that poor performers are encouraged to improve their performance or leave, presumably because they do not believe that they are being fairly rewarded for the work that they do. However, if it is not just poor performers who believe that they are not being fairly paid, but also a substantial number of good performers, then the scheme may not be delivering the benefit claimed for it in this respect.

Poor performers are also more inclined to believe that they are not being paid more fairly as a result of the introduction of PRP than expected. However, despite the aggregation of values for both these variables to increase cell values, two of the nine cells contain expected frequencies of less than 5 and this equates to 22.2% of the cells. Consequently although the chi-square statistic shows that the variance between observed and expected counts is significant, it is difficult to be sure that the significance is reliable, because that statistic is based on breach the conventional rule that only 20% of expected values should be less than 5 (J.Healey 1990).

It was suggested above that one possible explanation for the relationship between a good performance rating and a belief that the PRP scheme is fair is that the respondent's view of fairness is influenced by the relative earnings

that they receive. A further crosstabulation of the respondent's view of fairness, this time with their last salary position against scale salary, shows, however, that there is no significant relationship between perceptions of fairness and position against scale salary (table 8 iii).

Table 8 iii – Crosstab salary/views

		Fairness/salary level	Count (Expected Value)	Not paid more fairly	not sure	Paid more fairly
Chi-square Pearson	Value 3.51209	Below scale	138 (137)	30 (30)	19 (21)	
		scale	63 (58)	9 (13)	7 (9)	
		Above scale	105 (112)	28 (25)	20 (17)	
Significance	.47604					

Salary position relative to scale salary in Thames Water is complicated by protection arrangements, which means that individual employees may have achieved a higher than scale salary simply because that is where they have been placed in order to protect overall earnings.

The evidence from this survey suggests that there is no relationship between an individual's position on the salary scale and their feelings about the fairness of the PRP scheme. There does however appear to be some relationship between rating assessment and perceptions of fairness. From

the employer's point of view this means that those they deem to be the best performers, that is to say those who get the best assessment, are more likely to find the system fairer, irrespective of their salary position. On the face of it this may be an attractive outcome for Thames Water, as it may encourage the better performers. The problem from the company's point of view is that the majority of employees, 72%, feel that they are being unfairly paid as a result of PRP and this may have a demotivating effect on them. It is also clear from the two crosstabulations above that the number of respondents saying that they felt that they were not rewarded more fairly was substantially greater than those who felt that they were being rewarded fairly, even amongst those who were rated as good or paid above scale. This again raises the question of whether or not PRP is acting as an incentive for poor performers to leave the organisation and good performers to stay. Respondents were asked two questions about leaving Thames Water. They were asked how strongly they agreed with the following statements:

“I sometimes feel like leaving this employer for good”

and

“Even if the firm were not doing too well financially, I would be reluctant to change to another employer.”

The data from the survey shows no significant relationship between either assessment or pay and the intention to leave Thames Water. Therefore the survey evidence does not support the proposition that the Thames Water PRP scheme is encouraging good performers to stay and poor performers to leave.

If fairness is being used as a determinant of which pay system employers should use, then the question arises, whose perceptions of fairness are the determining factor? The evidence from surveys of employers (Cannell and Wood 1992) and the prescriptions in management texts (Armstrong and Murlis 1994) are ambiguous about whose perceptions of fairness PRP is supposed to satisfy. From a theoretical point of view employers ought to be concerned with their employees' perceptions of fairness. Equity theory predicts that employees will adjust their work effort where those employees believe that comparators are being paid significantly more or less for comparable levels of work effort. Applying equity theory, employers ought to be concerned with employees' perceptions of fairness, as it is those perceptions which will have a direct effect on work effort. In this case the evidence from the survey shows that while Thames employees may view PRP as fair in principle, they do not believe it is fair in practice. Indeed given the report in Viewfinder 94, it is clear that Thames were aware of employee perceptions about the fairness of their PRP scheme.

### Motivation

In contrast to the largely positive view taken by respondents to the principle of relating pay to performance, a majority of respondents thought that the Thames PRP scheme failed to motivate employees. The survey asked employees whether they agreed that PRP had encouraged them to work harder, 70% disagreed with that statement, while 18% said that they had been encouraged to work harder by PRP (Appendix B.fiv).

Similar results were obtained in relation to two other questions, which also tried to ascertain the effects of PRP on employee motivation. Respondents were asked whether PRP was an incentive to exceed the requirements of the job and encouraged then to give sustained performance, roughly the same number said that PRP encouraged them to give sustained performance as those who felt PRP motivated them to work harder, rather less respondents felt that PRP was an incentive to exceed the requirements of the job (Appendix B.fv & fvi).

Individuals may not be the best judges of their own behaviour (Crozier 1964). They might, after all, be reluctant to attribute purely mercenary motives to their own efforts. Accordingly employees were asked whether PRP had encouraged other employees to work harder. It turns out that fewer respondents thought that PRP was motivating other employees to work harder, than those that believed that they had been encouraged to work harder by PRP, with a higher proportion of respondents being uncertain about whether PRP was encouraging others to work harder or not. These results set out in Appendix B.fvii suggest that respondents were perhaps reluctant to attribute motives to their fellow employees.

This view of the motivational effectiveness of PRP was reflected in some of the answers that were given to the open question in the survey, which ranged from scepticism about the motivational effectiveness of pay, as in

'The relationship between work and PRP is so tenuous little motivation is pay related' to more cynical view of the scheme, for example 'PRP is merely a management tool to distribute a fixed sum of money in the pot to the workforce, regardless of individual performance. As such it is unfair divisive unworkable and loathed by all.'

Taken at their best, these results show that PRP was having a motivational effect on 18% of respondents (Appendix B.fiv). Ideally the employer would no doubt want the PRP scheme to motivate all employees. However, even if only 18% of employees are motivated by the PRP scheme, it may nevertheless provide a cost benefit to the employer if the increased productivity from those 18% of employees outweighs any costs and disbenefit associated with the scheme. Some of the supposed disbenefit associated with PRP were dealt with in the survey, and the results from those questions are examined later in this chapter.

### Work quality

One of the supposed advantages of PRP, over payment by results systems, is that PRP allows employers to direct effort into things other than the simple quantity of work produced. As payment is contingent on inputs as well as outputs, it is possible for employers to link pay to quality and other measurements of a more complex nature, as well as the amount of work produced. The Thames PRP scheme contains a number of these more

complex measures of work performance. In order to try and assess the effectiveness of this aspect of the scheme, Thames employees were asked whether they agreed that:

"The existence of performance related pay has made you willing to improve the quality of your work."

The responses to this statement (Appendix B.fviii) were in fact very similar to the same statement about quantity of work (Appendix B.fix).

"The existence of performance related pay has made you willing to improve the quantity of your work."

It is difficult to be sure whether respondents felt able to distinguish between quantity and quality of work, but there is nothing in these results to suggest that PRP was having a differential effect on quality of work compared to its effect on quantity.

### Work priorities

Another supposed advantage of PRP is that it enables firms to cascade business objectives down through the organisation so that effort is focused on the firm's priorities. In other words PRP targets should lead employees to concentrate on achieving goals that are important to the employer. If the scheme was effective in guiding employees towards achieving organisational goals then it would be prioritising their work. Employees were asked whether they agreed that:

"Performance related pay has given you a greater incentive to get your work priorities right."

The results show that 73% of respondents did not feel that PRP was an incentive for them to get their work priorities right, and only 17% thought that it was (Appendix B.fx). One of the features of the Thames Water PRP scheme is that performance is assessed against seven criteria. The use of so many criteria may make it difficult for employees to identify quite what priorities Thames water wants them to concentrate on.

### Cultural change

Some organisations use PRP as part of a programme of cultural change (Kessler 1994) or as part of a strategic human resource management approach to employment (Tichy, Forbrun and Devenna 1982 and Thompson & Milsome 2001). Thames Water introduced PRP as part of their Employee Project, which aimed to generate a more flexible approach to work by their employees by breaking down some of the traditional barriers between groups of workers and between management and workers. The survey included a number of questions which aimed to test employee perceptions of the changes that had taken place in Thames during the period in which PRP had been in operation, without necessarily linking those changes to PRP. On the one hand, it would have been unfair to link the questions solely to PRP, as PRP was part of the wider Employee Project. On the other hand, by relating the questions to the time during which PRP had been in use, it is possible to get some feel for employee perceptions of the changes that have

taken place since the introduction of PRP. The introduction to these questions stated:

"This section asks about some of the other things that have been happening at work in the last two or three years."

The questions can be grouped into four categories.

i) Work intensification:

Firstly there were two questions which aimed at assessing whether employees felt about increasing workload. Nearly all respondents (92% Appendix B.fxi) felt that the pressure of work had increased in the last two or three years. Respondents' perceptions about workload appear to reflect employment trends in Thames. The number of employees in the area covered by this research, that is the regulated utility part of Thames Water's business, dropped from approximately 7,562 in 1992 to 6,673 in 1995 (Annual Report and Accounts 1993 and 1995). As a natural monopoly in the utility side of its business, Thames has a stable market and consequently reductions in the workforce will probably be achieved by increasing efficiency, which in may mean work intensification for a smaller workforce. At the same time employees continued to feel that there were likely to be further reductions in the workforce.

Only about 4% of respondents thought that there were unlikely to be any further reductions in the workforce, while 76% of respondents disagreed with the proposition that there was unlikely to be a further significant

reduction in the workforce (Appendix B.fxii). Taking these two results together, it is apparent that the majority of respondents felt that they were under increasing pressure as work intensified and numbers reduced.

ii) Communications:

Secondly, there were two questions which asked about communications between Thames Water and their employees (Appendix B.fxiii & fxiv). While the majority thought that communications had not improved, there were still a substantial number who thought that there had been an improvement and that Thames was more likely to listen to employees. Both these questions were testing improvements in communications, so that even though a majority said there was none, it could still be significant for Thames that as many as 30% of respondents (Appendix B.fxiii) thought there had been an improvement.

iii) Employee identification with Thames Water:

Respondents were also asked a series of questions that explored the extent to which employees identified with the employer. These questions were looking at how far old pluralist divisions had been replaced by a more unitarist view, where employee and employer interest were seen as the same by employees. Employees were asked whether the organisation's core values were supported by a larger proportion of the workforce than they used to be. While nearly 38% (Appendix B.fxv) thought that they were not,

a significant number, 26% thought that the organisations core values were supported by a larger proportion of the workforce.

When asked about divisions between employees and management, 77% did not feel that there was less of a feeling of 'us' and 'them' than there used to be, while only 12% of respondents thought that there was (Appendix B.fxvi).

Employees were also asked, whether they felt that they were being treated more as individuals, and whether PRP would lead to an increasingly individualised approach to the emolymment relationship by their employer. Essentially, this is a different approach to the same question about identification with the employer rather than with fellow employees. These questions are testing whether the employee believes that their individual contribution is valued or not and whether employees perceive that the employer is treating them as an individual rather than simply a cog in the machine.

A clear majority of respondents, 72%, did not agree that employees were more likely to be treated as individuals than they were in the past (Appendix B.fvii). However, over half of respondents, 53%, thought that PRP would lead to an increasingly individualised approach in the future (Appendix B.fviii). There is an apparent contradiction here, as most employees did not believe that they were being treated more as individuals than they had been in the past. At the same time, most employees thought that PRP would lead to a more individualised approach in the future. This highlights an important

point. The first question is about the employees' perceptions about how they and other employees are treated. Employees did not feel that they were being treated as individuals. In other words, they did not feel that their views were being listened to, or that they were being treated with respect, or that their contribution was being valued. The second question is concerned with the nature of the employment relationship, that is whether it is a collective or an individualised relationship. Employees saw PRP as a move away from the collective relationship. However it is important to be clear that a move away from a collective employment relationship is not the same as valuing employees as individuals. Nor as the answers to the two questions show is it perceived by employees as that. As one commentator (Gilman 1989) has observed PRP can be used by firms to create the impression of individualisation of the employment relationship, while at the same time extending control and standardisation.

#### iv) Outcomes:

Ultimately organisations try to change their culture in order to bring about a change in outputs. The mechanisms through which a change in output could be achieved through a change in organisational culture are discussed elsewhere in this thesis. It is argued that one possibility is that employee motivation will be increased. Equally, improvements in productivity might be made as a consequence of greater flexibility in relation to changes in working practices. Employees were asked two questions about working

practices, one dealt directly with flexibility and the other asked about trade union influence.

There was a roughly even split between those who thought that employees were more confident in being flexible about changes in their work and those who thought that employees were not more confident about being flexible (Appendix B.fxix). The question is asking about increased flexibility, rather than simply whether employees were prepared to be flexible, so the fact that 40% of respondents said that employees were more flexible is clearly a positive response from Thames Water's point of view.

Turning to the issue of the trade union role, some employers have used PRP schemes to diminish trade union influence (Cannell & Wood 1992, Kessler & Purcell 1992, Heery 1997a and Gunnigle, Turner & D'Art 1998). The most obvious way of doing this is to exclude the unions from collective bargaining over pay when PRP is introduced. However, the introduction of PRP into Thames Water was part of the 'Employee Project', which was agreed with the recognised trade unions in Thames Water, as have any amendments to the PRP scheme. The annual increase in PRP payments is agreed by Thames Water and their recognised trade unions on an annual basis. Thames Water appear, at least on the face of it, not to have used PRP as a mechanism for diminishing trade union influence. Nevertheless, PRP may effectively diminish trade union influence, if it is perceived by employees as individualising the employment relationship and placing more power in the

hands of line management, because they are responsible for performance assessment. And this appears to be what has happened in Thames Water. Employees were asked whether trade unions had a less important role in protecting employees than they used to have, 50% thought they had (Appendix B.fxx). It is worth pointing out that only trade union members were surveyed, so that one might assume that there would, if anything, be a bias towards believing that trade unions had a continuing role. While Thames Water appear not to have not actively pursued a policy of discouraging the trade unions, over the period that PRP has been in use about half the employees paid through PRP believe the importance of trade unions has diminished.

Overall, a rather complex picture emerges. While slightly more respondents thought that the workforce did not support Thames Water's core values, than those who did, a significant number were unsure. There is clearly a strong feeling that barriers between the workforce and employers have not been eroded in the last two or three years. On the other hand there was clearly perceived to be a move away from a collective employment relationship to an increasingly individualised one. Simply moving away from a collective employment relationship has not broken down barriers or increased identification with the company's core values.

Some of the views reported in Viewfinder 94 deal with the issues regarding company culture, which were tackled in the survey conducted for this thesis.

In relation to job security, 73% of employees said that they wanted job security, but only 35% said that their jobs provided it and only 33% said that they were satisfied with job security in Thames Water. While 66% said that job security had got worse in the last year or so. These figures are broadly consistent with the results of the thesis survey. On the other hand the figures in relation to communications are slightly different. Viewfinder 94 reports that 39% of employees were satisfied with communications, which is consistent with the thesis survey figures. Similarly 35% said that communications had got worse over the last year or so. However, only 12% thought that communications had improved in the last year or so, compared to around 30% of respondents to the thesis survey who said that they had found that communications had improved over the last couple of years. The questions asked were not the same and this may explain the discrepancy. Then turning to employee identification with the company, there seems to be a distinction in the results reported in Viewfinder 94 between employees views about their immediate working environment and their view of the wider company environment. A majority of employees were reported to be satisfied with working relationships (69%), supervisory practices (62%), and employee involvement (59%). But only a minority of employees was reported to be satisfied with company identification (49%), management effectiveness (32%), and company image (30%). Likewise, only 30% thought that Thames Water Utilities was well managed and only 20% thought that senior management provided a clear sense of direction. And therefore perhaps not surprisingly, only 47% of employees had a clear

understanding of the goals and objectives of Thames Water Utilities as a whole. Employee views of the wider company environment are similar to the results obtained in the thesis survey in respect of employee identification with the company, if marginally more positive. This difference may be explained by differences in the questions asked. In particular it is not clear what question was asked for Viewfinder 94 to ascertain whether or not employees were satisfied with company identification, or what is meant by company identification in this context, presumably it is to do with the company's image.

### Teamwork

One of the arguments used against PRP is that it damages teamwork (Demming 1982, Kanter 1989, Kohn 1993 and Pfeffer 1998). It is said that individual employees focus on the achievement of their performance targets to the detriment of team working, because those targets carry a financial benefit for the employee, while co-operation with the rest of the team does not. Many PRP schemes attempt to avoid this inherent problem with PRP by including team working as a target against which employees are assessed for the purposes of deciding whether or not they receive a performance payment. One of the seven criteria against which employees are assessed in the Thames Water PRP scheme is Working Relationships.

Employees were asked two specific questions about the effect of PRP on team working. Firstly, whether they thought as a general principle that PRP could damage teamwork; 26% thought that it could (Appendix B.fxxi). Secondly, they were asked whether the Thames Water PRP scheme caused jealousies between staff; 17% thought that it did (Appendix B.fxxii). It is this 17% figure, which is important, because it is this proportion of respondents who believe that PRP is having a dysfunctional effect on team working in Thames Water in practice. Consequently this is one of the disbenefits that needs to be balanced against the benefits of PRP in Thames, in order to make an assessment of whether PRP is of overall benefit to Thames.

### Working relationships

A related, but different point, about the negative effects of PRP concerns its impact on employees' working relationships with their managers. Some commentators (Kanter 1989, and Kohn 1993) have argued that the relationship between employees and their managers should be based on trust and co-operation. Instead, so the argument goes, PRP creates a barrier between the employee and their manager, because the manager also has to assess the employee's performance for the purposes of the PRP scheme. Employees are more likely to be cautious about taking managers into their confidence over issues which could affect their performance payment, than employees whose pay is not contingent on the achievement of performance targets. Equally, there is a danger that employees may be

too eager to keep on the good side of a manager who is responsible for making a performance assessment that will affect their earnings.

In the view of some commentators (Lawler 1981 and Siegall & Worth 2001) employee trust in their manager is a necessary precondition to the effective operation of PRP. The importance of trust for PRP to be an effective motivator is evident from at least two of the theories being examined in this thesis. Expectancy theory predicts that an employee will work harder for a reward, if additional effort will be instrumental in achieving that reward. In other words the employee has to take a view about the probability of a future event occurring, namely the payment of the reward, this is essentially a matter of trust. Put simply the question is does the employee trust the manager to make a fair assessment of the employee's performance. Equally in the absence of trust there may be problems of procedural and distributive equity from the employee's viewpoint that result in the employee adjusting their work rate, for example by doing the minimum necessary work, in an effort to find a more equitable balance.

Taken together these two views suggest something of a paradox. While, on the one hand, trust between the employee and the manager who reviews that employee's performance may be a precondition for the effective operation of PRP. On the other hand PRP may damage the trust between the employee and the manager who reviews the employee's performance by reducing the relationship to an instrumental level. The danger is that rather

than having an open and cooperative relationship with the manager the employee tries to manipulate the relationship in order to achieve a favourable performance assessment. This may adversely affect both the motivational effectiveness of PRP and also on then effectiveness of the firm.

The survey results suggest that PRP may have a negative effect on the level of trust between an employee and their manager. A substantial number of respondents, 44% (Appendix B.fxxiii), thought that PRP had eroded some of the trust that existed between them and the manager responsible for assessing them, while only 36%, thought that PRP had not eroded the trust between them and their manager. Similarly, 49% of respondents (Appendix B.fxxiii) felt that they had to keep on the right side of their manager to get a good rating. These results show that PRP is having a negative effect on the relationship between a substantial number of employees and managers. This ought to be an area of concern for Thames Water, both because it is likely to reduce the effectiveness of the PRP scheme and because of the wider implications in terms of the damage to then employee manager relationship.

#### Does sex matter?

It is important to Thames Water that the PRP scheme should not discriminate against women. In the first place, if it did, then the PRP scheme would not be operating efficiently, because it would not be directing

additional pay to higher performers irrespective of their sex. Secondly, it would be illegal, following the Danfoss (1989) ruling in the European Court of justice, and would therefore potentially render Thames Water liable to additional costs from a successful court action. And thirdly, of course, any discrimination against female employees would contravene Thames Water's own equal opportunities policy.

Bevan and Thompson (1992) have argued that PRP may discriminate against women in one of two ways. Firstly, they argue that there is potential for discrimination in the PRP process, that is to say in the way in which performance assessments are structured and carried out. The performance criteria used in PRP normally include qualitative measures, which require a degree of objective judgement by the appraising manager. Bevan and Thompson found that managers valued different attributes in men from those they valued in women, this in turn tended to reinforce stereotypical views of the sexes, which could in turn influence the performance criteria that were used and the rating assessment that individuals got from their assessing manager. In short they argue there can be bias in the assessment process. However, in the three organisations that they studied, they found that the distribution of appraisal ratings for men and women were broadly similar, presumably on the basis that men and women were performing at broadly the same level.

Bevan and Thompson go on to argue that the second way in which discrimination can occur is through the PRP outcomes. Assessment may lead to both further training opportunities or promotion, as well as an increase in earnings. They found that in two of the organisations that they were looking at men fared better than women in terms of the training and promotion opportunities that they were offered through the assessment process. Thus discrimination may not come about simply as a result of the assessment process, it may also be a product of the opportunities identified in the assessment process.

Thirdly, Bevan and Thompson found that there were differences in the merit payments received by the two sexes, which reflected the structure of the payment system. In one of the organisations that they looked at job grades which were dominated by men tended to attract higher levels of performance pay increase than job grades dominated by women. In two of the organisations, performance increases were to be linked to length of service, which in turn tended to favour men over women because women often leave the labour market to care for children. On the other hand, in two of the organisations, women tended to get higher percentage increases in earnings than men, because the PRP scheme gave a higher level of increase to those the lower down the salary scale, and the women were generally lower down the salary scale than men. The results obtained by Bevan and Thompson show that while discrimination may occur through the

appraisal system, it is also important to look at the way in which that is translated into earnings.

The results from the thesis survey have been analysed to see whether or not there is a significant difference in the performance assessment ratings given to men and women. But it is not sufficient to simply look at the performance assessments for men and women to see whether there are any significant differences. After all, there may be no significant difference in the performance ratings achieved by the two sexes, and yet that would still be discriminatory if women were out-performing men. First of all a comparison needs to be made of the inputs and outputs for men and women, and the assessments that are made of those outputs in the performance assessment process. If the inputs and outputs for each sex are not on average very different, then there should be no significant difference between the performance assessments. Conversely, if one or other of the sexes is performing significantly better than the other, then that should also be reflected in the performance assessments for the two sexes.

It is difficult to identify a useful measure of performance inputs and outputs to use in testing whether there is a significant difference between the performance of the two sexes. Ideally, it should be the same measure as that used for the performance assessment, but not the performance assessment itself. In the absence of such a measure, motivation has been used as a proxy for performance inputs and outputs, on the premise that

motivation reflects inputs, which then vary according to the individuals level of skill, and are then in turn reflected in outputs, which will vary according to other external factors. In other words, while motivation does not give the full measure of performance, for the purposes of the performance assessment, it is clearly a key element.

**Table 8 iv** Sex/Motivation

Count (Expected Value)	Male	female
Strongly motivated	6 (7)	4 (3)
Motivated	46 (50)	25 (21)
Do not know	47 (42)	13 (18)
Not motivated	165 (169)	74 (70)
Strongly not motivated	77 (73)	26 (30)

Chi-square  
Pearson Value 4.56399  
Degrees of freedom 4  
Significance .33503

Respondents' answers to the question do you agree "Performance related pay has encouraged you to work harder" have been crosstabulated with their sex. The results have been tested, using the chi-square statistic, to see whether the null hypothesis can be rejected on the basis that there is a significant difference in the motivation of men and women. It can be seen from the results in table 8 iv, that there is no significant difference in the

motivation of men and women. Taking motivation as a proxy for performance, it should follow that there is no significant difference in the performance assessment achieved by men and women.

The assessment rating for men and women has been crosstabulated to see whether there is any variance in the way in which men and women are rated. The chi-square statistic has again been used to see whether there is any significant variance between the way in which men and women have been rated at their performance assessment. The ratings in the PRP process have been amalgamated to ensure that there is a higher count in each of the cells, otherwise the results would be unreliable as the chi-square test is sensitive to low cell counts. The conventional rule is that if the expected frequency is below 1 or there are more than 20% of the cells with an expected count of less than 5, then the chi-square significance is viewed as unreliable (J.Healey 1990).

Table 8 v Sex/Assessment

Chi-square Pearson	Value .49162	Count (Expected Value)	Male	female
Degrees of freedom	2	needs improvement	11 (10)	3 (4)
Significance	.78207	acceptable	212 (211)	86 (87)
		good	116 (118)	50 (48)

It can be seen from the results in table 8 v that there is no significant difference in the performance ratings achieved by men and women in the previous year's performance assessment. Consequently it would appear that there is no significant bias in the distribution of either inputs or assessments between men and women. Thus the first of Bevan and Thompson's suggested discriminatory practices, namely through the operation of the assessment process, is not evident from the survey data.

The position of men and women on the salary matrix has also been analysed to see whether or not there is any significant difference between men and women. On the face of it, if men and women received non-discriminatory performance ratings over a number of years then their earnings as a percentage of scale salary should also show no significant difference between the sexes. Each year's performance rating would lead to increases in salary for employees where there was no significant difference between those earned by men and those earned by women. Yet it can be seen from table 8 vi that there is a significant difference between the percentage of scale salary earned by men and women. Fewer men and more women than might be expected, earned less than 92.5% of scale salary. Likewise there were more men than women earning over 107.6% of scale salary than might have been expected. Although looking at the cells it can be seen that the variation from the expected count is no more than seven in any particular

case, there is a significant difference between men and women's earnings. In contrast, there is no significant difference between the performance assessments achieved by men and women (Table 8.vi).

Two possible explanations for the difference in results between performance assessment and earnings seem likely. Essentially, that difference occurs because in some cases the employee's position in the salary matrix does not reflect that employee's rating at the last performance assessment. One explanation for this is that the initial assimilation on to the new grades, when PRP was introduced in Thames Water included a system for protection of earnings, which meant that employees were placed on different parts of the salary matrix according to their previous earnings. Consequently, if the assimilation system favoured one sex or the other, then that would distort the results. A second possibility is that women tend to take time out of the job market as carers. Length of service will clearly have an impact on the respondent's position within the salary scale, as even the best performer can only progress to the top of the scale after going through a number of assessments. A third possibility is that men are being appointed to new jobs higher up the salary scale. Thames Water does not always appoint new recruits at the bottom of the salary scale. Adopting Bevan and Thompson's analysis of discrimination, these three possible explanations would reflect structural discrimination in the pay system.

Table 8 vi

Sex/Salary

		Count (Expected Value)	male	female
Chi-square		less than 85%	9 (15)	12 (6)
Pearson	Value 19.56589	85-92.5%	48 (54)	27 (21)
Degrees of freedom	6	92.6-99%	72 (66)	19 (25)
Significance	.00331	scale salary	59 (57)	20 (22)
		101- 107.5%	59 (61)	26 (24)
		107.6- 115%	37 (30)	5 (12)
		over 115%	17 (17)	7 (7)

Another alternative is that the difference may be due to differential assessments over previous years, in which case the question is whether those assessments were based on an objective assessment of differential inputs and outputs, or whether they reflect past discriminatory practices. In other words there may have been bias in the assessment in previous years, which was still reflected in the position on the salary scale. This seems unlikely simply because it is unclear why bias in assessment would cease to be evident in the year that the survey was conducted.

The difficulty for Thames Water is that for what appear to be structural reasons, that is to say bias within the salary structure and its operation, women are placed lower on salary scales than men, even though there is no significant difference between the performance of men and women. The water industry is a traditional engineering process industry and like similar industries tends to conjure up an image of an industry dominated by men. It is to Thames Water's credit that their assessment system appears not to be discriminating in terms of the assessment process. The difference in position on the salary scale between men and women does however raise serious questions about whether or not the PRP system discriminates in favour of men. If there is no significant difference between the performance of men and women then there should be no significant difference in their position on the salary scale.

#### The cost benefit of PRP

PRP is more than simply a motivational technique, employers may use PRP to achieve a number of different outcomes. The thesis survey focuses on the motivational effectiveness of PRP in order to test a number of hypotheses, which are based on various theories of motivation, about the way in which PRP motivates individuals. However, it has also been possible to use the results of the thesis survey to see to what extent the Thames PRP scheme can be said to have motivated employees and how far the Thames PRP scheme can be said to have achieved other potentially positive

outcomes. The thesis survey results also show some of the negative effects of the Thames Water PRP scheme.

The positive and negative effects of the Thames Water PRP scheme need to be weighed up to see whether the PRP scheme is beneficial to Thames Water. There is a very real danger that employers fail to appreciate that PRP may have negative as well as positive outcomes. Perhaps it is because they do not appreciate the potentially negative effects of PRP that employers generally do not evaluate the effectiveness of their PRP schemes once they are in place, other than through the anecdotal evidence of managers (Cannell and Wood 1992). In that respect, Thames Water are unusual because they did commission a survey of their employees to see what their employees views were on a number of issues including PRP. However, the Viewfinder survey did not attempt to quantify the potentially negative effects of PRP in Thames Water. It showed that employees were sceptical about the effectiveness of the PRP scheme to the extent that only 15% of employees thought that the PRP scheme penalised poor performance, and even fewer, 13%, thought that it rewarded superior performance. But Viewfinder94 did not provide an objective basis on which Thames Water could weigh the benefits of PRP against the disbenefits. Effectively it highlighted employee cynicism about the PRP scheme.

The thesis survey shows that while at best 18% of respondents thought that PRP might be having some motivational effect, there were also considerable

disbenefits to Thames Water. Some 44% of respondents thought PRP had eroded some of the trust, which existed between them and the manager responsible for their assessment, and 49% of respondents felt they had to stay on the right side of their manager to get as good assessment rating. On the other hand, only 17% of respondents thought 'PRP has caused jealousies between staff', while 60% thought it had not. The lack of trust between employees and their managers may detract from the motivational effectiveness of PRP and may have a negative effect on the operation of the organisation. If employees simply see the relationship with their manager as instrumental and one, which they need to manipulate in order to secure a benefit, this may well distract them from wider corporate objectives or from taking appropriate risks. On balance, the survey appeared to show that PRP was having a detrimental effect on the working relationships of more employees than it was motivating.

One of the other benefits that is sometimes claimed for PRP is that it encourages good performers to stay and poor performers to leave. The evidence from the survey suggests that the Thames water PRP scheme has not been particularly good at achieving any of these objectives. There is no significant relationship between respondents' PRP assessment and their views about whether they were likely to leave Thames Water. Consequently it would appear that the Thames water scheme is failing to exercise either a pull on good performers or a push on poor performers.

A cost benefit analysis depends upon quantifying the cost and the benefits of PRP. This must depend on the value that Thames Water places on both the costs and benefits that accrue from PRP. The issue is simply are the disadvantages of PRP outweighed by the benefit of the motivational effectiveness of PRP in respect of 18% of respondents, or are there other benefits that make PRP worthwhile for Thames Water, it has been argued in this thesis that Thames Water are more concerned with the benefits of PRP as a mechanism for achieving a change in organisational culture, than in any straightforward cost benefit.

The results from the survey in respect of cultural change are also mixed. Respondents were asked about changes over the last two or three years, that is to say over the life of the PRP scheme. While employees felt less secure in their employment, around a quarter of respondents also reported improved communications, and over 10% said that they identified more closely with Thames Water. Perhaps most important of all from Thames Water's point of view, 40% of respondents said that employees were more confident about flexibility at work. There also appears to be an unintended change in the culture in Thames Water, as a direct result of the introduction of PRP, as the relationship between employees and their managers changes and becomes more instrumental.

One difficulty with these results as a measure of PRP as an engine of cultural change, is how far change in culture can be attributed to PRP. While it is

clear from the qualitative research that a number of key players saw PRP as being principally concerned with cultural change, it is less clear how far PRP has been responsible for bringing about cultural change in Thames Water. Privatisation, changes in the management as new managers were brought in from outside, reduction in the workforce, as well as changes in the messages coming from the company, may all have played a part in changing the corporate culture. The question is how far PRP contributed to the change in corporate culture in Thames Water. A model explaining the processes by which PRP might bring about cultural change was suggested in one of the earlier Chapters. Application of the model to the survey data suggests that PRP may have helped bring about cultural change in Thames Water but it is less clear how big a part it played. The evidence suggests companies may well be using PRP as a mechanism for bringing about cultural change, it is less clear how important PRP is as an agent for cultural change.

Cultural change may be the justification for using PRP, nevertheless the more effective the PRP scheme is in motivating employees the more beneficial it will be from the point of view of Thames Water. And to that extent the company has an interest in ensuring that the PRP scheme is motivationally effective, even if the principal objective in using PRP is not primarily to motivate employees. The difficulty with motivation is that the evidence, which can be quantified, shows that PRP is not a particularly effective motivator.

Employers focus on soft outcomes such as cultural change, because these soft outcomes fit in with a broader agenda, but the results are less readily quantifiable. PRP may be attractive as an agent of change because:

- Other companies use it, particularly in the private sector.
- It gives managers greater power and forces them to manage.
- It helps justify highly differentiated individual pay at the top of the organisation.

Each of these elements can be seen as an aspect of cultural change. Using PRP because other private sector companies use it, is a way of signalling the type of organisation you are. This can be important especially for privatised companies like Thames Water. Empowering managers by devolving pay decisions to them, and forcing them to confront performance issues through the appraisal system is again an important message. Finally some of the biggest pay increases as a result of privatisation have been for those at the top, these increases have been justified by arguments about market rates and rewarding performance (Hodgson, Kirkwood & Smith 1999 and the Top Pay Research Group 2003). PRP fits with an ethos of rewarding performance, even if the benefits are less dramatic lower down in the organisation.

### Conclusions

PRP does not appear to be motivating the majority of Thames Water employees, the survey results suggest that at best it is only 18% who are motivated. Nor is there any evidence that PRP is encouraging poor

performers to leave Thames Water. Indeed the evidence is that a majority of even good performers feel that PRP is not rewarding them fairly. On the other hand, it was clear from the survey that PRP is having a negative effect for a substantial number of employees on important working relationships. A number of respondents report that PRP was causing jealousies amongst employees and might damage teamwork. Perhaps more importantly nearly half said that it had damaged the trust between them and their manager.

Thames Water wanted to use PRP as an engine of cultural change and it might be argued that this meant that the motivational impact of PRP was less important to them. Even here the evidence is patchy. While a number of employees reported a less collective more individualistic working environment, most employees did not feel that they were more valued as individuals. A substantial number of employees reported an increase in work flexibility, but it was quite unclear that this was as a result of PRP. Perhaps the most important question for Thames Water in respect of cultural change is whether they wanted to create a culture in which employees reported that team working could be damaged and a lessening in trust in their managers.

## **Chapter 9**

### **PRP and motivation in Thames Water.**

#### **Introduction.**

The outcomes of the Thames Water PRP scheme, from the employer's point of view, were considered in Chapter 8 using the results of a survey of Thames Water white-collar employees conducted for this thesis and comparisons were made with other survey results. The survey shows that fewer than 20% of respondents reported any positive motivational effects from the PRP scheme. The results also show that the PRP process may actually be making the relationship between managers and employees more instrumental and reducing employees' trust in their managers. It is argued in this thesis that a reduction in the lack of trust between employee and manager may have an adverse effect on both the organisation and the motivational effectiveness of PRP because of the importance of trust in respect of both the instrumentality and fairness of PRP. It is hypothesised that the motivational effectiveness of the PRP scheme, or indeed the lack of it, can, at least in part, be explained by various theories of motivation. Goal setting theory in particular might explain the motivational effectiveness of PRP in terms of the performance management elements of the PRP process, that is to say the appraisal, rather than in terms of the financial reward. Finally, a mechanism has

been proposed whereby PRP might bring about changes in organisational culture. This chapter tests these hypotheses.

The key elements, which are being tested from each of the various theories of motivation, are examined against relevant data from the survey, to see how far the results are consistent with those theories. Using the survey in this way gives an overview of the extent to which the Thames Water PRP scheme puts into practice the various elements necessary for the operation of each of the theories. However, these results need to be seen in the overall context that, at best, only 18% of those surveyed said they were motivated to work harder as a result of the introduction of PRP. It is the extent to which there is a significant relationship between employee motivation and the key elements of any particular motivational theory that determines how far a theory of motivation is useful in explaining employee motivation.

#### The elements of the theories.

This thesis has focused on the three theories of motivation, which it is argued are the most relevant to an understanding of the motivational effectiveness of PRP (see Chapter 3). Two of these theories, expectancy theory and goal setting theory, are cognitive theories of motivation (Vroom & Deci 1992). The other theory, equity theory, is concerned with the individual's response to how others are treated, that is to say it is a

social cognitive theory of motivation (Arnold et al. 1995). These cognitive and social perspectives provide a useful framework for analysing the results from the thesis survey in order to see how far each of the three theories of motivation and associated hypothesis helps to explain the motivational effectiveness of PRP.

Cognitive theories of motivation focus on the processes by which the individual works towards goal achievement to explain motivation (Vroom & Deci 1992). They work on the premise that individuals will work to achieve a goal that they are committed to achieving. It is said that the amount of effort the individual will input to achieve the goal can be understood by reference to the process by which the goal is set and the mechanism by which the individuals commitment to that goal is obtained. So in order to understand how far these theories are relevant to the Thames Water PRP scheme it is necessary to look at the goal setting and goal commitment processes within the scheme.

The first step is to look at the target or goal setting process. The central concept in cognitive theories of motivation is the premise that behaviour will be directed, that is to say intentional (Lewin 1951). The process by which the individual's behaviour is directed or given a goal is therefore critical to an understanding of motivation using cognitive theories of motivation. This raises the preliminary questions has the individual been

given a goal and if so is the goal clear to the individual. These issues are examined in the next two sections of this Chapter.

The directive effect of a goal will be a function of the individual's acceptance of and commitment to the goal. According to expectancy theory goal commitment is determined by the expectancy of a valent outcome. The greater the valence of the outcome the more motivated the individual will be to achieve that outcome. In expectancy theory valence, expectancy and instrumentality determine both goal commitment and motivation. Goal setting theory is less explicit about the determinants of goal commitment and predicts that goal difficulty rather than the level of goal commitment will determine effort. Goal commitment is examined after target setting and target clarity. The mechanisms for achieving goal commitment are looked at in terms of the outcomes for the individual. Those outcomes may be the explicit financial rewards: in the case of the Thames Water PRP scheme this means the performance payment. The individual's perception about the relationship between effort and the performance payment is critical to the process of motivation. For some individuals non-financial rewards may be important valent outcomes. Some of these non-financial rewards may be extrinsic, but others may be intrinsic that is to say arise from feelings that the individual experiences as a result of achieving their goal, such as feelings of self-efficacy. Both goal commitment and each of the potential outcomes are explored.

Equity theory has been described as a social cognitive theory of motivation, because it predicts that goal direction for the individual will be critically determined through comparison (Arnold et al. 1995). In other words equity theory is concerned with the process used for goal determination and goal commitment. But it predicts that the individual's level of motivation to achieve that goal will be determined by reference to comparison with others in the broader social context. The individual is concerned with fairness and specifically comparative fairness. There are two aspects to fairness. One is procedural; are the procedures employed to determine the outputs the individual gets for their inputs fair (Greenberg 1987)? The second is distributive; is the ratio of inputs to outputs fair (Adams 1965)? Each of these aspects is considered in turn.

Finally two further aspects of the Thames Water PRP scheme are considered at the end of this Chapter. These are essentially aspects of the PRP scheme that seemed particularly important from the company's point of view. It is apparent from the qualitative research reported in Chapter 7 that, aside from managing their salary bill, the company was primarily concerned to achieve two objectives through the introduction of PRP.

- ◆ Ensure performance took centre stage in the employment relationship (Performance Management)
- ◆ Change the corporate culture

In relation to the first point about Performance Management, the need to ensure that performance took centre stage in the employment relationship, there was a concern that managers were not talking to employees about their performance. PRP was meant to ensure that managers had to talk to employees about their performance. The issue of feedback from managers is explored towards the end of this Chapter. From a theoretical perspective, feedback forms part of the cognitive approach to motivation. Some of the goal setting literature emphasises the importance of feedback (Pritchard et al.1988). Nevertheless it seems appropriate to deal with it separately as one of the consequences Thames Water intended to come out of the introduction of PRP.

Cultural change on the other hand does not fit into the theoretical framework examined above. Corporate culture is seen as a means of exercising control over behaviour employee behaviour through a system of normative order (O'Reilly 1989). So it is argued that if an organisation can change its culture to one that fully supports the organisation's strategic aims it will become more effective by reducing transaction costs and improving performance as employees behaviour conforms to corporate objectives (Denison 1990). Thames Water saw the introduction of PRP as part of a programme of cultural change. It has been suggested that a substantial part of the explanation for the spread of PRP in the UK is its role as an agent of cultural change (Kessler 1994).

The processes by which cultural change can be achieved were considered in Chapter 5 and those processes are examined further in relation to the survey evidence at the conclusion of this Chapter.

### Target Setting

The Thames Water PRP scheme judges employee performance against certain general criteria or traits and against the achievement of specific targets and objectives set for the employee during their SPR. Although the SPR is not formally part of the PRP scheme it plays an important part in the PRP process, as it enables managers responsible for reviewing performance to set targets and discuss performance. All employees are meant to have at least one SPR each year, more can be arranged if it is felt appropriate.

The survey results show (item c1 Numbersprs) that the majority of employees had one SPR (62%), with some (13%) having two, and some having three or more (2%), within the preceding twelve months. However, 22% of respondents reported that they had not had an SPR in the last twelve months. Less than 1% of respondents had been with Thames Water less than a year, so there was a fairly substantial proportion of the workforce in receipt of PRP who had had no targets set for them, at least not annually, even though they should have done. It turns out that the problem relates to the tenure of Thames Water

Managers. Julia Cherrett, the Thames Water Director of HR for the UK and Ireland, commenting on these figures said:

'The pace of change in the Company is now so fast that our own figures show that managers are in post for no more than 18 months on average. This poses a real problem for us in terms of managers developing a relationship with those employees they are responsible for managing. My guess is that it is the turnover in managers that leads to such a high proportion of SPR interviews not being done.'

Harris (2001) found in a survey of middle management attitudes towards PRP that 17% thought PRP was unworkable in a time of major organisational upheaval. The problem from Thames Water's point of view is that the survey of Thames Water staff was not conducted at a time of any greater upheaval than usual. Thames Water would argue that they are a dynamic company where managers can expect to move on rapidly. On the other hand one of the arguments Thames Water used to justify the introduction of PRP is that it would ensure that managers talked to the employees that they managed about their performance. It may be that without the incentive of PRP even fewer SPR interviews would have taken place, but if a fifth of those surveyed did not have an SPR in the last year then the PRP scheme is not being wholly successful in ensuring performance management takes place.

The SPR interview is critical to the operation of both the Thames Water PRP scheme and the operation of at least two of the theoretical models being examined in this thesis and the large number of staff not receiving an SPR interview could well have an adverse effect both on the

motivational effectiveness of PRP and on its effectiveness as an engine of cultural change. On the face of it, failure to ensure that all employees got an SPR interview could well have had a damaging effect on the function of the Thames Water PRP scheme as an employee motivator. The danger is that in the absence of the annual SPR, the employee may have been left without objectives or targets against which their performance could be assessed, or the targets that they had may have been out of date or no longer relevant. If no targets are set, or performance against target is not appraised on a timely basis, then this is likely to have an adverse effect on employee confidence in the link between pay and performance. Indeed the setting of effective targets at the SPR would appear to be a precondition to the operation of both expectancy and goal setting theory. Yet a substantial proportion of the workforce appears to have had no SPR in the last twelve months.

The association between the SPR interview and the motivational effects of PRP can be tested using a crosstabulation of the effectiveness of PRP and whether or not the employee has had a SPR interview in the last twelve months. Somewhat surprisingly there appears to be no association. This suggests two alternatives. Objective setting may be irrelevant to the motivational effectiveness of PRP. Alternatively it may be other factors in the objective setting process that determine whether or not PRP has any motivational effect. The evidence supports the latter interpretation. Consequently the Thames Water survey shows that it is

not the process of the SPR interview that makes PRP motivate employees, but other factors associated with that process. And that surprisingly employees can feel motivated by PRP even when they have not had an SPR interview, or at least not in the last twelve months.

Table 9 i Motivation/Number of SPR Interview in last year		Count (Expected Value)	Not Motivated by PRP	Motivated by PRP
Chi-square Pearson	Value .69061			
Degrees of freedom	1	None	74 (72)	9 (11)
Significance	.40596	At least one SPR	348 (350)	58 (56)

### Target Clarity

Target clarity is important for a number of reasons. The Thames Water PRP scheme requires managers to set clear targets and, if the targets are not clear, employees may not know or understand what is expected of them. Indeed research on goal setting theory (Earley, Connolly & Ekegren 1989) contrasts the motivational effectiveness of giving specific targets with the simple 'do your best' type of approach. Goal

specification is also important in expectancy theory. If the goal that is set is ambiguous or unclear both the link between goal achievement and a valent outcome and the expectancy that there will be a valent outcome will be eroded.

The questionnaire asked respondents what had happened at their last SPR, whenever that was. Respondents were asked how long their SPR interview had taken (c8 Sprlength); 23% reported that the interview lasted less than 30 minutes, 32% said that the interview lasted more than 30 minutes but less than an hour, and 39% reported that it lasted over an hour. Most respondents (58%) seem to have had four, five or six objectives set for them during their SPR (c2 Numbergoals). If the manager allows insufficient time to explain all the objectives that are being set and how they are to be achieved, there is a danger that the employee be unclear about what is expected of them. Respondents were asked (c3):

'Was it clear to you at the Staff Performance Review how you could achieve the objectives which had been set?'

A majority (63%) was either quite clear or very clear about how they could achieve the objectives that were set for them. This left 20% of respondents who were unclear about how they could achieve the objectives set for them at their SPR and therefore unsure as to whether, if they tried harder, they could increase the reward they received. The greater the length of the SPR interviews the greater the goal clarity (r.27)

and the fewer targets set the greater the goal clarity (r.21). This would suggest that Thames Water training on the PRP scheme for manager should, amongst other things, ensure that managers avoid giving employees too many targets and ensure that they allow sufficient time at the SPR interview to explain the targets that they are setting. That should help to ensure that a higher proportion of employees is clear about the targets that have been set for them.

### Commitment to the Targets

Respondents were asked about their commitment to the objectives that were set for them at the SPR interview. The goal setting literature in particular has emphasised the importance of the employees' 'buying in' to the objectives that have been set (Locke, Latham & Erez 1988). Some commentators have suggested that there is likely to be greater goal commitment where the employee agrees to the objectives that have been set (Latham, Mitchell & Dossett 1978, and Erez & Arad 1986); or where the legitimacy of goal assignment is accepted (Oldham 1975); or where there is a greater degree of trust between the employee and the person assigning the goals (Early 1986).

Employees were asked a number of questions about the nature of the goal setting process during the SPR interview (Appendix C.f1,fii &fiii). A majority of respondents felt that their manager took the SPR seriously

(54%) and that they had the right amount of influence over the process (51%). And a much larger proportion (83%) felt that the objectives that they were being set were relevant to their job.

When asked directly about their commitment to the goals that had been set for them (Appendix C.fiv), a clear majority (76%) of respondents reported being committed to the goals they had been set at the SPR, while only 11% said that they were not committed to the goals that had been set. Goal commitment is correlated to the manager taking the SPR interview seriously (r.30), the respondent feeling that they had the correct amount of influence over the goal setting (r.35), and the perceived relevance of the goal to work (r.37).

The literature suggests there is a link between employee feelings about involvement in setting targets, the legitimacy of those targets, the relationship with the manager, and goal commitment. It is clear from the survey that that there is an association between involvement with setting the targets, the legitimacy of those targets, the relationship with the manager, and goal commitment, in the Thames Water scheme. Indeed a majority of respondents reported being committed to achieving the goals that were set for them at the SPR interview. However, only 22% said they were very committed to achieving the targets that had been set for them. Greater emphasis by managers on getting employee buy-in to the targets that are set, either through greater involvement in setting those

targets or through giving greater emphasis to the legitimacy of those targets, might increase the level of commitment employees have to achieving the targets.

### Extrinsic employee rewards

The Thames Water PRP system links increased pay to the achievement performance criteria and specified objectives or targets. Employees were asked whether they thought they could get more pay by working harder, both in respect of the objectives set at the SPR and in respect of the performance criteria. In response to the question:

'Do you believe that by trying harder to improve your performance in relation to the Performance Criteria it would be possible to increase the amount of pay that you earn?'

Yes ...19.7%  
No ...73.4%  
Do not know ...6.4%

A similar question was asked about the objectives set at the SPR:

'Do you believe that by trying harder to achieve the Objectives that are set for you at the Staff Performance Review it would be possible to increase the amount of pay that you earn?'

Yes ...14.2%  
No ...78.5%  
Do not know ...5.6%

A substantial majority of respondents clearly did not believe that they could increase the amount they earned by working harder to achieve either the objectives or performance criteria set for them. This is fundamental to the question of motivation. Expectancy theory in particular would suggest that motivation has a direct relationship with the ability to secure valent rewards such as higher earnings. It also seems to be at odds with the whole concept of relating pay to performance to have nearly 80% of the employees believing that they cannot improve their pay by working harder on the targets set for them.

Respondents were marginally more optimistic about the effects of goal achievement on future pay increases. They were asked whether by achieving the goals set for them, they would increase their pay prospects in the future (Appendix C.fv). Although a majority of respondents (55%) did not believe that their future pay prospects would improve if they achieved the goals set for them, some 27% believed there was a link between attaining their SPR goals and future pay increases. One possible explanation for the difference between the numbers who thought that by working harder they could increase their pay and the larger number who thought achieving their goal would improve their future pay prospects may be a belief in the increased prospect of promotion if you achieved your objectives, and it turns out that 21% (Appendix C.fviii) of respondents thought achieving your objectives would improve your prospects of promotion. However there is also an important difference in

the wording of the two items, the questions about the immediate pay rise, items motivecriteria (h2) and motiveobjectives (h1), are asking about an effort reward relationship, whereas the item goalpayrise (d5) is concerned with the possible future outcomes. It is the effort reward relationship which is at the heart of PRP.

### The relationship between effort and reward outcome

It is important to understand why the majority of respondents did not believe or expect increased effort to lead to an increase in pay. One way of looking at the issue is to consider it in three parts. Firstly did employees have the necessary skills and abilities in order to achieve the targets set for them? In other words were these achievable targets? Secondly, did they believe that they would have to work harder to achieve the objectives that had been set? There is always the possibility that employees believe that the targets would be achieved irrespective of any additional effort on their part. And finally, did they believe that by working harder they would achieve the target and get a performance payment?

Most respondents thought that they had the right skills and ability to achieve the targets that were set for them (Appendix C.fvi). It is important to note that 20% of respondents were either not sure whether or not they had the right skills to achieve the objectives that they had

been set or believed that they did not have the necessary skills. Ideally, all employees should feel that they have the necessary skills and ability to achieve the target set for them. The Thames Water SPR interview is in part designed to address employee development issues and issues about skill levels and training should be addressed in conjunction with the target setting process.

Employees were also asked whether they agreed that:

'It will be necessary to increase your effort at work to achieve the Objectives that have been set for you.'

Nearly half respondents thought that they would have to increase their effort in order to achieve the objectives that had been set for them (Appendix C.fvi). This result is more interesting when looked at in conjunction with the other evidence from the survey about respondents' beliefs about their ability to achieve the objectives set for them and the consequences for them of doing so. Not surprisingly there was an association between respondent's belief about goal difficulty (Difficultgoal D7) and respondents belief that they would have to work harder to achieve the objectives that had been set for them, (r.41). Nevertheless most respondents, 77%, thought that they had the skills and ability necessary to achieve the targets that had been set for them. Yet only 20% of respondents thought they could earn more by working harder to increase their performance in relation to the performance criteria set for them (Motivectoria h2). And even fewer respondents, 14%, thought that they could increase their pay by working harder to achieve the

objectives set for them at their SPR (Motiveobjectives h1). This clearly suggests that respondents believed there were significant process problems in the Thames Water PRP scheme.

That still left nearly half of the respondents who either thought that they could not achieve the targets set for them through increased effort or who were unsure whether or not they could. Leaving aside those who were unsure about whether or not they could achieve the target set for them by increasing their effort. Just under a third of respondents who did not believe that they would have to increase their effort to achieve the target that they had been set. It follows that they either thought that they would achieve the targets without any additional effort or that they could not achieve the targets even with additional effort. Those who thought that they could not achieve their targets, even if they worked harder, seem likely to have done so for one of three reasons. Firstly, they may have believed that they lacked the relevant skills or ability. Secondly, they may have believed that the achievement of those targets was dependent on factors beyond their control. And finally they may have believed that their managers' assessment of whether or not they achieved the targets was likely to be unfair or biased in some way.

The employees' perceptions about the connection between effort and receiving more pay are also relevant to equity considerations. The implications are perhaps most obvious in respect of procedural equity. If

the Thames Water PRP scheme is not perceived by employees to be operating fairly then procedural equity theory predicts they will actually decrease their effort in response to the inequity (Greenberg 1987). Distributive equity is based on the individual's perceptions about the treatment that they are receiving compared to others who they consider their relevant comparitors. If they believe that they are being less well treated then according to equity theory the amount of effort that they put in will be adjusted downwards to compensate (Adams 1965).

So in summary, it can be seen that there are two ways of looking at the theoretical implications of respondents' feelings about the link between effort and reward. Firstly using expectancy theory, scepticism about the link between hard work and pay can be seen as reflecting concerns about the instrumentality of the scheme or the expectancy of a valent outcome. And from an equity point of view, these same feelings can be seen as concerns about the fairness of the operation of the scheme. Essentially these are issues of trust, does the employee trust the manager who is responsible for assessing that employees performance to behave fairly and does the employee trust the employer to translate a fair assessment into an appropriate performance payment.

### Non pay extrinsic reward outcomes

PRP links pay to performance and consequently focuses on pay as the outcome for performance. From the employee's point of view there may be other perhaps more or equally important consequences. The survey questionnaire asked about job security, promotion and increased self-confidence as possible outcomes from achieving the SPR goals. Respondents were less optimistic about the impact of achieving their goals on their promotion prospects than they were about the impact on future pay rises (Appendix C.fviii). Only 21% thought that achieving their SPR goals would improve their promotion prospects. As against 51% who did not believe that achieving their SPR goals would improve their promotion prospects. These results may reflect Thames Water's decision to reduce the number of grades when PRP was introduced, which in turn would have reduced the opportunities for employees to get a higher grade.

Respondents were slightly more optimistic about the effect of achieving their SPR goals on job security (Appendix C.fix). Although a majority, 51% of respondents did not believe that there was any link between the objectives set at the SPR interview and job security, 29% did. In fact the agreed redundancy selection process in Thames Water does take account of employees' performance in their job, so that there is a very real

connection between job security and performance assessment. It is also worth recalling that 76% of respondents (i3 Nojobcuts) thought that there was likely to be further significant reduction in the size of the workforce, while Viewfinder 94 reported that 73% of employees said that they wanted job security. It would appear that job security would be quite an attractive extrinsic reward for the majority of Thames Water employees.

The results of the survey in respect of pay increase, promotion, and job security, reflect respondents' beliefs about the instrumentality of the objectives in respect of extrinsic rewards. In no case did a majority of respondents see a link between attaining the objectives set for them at the SPR interview and the extrinsic reward. This may in part reflect some of the process problems encountered in respect of SPR interviews. The proportion of respondents who agreed that there was a link between achieving the objectives set for them and the three extrinsic rewards ranged from 14% to 29%.

Intuitively it could be assumed that pay increases would be more readily linked with performance than the other rewards, in a pay scheme that explicitly links pay to performance. Surprisingly, fewer respondents reported links between achieving the objectives set for them and pay, than between achieving those objectives and the other two extrinsic rewards. One possible explanation for this is that the more intangible

nature of the non pay rewards may make it easier for respondents to believe that they are linked to achieving the objectives, than the more tangible reward of a performance payment.

### Intrinsic employee rewards

Quite apart from any extrinsic rewards that the employee might expect as a result of achieving the objective set for them, there is the prospect of intrinsic rewards. These intrinsic rewards may come about through feelings of achievement or feelings of pride in a job well done. Porter and Lawler (1968) have elaborated on the basic expectancy model and argue that the individual's motivation will be a function of both intrinsic and extrinsic satisfaction. It has also been argued that personal goals are important in goal setting theory (Earley & Lituchy 1991), because the individual's feeling of self-efficacy is enhanced when those goals are achieved, which in turn improves their future performance. Respondents were asked whether they agreed with the following statement about their SPR interview:

'Attaining the goals set for you would increase your sense of self confidence at work.'

Over half of respondents, 56% (Appendix C.fx), thought that achieving the goals set for them would increase their self-confidence, while only 30% said it would not. It is interesting to note that a higher proportion of respondents thought that achieving their PRP goals would lead to an intrinsic reward (56%), than believed that it would lead to an extrinsic

reward (14% to 29%). The contrast between these figures may reflect employee perceptions about the instrumentality of the scheme. While extrinsic rewards depend upon the effectiveness of the scheme in delivering rewards for goal achievement; intrinsic rewards depend upon the employee's own feelings about achieving the goals set for them.

### Fundamental and ancillary rewards

In assessing the Thames Water PRP scheme, it is worth noting that only one of the four potential outcomes above examined in the survey is fundamental to the scheme itself. The explicitly stated outcome for the employee, who achieves the objectives that have been set, is a performance payment. If employees believe that achieving the objectives set at the SPR interview will also improve their job security, promotion prospects and increase their self-confidence, these are ancillary and unspecified outcomes. They are also outcomes that could presumably be achieved without a PRP scheme. So, for instance, an effective appraisal or SPR system could lead to increased job security, promotion prospects, and increased feelings of self confidence for those who achieved the objectives that were set for them, without the need for a performance payment. This raises the interesting question of whether an appraisal scheme which did not involve monetary reward would have the same motivational effectiveness as the PRP scheme. Potentially such a scheme might also avoid some of the negative effects, which equity

theory and some commentators (Marsden and Richardson 1994, Isaac 2001, and Brown and Benson 2003) suggest might be associated with feelings of inequity about the level of reward some individuals receive. It has been argued that the danger is that managers might fail to carry out the appraisal if it had no financial outcomes associated with it. After all even in the Thames PRP scheme around 20% of respondents to the survey reported that they had not had an SPR in the last twelve months.

### PRP and Equity

Most employees did not appear to be generally antipathetic to PRP in principle. Respondents were asked in Section A of the questionnaire for their views on PRP generally, as distinct from their views about the Thames Water PRP scheme. A majority, 67%, agreed with the proposition that PRP was a fair way of paying staff and only 18% said that it was not (Fairgen a1). More respondents, 45%, agreed with the statement:

'Employers benefit from having a well designed performance related pay scheme, because employees work harder.'

than disagreed with it, 32% (Prpmotivate a2).

However when it came to the Thames Water PRP scheme employees were less satisfied with the fairness of PRP, particularly as it affected them. When asked whether they agreed with the statement:

'You personally have been paid more fairly as a result of the introduction of performance related pay.'

Fairme (h6)

72%, said that they disagreed with the statement, while only 11% agreed with it (Appendix B.fii). Equity theory suggests two mechanisms by which dissatisfaction with the fairness of PRP might adversely affect employee motivation, that is either through procedural or distributive equity.

### Procedural equity

The procedure for setting targets and assessing employee performance against those targets depends on the employee's SPR. Some aspects of the SPR process have already been explored above and, in so far as that process fails to support the causal link between target setting, performance assessment and reward, this may have caused employees to believe that the PRP process was unfair. Employee perceptions of the fairness or otherwise of the procedure may also have been heavily influenced by their views about how fairly their manager had assessed their performance. This is an important issue from Thames Water's point of view. One of the company's reasons for introducing PRP was in order to create a more performance focused relationship between managers and employees. If instead of the employee manager relationship being positively focused on performance issues by the PRP scheme, that relationship is soured by employee concerns over the fairness of the

manager's performance assessment, the PRP scheme may have the opposite effect to that intended.

Employees were asked whether their most recent assessment was a fair reflection of their performance (Fairgenassessment f4), and as can be seen from the Appendix, 57% thought that it was, while 25% thought that it wasn't (Appendix C.fxi). The 25% who did not feel that their last assessment was a fair reflection of their performance, clearly believed that there was some unfairness about the system of performance assessment. The results of the survey suggest a number of possible reasons for this.

Some of the problems appear to have been attributed by respondents to the specific assessment they been given. For some respondents the principal problem was the nature of the assessment criteria, as for the 22% who felt that the performance criteria against which they were being assessed were not fair (Fairgencriteria f6). For other respondents it was their manager's ability to apply those criteria. Thus 33% of respondents did not believe that the manager knew enough about them to make an accurate assessment of their performance (Prpmanagerknow f3).

Clearly, the relationship between the manager carrying out the assessment and the employee being assessed, and the employee's

perceptions about that relationship, are important to the operation of PRP. There is always the danger that employees will feel that their manager is doing the performance assessment subjectively, and using PRP to reward those employees who are most compliant or who fit in, the so called 'blue eyed boy syndrome'. When asked whether they agreed with the statement:

'You have to keep on the 'right side' of your manager to get a good assessment rating.'

48% of respondents agreed that they had to keep on the right side of their manager to get a good assessment rating (Appendix C.fxi). In some senses this is hardly surprising, indeed it is perhaps only natural for employees to believe that they would get a more favourable assessment from a manager they get on with. Nevertheless, if employees feel that there is bias in the performance assessment process that may affect their belief in the procedural equity of the PRP scheme, and so militate against the motivational effect of PRP. There is also a danger that, if there is a tendency to reward compliance and the ability to fit in, this will damage organisational innovation. Some commentators (Demming 1982, Kanter 1989, Kohn 1993 and Pfeffer 1998) have argued that PRP is innately damaging to the dynamics of an organisation, precisely because it fosters conservatism amongst employees, by rewarding compliance with predetermined criteria and the achievement of set targets; as opposed to initiative, innovation, and risk taking.

Even if the employee believes that their own manager would give them a fair assessment, there is always the danger that the employee will feel that the scheme is being manipulated by more senior managers, in such a way that the employee will not get a fair assessment. There is evidence in some schemes (e.g. the Revenue Scheme, Marsden & Richardson 1991 and Marsden & French 1998) of a perception that the employer is operating a quota system whereby only a certain proportion of employees are allowed to be placed in each performance rating category. Obviously from the employees' point of view the danger is that they are denied the assessment that they deserve either, because of a decision by a more senior manager or, because of the operation of a quota system. A majority, 55% of respondents thought that there was a problem with good assessments being overturned by more senior managers (Appendix C.fxiii). Only 15% of respondents thought that this was not a problem. According to the survey 59% of respondents thought that their own performance assessment had been fair, so it follows that quite a number of the employees who thought that their assessment was fair, nevertheless felt that the scheme was flawed because a fair assessment could be overruled. From the point of view of procedural equity its possible that even employees who thought that their own assessment was fair, may have felt demotivated by their concerns about the PRP scheme generally. There appears to have been little foundation for these concerns about a quota system or arbitrary intervention by

more senior managers. This concern may be symptomatic of employees' low trust in the management.

The Thames Water PRP scheme requires assessors to get their assessment countersigned by their manager, personnel then record that assessment centrally (Chapter 6). Once the records of PRP assessments have been collated centrally the resulting data is looked at to see if there is a normal distribution of assessments, that is to say a bell shaped distribution. In practice Thames Water expect the distribution of assessments to be skewed to the right with a tendency for assessments to peak at 'very good'. The data is broken down according to gender and ethnic origin and then examined, to see whether there is any bias against any particular group. Any obvious anomalies, either in the way in which individual managers have scored the performance assessments, or in terms of bias against a particular group are then discussed with the manager concerned (*ibid.* Chapter 6).

In PRP schemes which use a quota system to ensure that the distribution of performance ratings conforms to a predetermined distribution, managers will be told in advance that a certain proportion of the workforce must be in each rating category. Consequently an employee's rating in a scheme with a quota system depends both upon the assessment of that employee's performance and the operation of the quota system. Thames Water does not operate a quota system and the

statistical analysis done by Thames Water after the assessments have been done is aimed at identifying either bias or anomaly in the performance assessments. In the Thames Water scheme it is acceptable for a manager's performance assessments to deviate from the slightly skewed normal distribution that Thames Water generally find with assessments, provided that those assessments can be justified. Nevertheless, a majority, 67%, of the respondents thought that there was a quota system being operated by Thames Water, which denied employees the performance rating that they were entitled to, while only 11% believed there was no such system (Appendix C.fxiv). Paradoxically, it may be that the very mechanisms used by Thames Water to ensure that the performance assessments are being carried out fairly by managers may be seen by employees as an interference in the fair operation of the PRP scheme. This suggests employees do not fully understand the operation of the Thames Water PRP scheme. However, when Thames' employees were asked (Prpunderstand f1) how well they understood the employer's performance related pay scheme, 73% said they either understood it very well or quite well, and only 21% saying they did not understand in part or at all. Even so, respondents may not have understood the scheme as well as they thought they did. Alternatively respondents' perceptions about the manager's assessment being overruled and the operation of a quota system may be indicative of a low level of trust. Employees may know about the operation of the mechanisms used to ensure fairness in the assessments, but nevertheless

believe that in reality the scheme operates unfairly with managers' assessments being arbitrarily overruled and a quota being applied to the assessments. The survey results suggest that Thames Water would be well advised to try to ensure that employees are aware of the mechanisms that are used to avoid bias and anomalies, and see these mechanisms as distinct from any arbitrary interference in the fair operation of the assessment process. One way of achieving this sort of transparency would be to involve the trade unions more in the monitoring of the PRP scheme.

Finally it is clear that respondents were also concerned about the basic fairness of the link between effort and reward in the Thames Water PRP scheme. This has already been touched on in relation to the respondents' answers to the questions about the link between pay and performance, which showed that at best only 20% thought that they could increase the amount that they earned by working harder. It seems likely that respondents' scepticism about the link between performance and pay reflects some of the process issues identified above. However, there is also evidence from the answers given to the open question in the Questionnaire that there is confusion and resentment amongst employees over the operation of the Thames Water PRP system.

Respondents expressed resentment at the way in which performance pay reflected not only the employee's performance, but also their position on

the pay matrix for their grade. The pay matrix was intended to bring employees to their so-called 'natural level' on the pay scale. This 'natural level' was meant to reflect the level on the scale that corresponded to the employee's performance, so that a fully competent performer would have a higher 'natural level' than a less competent performer. Essentially movement to these 'natural levels' was achieved by determining the level of increase an employee received by reference to both their performance rating and their position on the pay matrix (Chapter 6). This meant that two employees who receive the same performance rating could get different levels of increase by virtue of being at different points on the pay matrix, and that the employee with the higher rating could get a lower increase if they were higher up the pay matrix. This was because the level of increase reduces for all levels of performance rating the higher the employee is up the pay matrix. The system was further complicated because initial assimilation onto the pay matrix depended in part on the employees previous grade, before the new pay and grading structure, which included a job evaluation scheme, was introduced. A number of respondents commented on the perceived unfairness of the system from their point of view: e.g.

'If a person was over salary scale when PRP commenced there is no way, no matter how hard you work or how dedicated your performance is, that you get anything other than the PRP %. This is soul destroying when you find that another person... because they are lower down on the scale, in fact receives a higher % overall.'

and

'Having achieved 'very good' and 'excellent' my PRP was limited to my position on the scale and this proved a disincentive...'

From the comments received it would seem respondents to the survey may have been negatively influenced in their perceptions about the link between targets and future pay increases by the use of the pay matrix.

This would suggest that the link between pay and performance is likely to be more readily understood by employees when the pay matrix is not used to determine the level of pay for performance.

In 1998 Thames Water stopped using progression through the pay matrix to determine the level of pay increase employees will receive for any particular PRP assessment. Instead, all employees who achieve a particular level of performance got the level of pay increase for that performance level until they reach the top of the scale; this change may have helped clarify the link between performance and pay for employees.

### Distributive Equity

Respondents also expressed concern about the amount of pay they received compared to other employees. In theory PRP should ameliorate some of the equity problems caused by an incremental or rate for the job

pay system. Where workers are paid the same for doing the same job, there is a danger that, if they believe they are working harder than other workers who are paid the same, they will resent the difference and reduce their effort (Adams 1963). PRP gets around this by relating reward to individual effort, so that at any particular level of skill and responsibility, a worker's individual effort will be rewarded by a performance payment that reflects that effort. However, the results of the survey of Thames Water employees in receipt of PRP suggest in practice Thames' employees had a rather different perception of the impact of PRP.

For PRP to be fairer than schemes that are based on the rate for the job or incremental progression there needs to be a direct relationship between effort and reward. Yet most employees believed that the Thames PRP system did not fairly reward hard work. Over 80% of respondents believed that their employer did not adequately reward hard work (Appendix C.f xv).

Adams' equity theory (1963) predicts that it is an individual's sense of the comparative merits of the reward they are receiving which will determine its motivational effectiveness. It is unclear from the literature who any given individual will choose as their comparators. For the purposes of this study it has been assumed that the natural comparator for Thames Water employees in receipt of PRP will be other Thames Water

employees in receipt of PRP. The survey asked employees whether they felt other colleagues or other parts of the organisation did better out of PRP than they did. Most respondents were uncertain whether it was easier to get a higher performance rating in other parts of the organisation. Most 55% were not sure, 37% thought that it was easier to get a better assessment elsewhere in the organisation, and only 8% disagreed with the proposition that it was easier to get a better assessment elsewhere (Appendix C.fxvi). There was a more even division amongst respondents about whether they did as well as their colleagues out of PRP (Appendix C.fxvi). On balance respondents were more likely to feel that their colleagues did better out of PRP than they did, with 39% saying they either agreed or strongly agreed that others did better out of PRP than they did. Just over a third, 35% said that they were not sure. And 26% did not believe that they did worse than their colleagues out of PRP. The overall picture that emerges is one in which there is a substantial amount of uncertainty among respondents about the distributive equity of the Thames Water PRP scheme. Just over a third of respondents thought that they were not being fairly rewarded for their work in comparison to what others were getting.

The results show that while a majority, 67% (Fairgen a1), of Thames Water employees felt that PRP generally was a fair way of paying workers, a substantial number of them, between a third and two thirds, did not believe that the Thames Water PRP scheme was fair. Either

because they believed the scheme was being applied unfairly by managers who did not understand their work sufficiently and whose assessment was, in any event, likely to be overturned. Or because they believed that they received less performance pay than others for comparable work. Overall only 11% of respondents thought that they had been paid more fairly as a result of the introduction of PRP, whereas 72% thought that they had not been paid more fairly as a result of the introduction of PRP (Fairme h6). It seems that whilst Thames Water employees were largely objectively well disposed towards PRP as a fair payment system, their subjective experience of the Thames Water PRP scheme led them to believe that its introduction had not led to most of them being paid more fairly.

The problems over fairness have a double impact. First of all it is clear from the Company's own guidance notes for employees (Chapter 7) that Thames Water introduced PRP in the belief that it was a fairer way of paying employees. Indeed fairness is quoted in the literature that is supportive of PRP as one of the benefits of PRP (Armstrong and Murlis 1994). In practice the impact of PRP in Thames Water has done the converse of what was intended with most employees believing that it has not increased fairness.

There is also a danger that employee perceptions about the unfairness of the Thames Water PRP scheme will serve to demotivate employees. If

the scheme is seen as being operated unfairly, then that will detract from employees' belief in its instrumentality in producing a valent outcome, and so employees will not develop expectancy that additional effort will produce a performance payment. The lack of procedural equity will also tend to demotivate employees (Greenberg 1987). Logically the lack of procedural equity is also likely to impact on distributive equity. If the system is flawed by lack of fairness it seems likely that the outcomes from that system will also be thought to be unfair. In any event the survey results show that a substantial number of employees felt that other Thames Water employees were being better rewarded than they were. Equity theory predicts that in these circumstances employees are likely to reduce their effort in order to ensure an equitable balance between their effort reward relationship and that of others. So it can be seen that inequity in the PRP system is likely to have a demotivating effect, from a number of theoretical perspectives.

Thames Water might be well advised to try and address the equity concerns highlighted by the survey. The Thames Water PRP scheme was specifically introduced with the declared intention of increasing fairness (Chapter 7). A review of the scheme and its operation focusing on the fairness of the scheme would therefore be consistent with the declared objective for the scheme. It would also have the advantage of re-emphasising the fairness aspects of the PRP scheme. The point was made in the previous Chapter, that there is always a danger that the

apparently limited benefits of PRP might in practice be outweighed by its disbenefits. In crude terms, if more employees are demotivated by PRP than are motivated by PRP, it could be said that overall PRP is having a negative effect on motivation.

### Feedback.

One of the principal reasons for introducing PRP to Thames Water was to ensure that managers talked to staff about their performance (ibid. Chapter 6). There was a concern that, to quote Steve Jay, the then Director of Personnel, managers were 'abdinating their responsibility for managing people'. PRP was intended, as the then Director of Personnel put it, to 'bring the linkage with employees and their performance right into the centre of the stage'. Clearly feedback from managers to the employees they were responsible for managing was an important part of the PRP scheme in Thames Water.

The Thames Water PRP scheme is based on targets set at the SPR, the SPR in turn should be used to give the employee feedback on performance (Chapter 7). Each employee is intended to receive at least one SPR a year, if not more. In one sense, the ultimate feedback in any PRP scheme is the performance assessment on which the performance payment is based. However, the survey results suggest that over a fifth of respondents did not get even this feedback from their manager, as

22% of respondents claimed not to have had an SPR interview in the last twelve months (c1 Numberspr).

When asked whether their manager was good at giving them feedback, only 38% of respondents disagreed (e1 Feedbackquality). About 47% thought that their manager was bad at giving them feedback. However, there is always the danger that a survey of employees will produce a distorted view of the process based on the subjective experience of the interview. An employee could for example take the view that a manager was bad at giving feedback, because the employee did not agree with their manager's assessment of their performance. Objectively, whether a manager is good at giving feedback or not seems likely to depend on two things, first of all the frequency, and secondly the quality of that feedback.

The frequency of feedback is important, because it gives the recipient of the feedback the opportunity to modify their performance in the light of that feedback. It should also be a more objective test in a survey than questions about the quality of the feedback received because the answer is less likely to be open to individual interpretation. The evidence from the survey suggests that managers were not particularly good at giving employees frequent feedback. The formal feedback process was determined by the number of SPR interviews employees had, and while 22% said that they had not had an SPR interview in the last twelve

months, only 16% reported having two or more SPR interviews in the same period (c1 Numbersprs).

As the comments by the Director of Personnel indicate, Thames Water were clearly hoping to build a culture in which the relationship between manager and managed focused on work performance. For this to happen, performance had to become something more than an issue that was discussed once a year at the SPR interview, it needed to be a key issue on which the employee received frequent feedback about their progress. In addition to the formal feedback given during the SPR interview, managers gave employees informal feedback. When asked how many times they had received informal feedback during the last year, 39% of respondents said they had not received any, 10% said they had it once, 16% twice, and 27% said that they had been given informal feedback on three or more occasions. Respondents were also asked whether they agreed that:

'You receive frequent informal feedback from your manager regarding your progress towards the Objectives set for you at your Staff Performance Review.'

About a quarter of respondents thought that they did get frequent informal feedback and this roughly corresponds with the number who said that they had been given feedback on three or more occasions (Appendix C.fxvii).

The overall picture that emerges is that only 16% of respondents had

more than one opportunity for formal feedback during the course of the last twelve months, while 25% agreed that they had received frequent informal feedback. In terms of the frequency of the feedback being given the PRP scheme appears to have failed to place the linkage between performance and people at 'the centre of the stage' for more than a quarter of Thames Water employees.

In terms of the quality of the feedback received, respondents were asked whether or not the feedback they had received had been encouraging or not. Over half, 54%, reported that it had been encouraging, with only 18% saying that it had not been encouraging (Feedbackencouraging e3). If recipients of the feedback think that it is encouraging, then that suggests that the feedback is playing a positive role. This would seem to be the most useful indication of the quality of feedback from a survey of the views of those receiving the feedback. So that while feedback was not given frequently enough, when it was given, it appears that in just over half the cases it was good in that it was felt to be encouraging.

Two further questions dealt with employees' views about the importance of feedback: the answers suggest that feedback was important to employees and reinforce the importance of feedback to the operation of the Thames Water PRP scheme. A substantial majority of employees found feedback useful both in terms of increasing their sense of achievement (Appendix C.fxix) and more directly in helping them to

achieve their objectives (Appendix C.fxx). The two questions are in a sense complementary, as feelings of achievement may increase performance and therefore help employees to achieve the targets set for them.

Increased feelings of achievement may help increase performance and therefore the ability to achieve goals, by increasing the individual's feelings of self-efficacy (Bandura 1986). As the individual's self confidence grows through increased feelings of achievement, so it is argued their performance will improve, both, because individuals will then set and accept higher targets for themselves, and because the individual's performance will be improved by their belief in their ability to achieve their goal. In addition, increased feelings of achievement should increase the effectiveness of goal setting as a motivational technique, as self-efficacy is said to mediates the relationship between assigned goals and performance (Early and Lituchy 1991).

A larger majority of respondents, 81%, thought that feedback would help them to achieve the objectives set for them. In a sense this seems self-evident. Feedback to employees about their performance ought to assist them achieve their objectives by identifying what, if any, corrective action they need to take in order to achieve those objectives. Nevertheless, it is helpful to look at the literature and then consider some of the practical arguments around feedback, as these reinforce the importance given to

feedback by both respondents to the survey and Thames Water.

The literature on goal setting in particular supports the importance of feedback. In a field study conducted with units of the United States Air Force, Pritchard et al. (1988) found that feedback increased productivity by 50%, before either goals were set or incentives offered for the achievement of those goals. Feedback has been found to increase the effectiveness of goal setting as a motivator (Hall & Foster 1977, and Tubbs 1986). The literature on expectancy is less explicit about the role of feedback. Porter and Lawler (1968) proposed a model of expectancy, which included a feedback loop, however feedback in this model was a consequence of the individuals' previous experience of the expectancy cycle, rather than a consequence of information being provided by a third party.

Clearly one of the critical considerations is the individual's own performance. This may be self-evident, or it may be more difficult for the individual to evaluate their performance because of the nature of the goal that has been set. Some goals may be clear-cut from the outset, such as a particular level of production. Others, such as the way in which work is carried out are likely to be more difficult for the individual to assess. PRP schemes tend to focus on worker inputs, and the Thames Water scheme brings into assessment the way in which work is performed, what is termed behavioural traits for four out of the six or seven criteria against

which employees are assessed. Thus from a practical point of view feedback from the manager may be the best way for an employee to know how their performance measures up against the criteria for a performance payment.

Thames Water introduced PRP in part to focus managers on the central importance of performance, to do this effectively managers need to give their employees feedback. It turns out from the survey that employees also feel that feedback is important both for their feelings of achievement and to help them achieve their job objectives. Yet the survey results show that only a quarter of employees felt they were getting frequent informal feedback about their progress towards the objectives set at their SPR. In those cases where feedback was given most of it appears to have been encouraging. Overall the results of the survey suggest that there is a lack of trust in the relationship between employees and their managers, which PRP seems to have contributed towards, and which has detracted from the effectiveness of PRP as a motivator. At the same time the results of the survey highlight the benefit employees feel that they get from frequent and encouraging feedback.

### Cultural Change

The introduction of PRP formed part of a larger programme of cultural change within Thames Water, called the Employee Project. Thames

Water wanted to change their culture from what they perceived to be a public sector type culture, inherited from the time when the water industry was publicly owned, to a more commercially focused culture. The Director of Personnel characterised this process as trying to get employees, particularly managers, to think about and accept responsibility for the performance of the organisation (Chapter 7).

The literature on changing organisational culture was examined in Chapter 5. Essentially cultural change involves changing the employees' beliefs and values so that they will use different beliefs and values to guide their behaviour. Clearly, from the organisation's point of view, the aim is to get the employee to adopt a belief and value system that more closely corresponds with the organisation's own beliefs and values, so that the individual will intuitively act in the interests of the organisation (Denison 1990). If the employees' beliefs and values are aligned with those of the organisation this should have the effect of reducing transaction costs and improving performance. Employees are more likely to align their beliefs and values to those of an organisation that they identify with, and both Denison (1990) and Brown (1995) have identified commitment as a key element in achieving a change in corporate culture. Thus the process can be seen as one in which the organisation sets new cues for employee behaviour, which should have the effect of increasing employee commitment, so that employees adopts a belief and value system more closely aligned to that of the firm.

Pay systems are widely seen as an important cue or lever for achieving cultural change (Drennan 1992). Indeed, Kessler (1994) has suggested that one of the principal reasons why firms use PRP is because PRP is perceived to be a mechanism for getting an organisation's culture to change. Thames Water believed that PRP would play an important role in changing culture within the organisation (Chapter 7).

It is difficult to know how far the programme of cultural change in Thames Water has succeeded or indeed how much of any cultural change can be attributed to PRP. The survey questionnaire contained a number of questions concerned with employees' perceptions of change over the period since the introduction of the Employee Project. Overall most respondents felt that communications between management and workforce had not improved (Appendix B.fxiii & fxiv) and that employees were no more likely to identify with the firm (Appendix B.fxv & fxvi), since the introduction of the Employee Project. About the same number of respondents (40%) reported an increase in employees' confidence about accepting changes in working practices, as said that there had been no increase. About a quarter of respondents said that there was greater identification with the core values of Thames Water. But most significantly nearly 80% of respondents said that feeling of 'them' and 'us' remained unchanged. And just over 70% of respondents rejected the idea that employees were being treated more like individuals than

they had been in the past(Appendix B.fvii).

From the Company's point of view, the fact that a proportion of employees reported what the Company would see as positive changes in attitude since the Employee Project can be seen as indicative of changes in employees' beliefs and values. At the very least it shows that some employees believe that attitudes are changing. There is the prospect that even those respondents who report no change in attitude in response to the survey may change their view over time. The survey was conducted about two and a half years after the introduction of PRP in Thames Water. It may take time for the programme of cultural change to be effective. Fundamental values and beliefs that have developed over a long period will take some time to change. From the Company's perspective at least some employees are reporting changes in attitude over important issues like flexibility over working practices. But the data should also give the Company cause for concern. A substantial number of respondents see the employment relationship as one of 'them and us' and nearly as many detect no move by the organisation to treat employees as individuals. These results suggest a degree of alienation at a time when the Company is trying to increase employee identification with the Company.

It is also crucial to consider the issue of causation in terms of the changes that have taken place. In other words, have the changes in

employee values been brought about by the programme of cultural change introduced by Thames Water, or are they the result of other factors such as changes in society generally or other changes in the way in which Thames Water operates. And more specifically, what role has PRP played in changing organisational culture within Thames Water. Using the framework for understanding the process of cultural change described in Chapter 5, it can be seen that an effective programme of cultural change uses cues which lead the employee to adopt values and beliefs that are aligned with those of the organisation they work for. Consequently it has been hypothesised that where those cues have been effective in changing employees values and beliefs there should be increased commitment to the employer. In other words the product of an effective programme of cultural change should be increased commitment to the employer.

The evidence from the survey is that Thames Water employees were generally committed to their employer. A standard commitment questionnaire (Cook & Wall 1980) has been used in the survey to measure employee commitment. This comprises nine questions, each of which can be seen to fall into one of three categories (Cook & Wall 1980 and Peccei & Guest 1993). The first is made up of three questions dealing with the respondents' pride in and identification with Thames Water. A summary of the results is set out in Appendix C. fxxi - fxxiii.

It can be seen that between 55% and 67% of respondents identified with Thames Water, either in terms of the way they felt about the organisation or their pride in the organisation, while at most only 34% said they did not identify with the employer.

The second category concerns respondents' intention to stay with the employer or loyalty, a summary of the results are set out in Appendix C. fxxiv-fxxvi. Over half of respondents said that they sometimes felt like leaving Thames Water. Surprisingly rather less, only 47%, said that they would leave for the offer of a bit more money. Similarly the financial well being of Thames Water seemed to have relatively less bearing (36%) on respondents' views about whether or not they would stay with Thames Water. There were a number who said that they had thought about leaving, who did not identify money as influencing their views about whether or not they would stay with Thames Water.

Finally respondents were asked about their willingness to make an effort for the organisation or put another way their feelings of involvement (Appendix C. fxxvii-fxxix). A large number indicated they were keen to make a contribution to the success of the organisation. Some 77% said that they were prepared to put themselves out for the benefit of the organisation. Over 90% saw their work as being for the good of the organisation and not just their own benefit.

So broadly speaking it could be said that while a majority of respondents

had thought about leaving Thames Water, most of them identified with Thames Water, and the overwhelming majority said that they were prepared to put themselves out for the benefit of the organisation.

The differing levels of commitment identified in relation to the three elements in Cook and Wall's commitment questionnaire may reflect commitment to different aspects of the organisation. Organisations of the size of Thames Water are complex bodies comprising many different parts. Employees may distinguish between those different parts in their commitment to the organisation. For example employees may be distinguishing in their answers between Thames Water as a commercial entity and Thames Water as a supplier of essential services.

The service delivered by Thames Water Utilities is essential for public well being both in the delivery of fresh water and the treatment of wastewater. This may explain why respondents felt that they would be willing to put themselves out for the benefit of the organisation. In effect what they may have been saying is that they were prepared to put themselves out to deliver an essential public service, either out of some feeling of altruism or public duty. Anecdotally many Thames Water employees are seen as having a strong public service ethos. Many of the respondents had joined Thames Water when it was a public sector organisation. Intention to stay may in part be a reflection of the ethos of public service amongst employees. Julia Cherrett, the European Director

of Human Resources for Thames Water has said:

'Many of our employees are proud to be working in an essential service and I have no doubt that explains some of their commitment to Thames Water.'

Feelings about the company and the commitment to stay with company may reflect more ambivalence in the attitude of respondents towards Thames Water an employer, than in their attitude to Thames Water as the provider of an essential public service. However, from the company's point of view it could be argued that it is employees' commitment to the firm as a commercial entity that is essential to the transition from a nationalised industry to a private company. The commitment to the service exists because of the nature of the service that is provided; that is to say because it is an essential service to the public. Getting employees and managers to think about and accept responsibility for the performance of the organisation means getting the employee to identify with the organisation as a commercial entity and not just the service that the organisation provides.

These results raise interesting questions about the concept of organisational commitment, such as commitment to who and to what (Swales 2002), which go beyond the scope of this thesis. There is also some debate about how far increased commitment contributes to improved organisational performance. Gallie, Felstead & Green (2001) found in two surveys of commitment amongst British employees that the impact of policies associated with increasing employee commitment was

variable. It has been suggested that the lack of consistent evidence about a link between commitment and improved organisational performance may reflect problems over measurement (Swales 2002). The argument in this thesis is that increased commitment increases performance by reducing internal transactional costs and increasing intrinsic motivation (Brown 1995). The extent to which PRP in particular has helped to increase employees' commitment to Thames Water is examined in the next Chapter.

### Conclusion

The survey identified serious gaps in the operation of the PRP scheme in Thames Water. About a fifth of respondents reported that they had not had an SPR in the last twelve months. This means that those respondents were getting no formal feedback on their performance and that any targets that they were working to achieve could be out of date. A similar number of respondents doubted that they had the skills and ability necessary to achieve the targets they had been set. These are serious process issues, which may go some way to explain the scepticism of respondents about the link between performance and pay.

Around 80% of those surveyed believed that they could not increase their pay by working harder. Respondents were generally more likely to associate intrinsic rewards and other non-pay rewards with goal

achievement than they were monetary rewards. The problem appears to be a lack of trust in the system and the way it is operated. Many employees believed that their assessment was liable to be altered by someone other than their manager, or that it was possible to do better in other parts of the organisation, or that there was some sort of quota system in operation. These concerns go to the instrumentality and fairness of the Thames Water PRP scheme and may help to explain its lack of motivational effectiveness for a large part of the workforce.

Thames Water also wanted to use PRP as an engine of cultural change. It has been argued in this thesis that in order for PRP to be effective as an engine of cultural change it needed to increase employee commitment. The survey showed that the majority of employees identified with the company and many were prepared to put in additional effort on the company's behalf. It is however unclear how far that commitment is as a result of PRP or whether it reflects other factors such as for instance the public service ethic that employees may feel in providing such vital services to the public.

## Chapter 10

### **The motivational effects of PRP explained?**

#### Introduction

The two preceding chapters took a first look at the data from the Thames Water Survey in terms of both the outcomes from Thames Water's point of view and to see how far the data is consistent with the theoretical models of motivation identified in this thesis. However, the individual items from the survey do not capture some of the more complex psychological concepts relevant to an understanding of human behaviour (Bryman and Cramer 1990); further, some of the constructs in the theories being considered in this thesis are themselves not readily reduced to a single item in a questionnaire. Using principal component factor analysis it is possible to identify variables comprising items in the survey that are measuring the same underlying construct. Regression analysis using those variables identified from a factor analysis of the items in the survey gives a view of how far each of the theories identified in this thesis helps to explain the variance in motivation brought about by the Thames Water PRP scheme. This in turn highlights those elements of the PRP scheme that are most important in terms of the motivational effectiveness of the scheme.

## Factor Analysis and Scale Reliability

Principal Component analysis is a statistical technique, sometimes used to reduce items into a smaller set of variables by identifying through their correlation with each other those items which when taken together represent underlying constructs. Each of the items measured using continuous data in the questionnaire has been coded so that scores on reverse questions, that is questions which ask respondents their views on both positive and negative statements on the same issue, run in the same direction to ensure consistency of measurement. All of the continuous data from the survey, excluding biographical data, has been factor analyzed and the factors generated by that analysis have been used to represent the variables described below. Questions in the survey conducted for this thesis were grouped into Sections, which reflected specific aspects of employee experience of and attitudes to the PRP scheme and its outcomes. Factor analysis was applied to the data on both a sectional and global basis, that is to say each section was factor analyzed as well as the totality of the data, excluding biographical data. There was a consistency in the results from these two approaches to factor analysis. The results of the global factor analysis have been used to identify variables, because those results are based on a more rigorous process which captures items from the whole survey.

Scales created using factor analyses have been tested for scale reliability using Cronbach's  $\alpha$ . The conventional 'rule of thumb' is that  $\alpha > .7$  (Leary 1995), in order to be confident that the scale is reliable. However, Cronbach's  $\alpha$  can be shown as:

$$\alpha = \frac{kr}{1 + (k-1)r}$$

Where  $k$  is the number of items in the scale,  $\alpha$  is the average correlation between the items, where the items are standardized. It can be seen that  $\alpha$  is a function of both the number of items and their inter-correlation, consequently the  $\alpha$  score is sensitive to the numbers of items in the scale. It has been suggested that while the aim should be to achieve an  $\alpha$  level  $\geq .7$ , there is a hierarchy of confidence in scale reliability and that a reliability of  $\alpha \geq .6$  can at least be viewed as questionable (George & Mallery 1995). For this research the aim has been to get scale reliability of  $\alpha \geq .7$ , but given the trade off between the number of items comprised in the scale and the  $\alpha$  score, where a relatively small number of items have been used to construct a scale, a scale reliability of  $\alpha \geq .6$  has been taken as the threshold.

## MOTIVATION

PRP is concerned with performance, that is to say that PRP makes pay dependent on performance. It is evident both from the

literature (Cannell & Wood 1992 and Kessler 2000) and from the Thames Water case study that employers may introduce PRP for a number of different reasons, not all of them directly related to performance. Nevertheless the performance outcomes of PRP are important. But performance is a difficult measure to use in terms of understanding the success or otherwise of a PRP scheme. First of all, objective measures of performance are not readily available in a field trial setting. Secondly, variables outside the employee's control may affect performance. Some of these variables may relate to the employee, for example the employee may not have the skills or ability to achieve the targets that have been set. Other variables may be beyond the employee's control, for example the targets that are set may be unrealistic or the performance of other workers involved in the process may adversely affect the employee's ability to achieve the targets set. An alternative approach would be to look at the subjective measure of performance used by the employer, that is to say, the performance assessment. Without a control group against which to compare the performance assessments it is unclear what this would tell you about the success of the PRP scheme. Employees who perform well and are appraised as good performers might have performed equally well without PRP.

A critical measure for the employer is the additional effort that the employee has put into his or her work as a result of the PRP scheme, because that is likely to be an indication of the additional benefit the employer gains from PRP. In this thesis that additional effort has been referred to as motivation. If PRP increases employee motivation, then all other things being equal, such as skill, ability and work organisation, the employer should be getting more performance out of their employees. Factor analysis of the data set identifies a factor which loads seven items all concerned with the employees views about the motivational effect of PRP (see Appendix D) a variable MOTIVATION. This factor loads on those items that measure the respondents' perceptions about the motivational effects of PRP on them and on their colleagues at work. Including a question about the motivational impact of PRP on other employees should make the measure more robust. There is a danger that simply asking employees about their own level of motivation may give a distorted view as they may be reluctant to attribute motivation to something outside their own control (Crozier 1964), so the questionnaire included an item reflecting respondents' perceptions about other workers motivation. The variable MOTIVATION is the key dependent variable in this study, because it gives a measure of the motivational effectiveness of PRP.

However it is important to bear in mind when considering the analysis that follows that very few of the respondents to the

Thames Water survey reported being positively motivated by the PRP scheme; at best, in response to specific questions it was only 18%. Consequently MOTIVATION is measuring a largely neutral, or even negative, response to a set of questions that capture the underlying concept of PRP as a motivator; indeed, only 15% of the scores in the variable MOTIVATION are positive. Each of the theories of motivation identified suggests a group of independent variables, which according to the theories will have a causal effect on MOTIVATION.

### Expectancy Theory

In its simplest terms expectancy theory predicts that motivation is the product of valence, instrumentality and expectancy. Thus the three key variables are valence, instrumentality and expectancy, although Porter and Lawler (1968) have proposed a more complex model involving feedback and equity. The first arm of the expectancy equation is valence that is value of the outcome to the employee. Instrumentality is the belief that if given targets are met this will lead to a valent outcome. PRP schemes are predicated on performance being instrumental in producing a performance payment, which it is assumed the employee will view as a valent outcome. PRP schemes do this by making pay contingent on performance. The performance payment is the explicit valent outcome. But there are clearly other outcomes, some of which may be longer term

in their nature, that may be of benefit and value to the employee such as promotion, job security or simply satisfaction at having achieved the targets that have been set. The difficulty is predicting the benefit to the individual of any given outcome. In the Thames Water scheme, the level of the increase in salary associated with any particular level of performance is determined at the end of the year and consequently cannot be predicted precisely by the employee while they are working to achieve the targets to which the salary increase will relate. This makes it difficult to specify valence other than in terms of an outcome, which would appear to be beneficial. The question then for the purposes of expectancy theory is, does the employee believe that achieving the targets he or she has been set will lead to a valent outcome, whether in terms of a performance payment or some other beneficial outcomes.

Ideally, one would want to identify the three separate variables, specified in expectancy theory, namely valence, instrumentality and expectancy. Unfortunately, factor analysis of the data did not provide a neat three variable solution. Analysis identified one variable INSTRVAL which loaded on three items each of which identifies a connection between achieving the goals that have been set and an outcome that is likely to be of value to the employee, in effect this gives a measure of both valence and instrumentality of the PRP process (see Appendix D). In addition to measuring instrumentality, INSTRVAL also provides some measure of the valence of the outcome because it comprises items measuring three

positive outcomes for employees and the extent to which those outcomes are seen as connected to the PRP process is also therefore a measure of valence.

Expectancy is the employee's expectation that increased effort on his or her part will lead to a valent outcome. Expectancy differs from instrumentality, which is concerned with the belief that there is a causal link between target achievement and a valent outcome. Expectancy is concerned with the individual's belief that they can get the outcome that they want by improving their performance and factor analysis discriminates two items reflecting this belief (Appendix D) which has been used to identify a variable, EXPECTANCY. The two items used to construct the variable EXPECTANCY specifically relate to the employee's belief that by improving their performance they can get a performance payment.

Multiple regression (Table 10.i) shows that the independent variables INSTRVAL and EXPECTANCY are both positively associated with the dependent variable MOTIVATION (R .36) and that 13% of the variance in MOTIVATION is explained by the variance in INSTRVAL and EXPECTANCY. The Beta scores suggests that INSTRVAL is the more powerful explanatory variable, as the Beta scores demonstrate that a change of one standard deviation in INSTRVAL produces a change of .32

standard deviations in MOTIVATION, compared to a change of .11 standard deviations resulting from a similar change in EXPECTANCY.

<b>TABLE 10.i – Regression/Expectancy 1</b>			
Dependent Variable MOTIVATION			
Multiple R	.36	VARIABLE	BETA
R Square	.13	INSTRVAL	.32
Adjusted R Square	.13	EXPECTANCY	.11
Standard Error	.72	(constant)	.0000
F =	34.95	Signif F =	.0000

Regressing the independent variables INSTRVAL and EXPECTANCY, which represent the three elements of expectancy theory, with the dependent variable MOTIVATION shows a significant association that is consistent with expectancy theory, which predicts that individuals will be motivated by valence, instrumentality and expectancy. Moreover the association between the variables INSTRVAL, EXPECTANCY and MOTIVATION supports the second hypothesis being tested:

Hypothesis 2(a)(I)

*'Individual employee motivation will tend to increase as a result of PRP, where the employee has an expectancy that improved performance will be instrumental in leading to a valent outcome.'*

However, the important point to bear in mind when looking at the figures is that in the majority of cases employees were not motivated by PRP. The figures from the survey show that only 15% of the scores in respect of MOTIVATION related to a positive willingness to work harder as a result of PRP. The mean score for MOTIVATION is 2.22 (S.D. .77) on a Likert scale of five points, where five represents the greatest level of

motivation and one the lowest. Consequently the regression analysis is largely a measure of how far expectancy theory can help to explain the ineffectiveness of this PRP scheme as a motivator. Nevertheless, overall the results support the hypothesis by showing that it is the variance in valence instrumentality and expectancy that explains the variance in motivation, and that valence and instrumentality explain more of that variance than expectancy.

Porter and Lawler (1968) have suggested a more complex model of expectancy theory in which feedback and equity are relevant. Taking this in stages it is possible to look at the additive power of these other variables, so looking at equity:

Hypothesis 2(a)(ii).

*'The explanatory powers of expectancy theory in respect of the motivational effectiveness of PRP will be improved by factoring in Equity considerations'*

For the purposes of this hypothesis, equity can be seen as the fairness of the process in terms of the ways in which the system works, that is to say whether it is seen as being operated fairly by the employee's manager. Factor analysis reveals a variable which reflects process fairness in relation to the assessment, which will be termed FAIRA (Appendix D). The three items against which FAIRA loads are concerned with the employees' feelings about whether or not the employee's manager made a fair assessment of their performance, in other words

whether or not the procedure has been fairly applied.

Factor analysis identifies another variable termed INTERFEREA also concerned with procedural fairness. INTERFEREA combines three items related to employees' perceptions that PRP is subject to interference from others in the organisation, even if their own manager applies the scheme fairly (Appendix D). Adding these two variables to the regression analysis only increases the explanatory power of this model marginally (Table 10.ii).

<b>TABLE 10.ii – Regression/Expectancy 2</b>			
Dependent Variable MOTIVATION			
Multiple R	.39	VARIABLE	BETA
R Square	.15	INSTRVAL	.28
Adjusted R Square	.14	EXPECTANCY	.09
Standard Error	.71	FAIRA	.09
		INTERFEREA	.11
		(constant)	.0000
F =	20.84	Signif F =	.0000

It can be seen from the Beta scores in this regression analysis (Table 10.ii) that INSTRVAL remains the variable that explains more of the variance in MOTIVATION than any of the other independent variables in the expectancy model, even when equity considerations are factored in. On the face of it, adding in the additional equity considerations suggested by Porter and Lawler (1968) adds only a little to the explanatory power of the expectancy model.

However it is worth emphasizing that INSTRVAL includes both valence and instrumentality, and that instrumentality is the link between performance and a valent outcome. Thus INSTRVAL is a measure of both a specified valent outcome and connection between performance and that outcome. The link between performance and outcome is partly dependent on the fair application of the PRP scheme. If the scheme was being interfered with or applied arbitrarily then the employees are unlikely to see it as being instrumental in linking performance to outcome. Consequently INSTRVAL is in some senses a partial measure of the fairness of the scheme and this may explain why FAIRA and INTERFERA do not add a great deal to the expectancy model. It turns out that when the analysis is confined to procedural fairness these two independent variables on together explain some 7% of the variance in MOTIVATION (Table 10.viii) and there is a significant correlation between INSTRVAL and both FAIRA ( $r .28$ ) and INTERFERA ( $r .23$ ). In effect these elements of procedural fairness may already be accounted for in the measure of the instrumentality of the PRP scheme contained in the basic expectancy model.

Adding feedback variables, the other part of the Porter and Lawler (1968) model into the regression analysis does, however, make a greater difference to the explanatory power of the expectancy model. Factor analysis identified two feedback variables, which both measure different aspects of feedback. In the first one, GOODF (Appendix D), the three

items that comprise the variable reflect the respondents' perceptions about how good their manager has been at giving them feedback. The second one, POSITIVEF (Appendix D) comprises three items which represent the respondents' need for positive feedback. Both of these variables capture aspects of the feedback loop that Porter and Lawler (1968) argued would help to improve the effectiveness of the expectancy theory model.

**TABLE 10.iii – Regression/Expectancy 3**

Dependent Variable MOTIVATION			
Multiple R	.43	VARIABLE	BETA
R Square	.19	INSTRVAL	.21
Adjusted R Square	.18	EXPECTANCY	.09
Standard Error	.70	FAIRA	.03
		INTERFERERA	.10
		GOODF	.08
		POSITIVEF	.18
		(constant)	.1678
F =	17.88	Signif F =	.0000

Regression analysis using GOODF and POSITIVEF in addition to the other variables in the expectancy model explains 18% of the variance in MOTIVATION (Table 10.iii). It is worth repeating that MOTIVATION in the case of Thames Water is not for the most part a positive measure. These results support the third hypothesis about the relevance of expectancy theory to understanding the motivational effectiveness of PRP. Namely:

Hypothesis 2(a)(iii)

*'The explanatory powers of expectancy theory in respect of the motivational effectiveness of PRP will be improved by factoring in*

*feedback.'*

However the model itself could be more parsimonious. Removing variables from the model one step at a time selected on the basis that they add least in explanatory terms to the model produces a more parsimonious model. The first variable removed is FAIRA, which still leaves an expectancy model that explains 18% of the variance in MOTIVATION. Removing EXPECTANCY and INTERFEREA, reduces the explanatory power of the model by one per cent for each variable. This suggests a modified expectancy model comprising INSTRVAL, POSITIVEF and GOODF, and this explains 16% of the variance in MOTIVATION.

**TABLE 10.iv – Regression/Expectancy.4**

Dependent Variable MOTIVATION			
Multiple R	.42	VARIABLE	BETA
R Square	.18	INSTRVAL	.25
Adjusted R Square	.17	EXPECTANCY	.20
Standard Error	.70	POSITIVEF	.14
		GOODF	.18
		(constant)	.0020
F =	25.38	Signif F =	.0000

Overall it looks on the face of it as if feedback is a more important element in understanding the motivational effect of PRP in Thames Water than procedural fairness, possibly because procedural fairness is already captured by instrumentality. This suggests the formulation in Table 10.iv, which contains the three key elements of expectancy theory in the two variables INSTRVAL and EXPECTANCY, and the two feedback variables, and explains 17% of the variance in MOTIVATION.

## Goal Setting

Goal Setting theory predicts that individuals will work harder to achieve a specific achievable goal that they are committed to achieving than they would do otherwise, and that effort will be monotonically related to goal difficulty. The majority of goal setting studies appear to have been conducted in a laboratory setting; Locke and Latham (1990) reported that 239 studies had been conducted in the laboratory and 156 had been conducted in a field setting. Nevertheless the quantity of evidence available from both laboratory and field trials is higher than in the case of most psychological theories, and as Locke and Latham (1990, page 46) observe:

'Few if any theories in the fields of industrial-organizational psychology, human resource management, and organizational behavior, or even psychology as a whole, can claim such consistent and wide-ranging support.'

Goal setting theory is concerned with objective goal difficulty but this is difficult to measure in a field setting unless the tasks being measured are homogeneous and readily quantified. The alternative is to try to measure goal difficulty subjectively, as Locke and Latham (1990) say (page 75):

'Subjective difficulty typically correlates lower with performance than does objective difficulty. This may be because subjective goal difficulty is a confounded measure; it can reflect at least two different types of estimates: how hard the goal is objectively and the individual's self-efficacy.'

And (page 76)

'This caveat poses the most serious problem in correlational field studies in which goal difficulty is typically measured with a subjective question (a procedure that is necessary if multiple jobs are included in the sample).'

The Thames Water study posed precisely these challenges and it is important to bear these problems in mind when considering the results of the analysis for goal setting.

Factor analysis produces factors that load two items relating to goal difficulty and three items that relate to goal specification (Appendix D).

Factor analysis does not identify goal commitment as an underlying construct, although there is an item in the questionnaire dealing with goal commitment, but it does identify a measure of the respondents' belief in goal appropriateness based on three items. The three items have been used to create the variable RELEVANTG (Appendix D) which has been used as a proxy for goal commitment on the basis that the respondent's belief in the appropriateness of the goal is on the face of it likely to reflect goal commitment. DIFFICULTG and RELEVANTG both have a low scale reliability score ( $\alpha = .58$  and  $\alpha = .56$  respectively) and this is a further cause for caution in looking at the results of the analysis using goal setting. Only those cases where respondents reported having the skills and ability to perform the tasks set for them have been included in the goal setting model, because the objectives set must be achievable in order for goal setting theory to apply.

Goal setting explains less of the variance in MOTIVATION, than expectancy theory does, 5% compared to 18% (Table 10.v); this may be due in part to the difficulties over measurement. The relatively poor explanatory power of goal setting may have more to do with the problems over measuring goal difficulty and commitment than with the theory itself, which has a substantial body of research evidence to support it. Whilst goal setting theory poses an interesting model for understanding the motivational effectiveness of PRP, not least because it suggests a model in which the financial element of the process may be less important than the nature of the goal setting process and type of goal set, the results from this study need to be treated with caution. Indeed, it is difficult to be confident from the results of this analysis that goal-setting theory provides a robust explanation of the variance in MOTIVATION, given these difficulties. Consequently, the results of this survey do not give much support to the hypothesis that employee motivation will be directly related to goal difficulty.

**TABLE 10.v – Regression/Goal Setting**

Dependent Variable MOTIVATION			
	Multiple R	VARIABLE	BETA
R Square	.05	DIFFICULTG	.09
Adjusted R Square	.05	SPECIFICG	.17
Standard Error	.77	RELEVANTG	.08
		(constant)	.0002
F =		Signif F	
	7.14	=	.0001

### Hypothesis 2 (b)

*'In so far as goal setting theory explains the motivational effectiveness of a PRP scheme, individual employee motivation will be directly and positively related to goal difficulty for specific goals to which the employee is committed.'*

There is also a debate in the goal setting literature about whether goal complexity adversely affects motivation, because of the additional time, which is spent in strategy selection (Earley, Connolly & Ekeren 1989).

There is no continuous data in the data set concerning goal complexity. But respondents were asked about the number of objectives that they were set at their SPR and clearly the number of objectives set will have an impact on strategy selection. It turns out, the number of objectives set makes no difference to the explanatory power of the goal setting model. This may reflect the problems in operationalising the goal setting model or it may be that strategy selection does not adversely affect motivation in the Thames Water PRP scheme.

Some commentators (Kanfer and Ackerman 1989) have suggested that it is possible to reconcile expectancy theory and goal setting theory in one overall theory of motivation. Essentially it is argued that expectancy theory is both a distal and proximal determinant of resource allocation.

Goal setting is concerned with the proximal allocation of resources. Another way of looking at this is to say that expectancy theory determines both goal choice and commitment and goal effort. Goal

setting theory, on the other hand, predicts goal effort. If this model is correct and these are sequential elements in the motivational process then putting the elements of expectancy theory, EXPECTANCY and INSTRVAL in a regression analysis with DIFFICULTG and SPECIFICG, might be expected to explain either the same or more of variance in MOTIVATION than the models do on their own. If expectancy and goal setting theory are not sequential steps in the motivational process, by which PRP motivates employees; if instead they are measuring two different processes of motivation then their explanatory power seems more likely to be less than or the same as the aggregate explanatory power of the two models taken separately and indeed financial incentives may detract from the effectiveness of goal setting as a motivational technique (Lee, Locke & Phan 1997).

There is no need for a proxy for goal commitment in this model as expectancy determines goal commitment. In this thesis, it has been to argue that the two theories are distinct and that the effect will not be cumulative in this way.

#### Hypothesis 2 (c)

*'Goal setting and expectancy theory will not be cumulative in the extent to which they explain the motivational effectiveness of the Thames Water PRP scheme.'*

Analysis shows (Table 10.vi) that whilst adding DIFFICULTG and SPECIFICG increases the explanatory power of the basic expectancy

model, it does not have a cumulative effect. So in the combined model, expectancy theory and goal setting explain 17% of the variance in MOTIVATION, but expectancy theory and goal setting theory on their own explain 13% and 5% of the variance in MOTIVATION. Although these results tend to substantiate the hypothesis, all the caveats that applied to measuring expectancy and particularly goal difficulty apply to this aggregate analysis as well.

**TABLE 10.vi – Regression/Expectancy – Goal Setting**

Dependent Variable MOTIVATION			
Multiple R	.42	VARIABLE	BETA
R Square	.18	EXPECTANCY	.13
Adjusted R Square	.17	INSTRVAL	.32
Standard Error	.72	DIFFICULTG	.02
		SPECIFICG	.13
		(constant)	.0014
F=	20.07	Signif F	.0000

### Equity

Equity theory predicts that employees may adjust their contribution to ensure that the relationship between the effort they expend and the reward that they receive for that effort is comparable to others who they see as relevant comparators. Some commentators have argued that procedural equity or justice can be just as important in determining employee motivation (Greenberg 1987, Cropanzo & Floge 1991). Issues of fairness arise in relation to PRP both in respect of the comparative

rewards individual employees receive and in relation to the fairness of the mechanisms used to determine those rewards. Consequently both equity and procedural equity may be important issues in determining the motivational effectiveness of PRP from an expectancy theory perspective as well as from the perspective of equity theory.

The factor analysis did not identify a variable for distributive equity, nevertheless there is an item Comparison (f11) where respondents were asked, whether they agreed with the following statement:

'You do less well out of performance pay than some of your colleagues.'

The data from this item has been reverse scored and Comparison has been used as the independent variable in a regression analysis to test the explanatory power of Adams' (1965) distributive equity model in respect of the Thames Water PRP scheme. Regression analysis shows (Table 10.vii) that distributive equity as represented by the item Comparison explains only 2% of the variance in MOTIVATION.

The relatively poor explanatory power of the distributive equity model may, at least to some extent, reflect the problems of measuring distributive equity. These problems arise first of all in specifying the comparitor group (Dornstein 1988). In the Thames water survey employees were specifically asked about their colleagues. It may be that employees compare their effort reward ratio with say people in their social or family group, rather than with colleagues at work. The point is

that whilst it is appropriate to use work colleagues as comparitors for the purposes of equity theory in analysis of the motivational effectiveness of PRP, that may not be the group that employees are actually comparing themselves with. The second problem is that it would be preferable to have a variable constructed from a number of different items rather than just one item, as Oppenheim (p 143 1992) points out:

'An attitude precept or belief is, however, likely to be more *complex* and multi-faceted ..., and so it has to be approached from a number of different angles. There is no external way of *verifying* the answers and the questions and responses are generally much more *sensitive to bias* by wording, by response sets, by leading, by prestige and by contextual effects. For all these reasons, which have been confirmed many times by experimental findings, it is most unwise to rely on a single (or just a few) questions when dealing with non factual topics...'

Apart from the problems of measurement, there is one further quite fundamental problem with using equity theory to explain motivation. Equity theory (Adams 1965) simply predicts that where there is perceived to be an imbalance in the effort reward ratio between an individual and others in the comparitor group, the individual will seek to bring the ratios into balance. So for instance if someone else is being paid more, one way of balancing the effort reward ratio may be to do less work or to engage in cognitive dissonance. Equity theory does not predict what steps an individual will take to rectify an imbalance in effort reward ratios. Consequently the lack of a strong relationship between distributive equity and MOTIVATION, may simply reflect employees using other mechanisms to bring effort reward ratios into balance, such as reducing their effort, so that in effect PRP becomes de-motivating.

**TABLE 10.vii - Regression/Distributive Equity**

Dependent Variable MOTIVATION			
Multiple R	.15	VARIABLE	BETA
R Square	.02	F11 Comparison	.15
Adjusted R Square	.02	(constant)	.0000
Standard Error	.76		
F=		Signif F	
	10.96	=	.0010

Procedural equity, on the other hand, as represented by FAIRA and INTERFEREA, explains 7% of the variance in MOTIVATION (R .27)(Table 10.viii). Consequently, in the case of Thames Water the available data suggests that procedural equity is more important than distributive equity in explaining the variance in employee motivation resulting from PRP. This suggests that from the point of view of equity theory (Greenberg 1987, Cropanzo & Folger 1991) it is the way in which the PRP scheme is managed rather than the amount paid as a performance payment that is more important in influencing employees' attitudes, judgement and performance.

**TABLE 10.viii – Regression/Procedural Equity**

Dependent Variable MOTIVATION			
Multiple R	.27	VARIABLE	BETA
R Square	.07	FAIRA	.18
Adjusted R Square	.07	INTERFEREA	.16
Standard Error	.74	(constant)	.0000
F=		Signif F	
	18.71	=	.0000

Procedural equity is also clearly an important element in the instrumentality of the PRP scheme from an expectancy viewpoint. In

other words from a theoretical viewpoint procedural equity is important both in its own right in relation to the application of equity theory to the motivational effectiveness of PRP and also because it is an integral consideration in determining the instrumentality of the PRP scheme for expectancy theory. A PRP scheme that is perceived as being operated unfairly will lack both procedural equity and instrumentality. This point is illustrated by the fact that taken as two independent variables, without any other independent variables, FAIRA and INTERFERA account for 7% of the variance in MOTIVATION (Table 10.viii). However, when added to

**TABLE 10.ix – Regression/Expectancy 5**

Dependent Variable MOTIVATION			
Multiple R	.28	VARIABLE	BETA
R Square	.08	EXPECTANCY	.13
Adjusted R Square	.07	F11 Comparison	.08
Standard Error	.74	FAIRA	.17
		INTERFERA	.14
		(constant)	.0000
F=		Signif F	
	13.76	=	.0000

the basic expectancy model they increased its explanatory power from 13% (Table 10.i) to 15% (Table 10.ii). This would tend to support the importance of instrumentality in the expectancy model and suggest that procedural fairness is at least a part of the instrumentality measure in the expectancy model. It is worth recalling that INSTRVAL, which gives a measure of both valence and instrumentality, would appear to be the single most important explanation for the variance in MOTIVATION in the expectancy model judging from the Beta scores. Thus taken overall procedural equity appears to be an important consideration both for the

equity and expectancy models.

### The three theories of motivation and the Thames Water PRP scheme

Overall expectancy theory appears to explain more of the variance in motivation amongst Thames Water employees than either goal setting or equity theory. This suggests that Thames Water may need to look at the extent to which PRP outcomes are viewed as being both attractive and achievable if they want to increase the motivational effectiveness of the PRP scheme. However, this may not be as simple as it seems. On the face of it increasing the performance payment available under the terms of the PRP scheme should make the scheme outcomes more valent. But the qualitative research showed that since the introduction of PRP in Thames Water the overall size of pay increases each year has been low because Thames water have felt themselves constrained in the amount of money they put into the annual pay award by low inflation. Consequently the level of increases for the different performance ratings have not been highly differentiated, so that poor performers have not faired as relatively badly as they might have done, if there had been more scope for differentiation in the amount of money available for pay increases. In Thames Water the very poorest performers get no pay increase, but while inflation is in low single figures the relative decline in the value of their income will be less than it would have been if inflation had been in double figures. At the same time Thames Water has

restricted the amount of money available for the annual pay award because there is low inflation which means that there is less money available to reward those employees judged to have performed better. The low level of pay differentiation in the Thames Water PRP scheme was also initially exacerbated by the use of a pay matrix, which it will be recalled rewarded employees lower down the pay scale with a higher percentage increase than those higher up the scale for the same performance. Consequently it is difficult to see how the current scheme, where the performance payment takes the form of the annual salary award, can be used to increase the valence of the outcome without putting more money into the annual salary award. Employers sometimes argue that the improved performance from PRP will increase the amount of money available for pay increases allowing them to put more money into the annual salary award. However, the evidence from interviews with key players in Thames Water suggested that PRP was seen as a means of controlling the salary budget and not increasing it. Substantial increases above the rate of inflation in Thames Water pay would have altered Thames Water's position in relation to the market rate for pay, at a time when managers were arguing that Thames water was paying in excess of the market rate and needed to reduce pay levels.

This leaves the difficult question of how Thames Water should distribute the limited funds available for pay increases between employees in order to increase employee motivation. One approach is to give a

comparatively large award to relatively few employees in order to differentiate awards employees receive. Unfortunately, while this may increase the instrumentality for a minority, it would also decrease the expectancy of achieving a valent outcome for the majority of employees. In short, given a limited wages pot, the more comparatively attractive wage outcomes appear for the high achievers, the less achievable they appear for the majority.

Valence is not limited to salary outcomes. Respondents were asked about a number of other potentially valent outcomes including promotional prospects and greater job security. The difficulty with these outcomes is that they are contingent on factors, which may be outside the employee's control. Employees may not face redundancy and there may be no promotion prospects. So that whilst valence instrumentality and expectancy may be important elements in the expectancy model, it may not be easy for Thames Water to do that much to the PRP scheme in these two areas to improve its motivational effectiveness. Thames Water may be more readily able to make improvements, which will increase the motivational effectiveness of PRP in other areas.

Perhaps the most obvious area for improvement is in respect of feedback. Feedback is important (Table 10.iii), for employee motivation, it improves the explanatory power of the expectancy model. As nearly a quarter of respondents had not been given an SPR in the preceding twelve months,

Thames Water could readily improve the motivational effectiveness of the PRP scheme through a more rigorous application of the requirement that managers carry out an SPR. This would at least ensure that employees were getting some feedback through the SPR, though feedback should also happen through the year. In addition, training for managers on how to give feedback would also seem likely to be beneficial. Good feedback is important, but the survey shows that the most effective feedback in motivational terms was feedback that gave employees confidence that they could achieve the goals that had been set for them. Employees were more motivated where they felt that their managers were supporting them.

One of the arguments used by employers for adopting PRP, and adopted by Thames Water, is that PRP is a fairer way of rewarding employees than other payment systems (page 18 Armstrong and Murlis 1994). Fairness in this context means that reward should reflect effort. The results of this research show that employees may have a different perspective so far as fairness is concerned. Equity theory focuses on the comparative effort reward ratio between employees, which is in essence the employer's argument for adopting PRP, yet this accounts for only 2% of the variance in motivation. Employees it turns out are more concerned with procedural fairness, which accounts for 7% of the variance in motivation. Employees expressed two concerns about procedural fairness, first of all that the procedure was being applied fairly and

secondly whether the manager's appraisal score was being overridden. The first question is whether the procedure is being applied fairly. There is research evidence showing that managers may adapt their appraisal to give what they feel is an appropriate rating (Harris 2001) or to reflect their prior commitment to the employee resulting from their involvement in that employee's appointment (Brody, Frank & Kowalzyk 2001) rather than applying the scheme objectively. However the survey results reflect the employees' perceptions about the fairness of the scheme, and while those perceptions may or may not be justified, they are effectively a measure of the employee's trust in the manager who conducts the appraisal. Turning to the question of interference, qualitative evidence is that Thames Water does not operate any quota systems to limit managerial appraisal scores, although they do monitor appraisals. Concern about interference with managerial appraisal scores may in part be a result of employee ignorance about the operation of the PRP scheme, but it largely seems to reflect a lack of trust in the firm. A scheme that from the employer's point of view was meant to increase the fairness of the pay system, is seen as unfair by many employees because of a lack of trust in their managers and Thames Water, which in turn damages the motivational effectiveness of the scheme (Lawler 1981 and Siegall & Worth 2001).

Initially one of the key aims of this research was to see whether goal setting theory provided a good explanation of the motivational

effectiveness of PRP. The research has not supported this approach. The quantitative research does not provide either reliable scales or a robust model of goal setting, but the difficulties of operationalising goal setting in a field setting only became evident once the research was under way. Nevertheless given the weight of evidence from both laboratory and field research supporting goal setting and its obvious affinity with PRP, it remains an attractive area for further field research.

### Changing the organisation's culture.

To understand how far PRP accounts for changes in corporate culture in Thames Water, it is necessary to understand how PRP works as an engine of cultural change. It is argued in this thesis that PRP can change culture by reinforcing the importance of performance to employees and increasing employee commitment. PRP reinforces the importance of performance by putting performance closer to the heart of the reward calculation. Employee commitment is increased as key corporate objectives are cascaded down through the organisation, as the performance targets employees must achieve in order to get a performance payment. As employees strive to achieve the performance targets set for them so they will come to see the company's values and beliefs as legitimate values and beliefs that they share. If these arguments are correct and it is the focus on performance and the effect on commitment of cascading corporate objectives that lead to changes in

organisational culture then it follows that, in order to work effectively as an engine of cultural change, PRP must be effective in motivating employees. An effective PRP scheme will send a clear message about the importance that the employer attaches to performance and at the same time it will cascade key organisational behaviours and targets down through the organisation as performance targets which need to be achieved in order to earn a performance payment. A PRP scheme that failed to motivate, on the other hand, is hardly likely to reinforce the importance of performance for employees or get them to take on board the organisational behaviours and targets that are set as performance targets.

These propositions about PRP as a mechanism for cultural change have been tested using three hypotheses about the association between changes in corporate culture, commitment and motivation. The first of these is:

Hypothesis 3(a)

*'The Thames Water programme of cultural change will have brought about a change for some employees in their view of the relationship with their employer, and that will in turn have increased the commitment of those employees to the employer.'*

According to this hypothesis those employees who have believe there has

been the greatest cultural change, will in turn have become more committed to the employer. Essentially this hypothesis is concerned with changes in attitude over time. Unfortunately within the constraints of the research it has not been possible to measure attitudes at different points in time. Instead regression analysis has been used to examine the relationship between respondents' views about the change in the employment relationship in Thames water since the introduction of PRP and their commitment to Thames Water.

The extent to which employees believe that there is a more unitarist employment relationship is captured by the variable UNITARY, which comprises six items that are based on respondent's own views of the change in the employment relationship over the period in question (Appendix D). Only 21% of respondents felt that there was a more unitarist employment relationship in Thames Water in the period since the introduction of PRP, the majority were either neutral on the subject or thought that there had been no change. This would appear to be a reasonably robust measure of employee views about the extent to which they believe that there has been a change in corporate culture.

Changes in the level of employee commitment over time have not been measured in the survey, instead respondents were simply asked about their current level of commitment using a standard commitment rating (Cook & Wall 1980). It is clearly an unsatisfactory to conflate a measure

of change over a period of time with a snapshot of current attitudes and try and draw meaningful conclusions. However the importance of cultural change to the Thames Water PRP scheme was less evident at the beginning of this research than subsequently, particularly because of the company's refusal to co-operate with the research at the survey stage. Crucially this meant that there was no access to the principal managers involved in introducing PRP into Thames Water until after the survey had been conducted. Consequently the importance of cultural change for Thames Water only became fully apparent after the quantitative data had been gathered.

However it is still interesting to see what association there is between perceptions about organizational change and employee commitment. Factor analysis of the data from the Thames Water survey identifies two variables that represent employee commitment. Cook and Wall (1980) originally conceived of the measure as having three dimensions, identification, involvement and loyalty. However a two factor solution where identification and loyalty form one of the constructs, and involvement is identified as a separate construct appears a satisfactory if less desirable outcome (Peccei & Guest 1993). The first of these, BELONG comprises six items concerned with the employees level of loyalty and identification with Thames Water (Appendix D). The second, INVOLVEMENT comprises three items concerned with the employees willingness to 'go the extra mile' for the employer (Appendix D). These

two variables have been produced using Cook and Wall's (1980) standard commitment questionnaire. Both BELONG and INVOLVEMENT have been used as the independent variables in a regression analysis of the relationship between current levels of commitment and perceptions of organisational change over a period of time. The results of the regression analysis may at least go some way towards supporting hypothesis 3 (a), firstly because UNITARY 'explains' 25% (see Table 10.X) of the variance in BELONG. It is perhaps not surprising that there is an association between UNITARY and BELONG, as an increase in the unitary view of the employment relationship by definition involves a feeling of identification with the employer.

**TABLE 10.X – Regression/Commitment 1**

Dependent Variable BELONG			
Multiple R	.50	VARIABLE	BETA
R Square	.25	UNITARY	.50
Adjusted R Square	.25	(constant)	.0000
Standard Error	.98		
F =	160.39	Signif F =	.0000

Secondly, regression analysis also shows that UNITARY explains 13% of the variance in INVOLVEMENT (see Table 10.Xi). INVOLVEMENT reflects employees' willingness to put themselves out for the employers. From the employer's viewpoint identification with the firm may be an attractive trait, not least because it may cut down on transaction costs and lead to behaviors, which tend to promote the values of the firm. However, the employees' willingness to put themselves out for the firm offers the prospect of a more immediately tangible benefit in the shape of

additional work. Overall, the point that emerges from this association between UNITARY and the two commitment variables is that higher commitment is associated with the perception of a positive change in attitude that corresponds with Thames Waters' programme of cultural change. The crucial point, which it has not been possible to explore in this research, is the extent to which this association changes over time. Does increased employee identification with the employer lead to increased levels of commitment. On the face of it, commitment would seem to be a logical outcome of increased identification.

**TABLE 10.Xi – Regression/Commitment 2**

Dependent Variable INVOLVEMENT			
Multiple R	.37	VARIABLE	BETA
R Square	.14	UNITARY	.37
Adjusted R Square	.13	(constant)	.0000
Standard Error	.78		
F =	160.39	Signif F =	.0000

Increased employee commitment should it is argued in turn lead to increased employee motivation as result of PRP. After all, it seems likely that employees who identify more closely with the firm are more likely to buy into two of the psychological mechanisms that are associated with motivation. An employee who identifies with the firm may be more inclined to have a greater expectancy in a valent outcome, as a result of their belief in the organisation, so that according to expectancy there should be greater motivation. If the employee feels a strong sense of identification with the firm and wants to go the 'additional mile' to make sure the firm succeeds, then intuitively it seems more likely that they will

buy into the PRP scheme. Likewise, in terms of goal setting theory, an employee who is committed to the employer might be thought to be more likely to be committed to the goals that are set for them than employee who is not. Following this argument it has been hypothesized that:

Hypothesis 3(b)

*'Employees who are more committed to their employer will be more highly motivated by PRP than employees who are less committed to their employer.'*

Employee commitment is associated with MOTIVATION in the Thames Water survey, R.26 (see Table 10.Xii), but the amount of variation in motivation explained by the two commitment variables is 7%. Commitment explains less of the variation in MOTIVATION than expectancy theory, but about the same amount as procedural fairness. On the face of it this result seems counterintuitive, particularly in respect of INVOLVEMENT, as an employee who says that they are willing to do more for the firm might be assumed to be more motivated. However it is important to bear in mind that the variable MOTIVATION is specifically measuring motivation arising from the PRP scheme. Commitment may explain rather more, or indeed less, of the variance in employee motivation generally, that is to say motivation not specifically linked to PRP. An employee may be committed to the employer to such an extent that they want to make an additional contribution, irrespective of any additional payment. However, the hypothesis being tested here is that if PRP has a substantial effect in changing organisational culture, by

affecting employees' values and beliefs about the organisation, then there will be a link between PRP as a motivator and the other aspects of cultural change such as commitment.

<b>TABLE 10.Xii – Regression/Commitment 3</b>			
Dependent Variable MOTIVATION			
Multiple R	.27	VARIABLE	BETA
R Square	.07	BELONG	.18
Adjusted R Square	.07	INVOLVEMENT	.13
Standard Error	.74	(constant)	.0000
F =	18.65	Signif F =	.0000

The fourth and final hypothesis about organisational culture was that PRP would be more effective in changing organisational culture in those cases where it had been more successful in motivating employees. For PRP to be successful in changing organisational culture, which operates at the level of the individual's belief system, logic would suggest that it must also be effective as a simple motivator. It has therefore been hypothesized that:

### Hypothesis 3(c)

*'PRP will be more effective in changing organisational culture where the PRP scheme is also successful in motivating employees.'*

MOTIVATION has been regressed against the dependent variable UNITARY to test this hypothesis and it turns out that there is a strong

association, (see Table 10.Xiii) which tends to support the hypothesis. This result needs to be seen with the results of the analysis relating to the two other hypotheses about corporate culture. Although the results, so far as they go, are all supportive of the hypotheses to some extent, there are a number of problems.

<b>TABLE 10.Xiii – Regression/Culture</b>			
Dependent Variable UNITARY			
Multiple R	.44	VARIABLE	BETA
R Square	.20	MOTIVATION	.44
Adjusted R Square	.20	(constant)	.0000
Standard Error	.70		
F =	119.07	Signif F =	.0000

First and foremost, these three hypotheses are in effect testing an analytical framework, which may not be that robust. The analytical framework is based on previous theoretical work in a complex area where there is relatively little quantitative empirical work on which to build. Whilst there seems to be a level of agreement that pay is an important tool for bringing about cultural change (Drennan 1992, Kessler 1994, and Brown 1995); at least two commentators have highlighted the difficulty in predicting the outcome of any particular strategy for achieving cultural change (Kessler 1994 and Brown 1995). Organisational culture comprises a number of different facets (Schein 1992), so that predicting which mechanisms are likely to bring about a change in culture and how effective those mechanisms might be, is difficult. External variables may also have some affect on the impact of mechanisms used by the organisation to bring about a change in organisational culture, making it

even more complicated to predict the outcome of any particular strategy for bringing about change in organisational culture. Consequently the simple analytical framework suggested in this thesis for understanding whether or not PRP has helped to bring about a change in organisational culture, may well oversimplify the process and fail to capture the true picture.

The results gleaned from testing the analytical framework that has been adopted may be misleading. The danger is that the model misrepresents the flow of causation or fails to identify an important mediator. Put another way, do the results confirm that PRP needs to be effective in motivating employees in order to work as a mechanism for achieving cultural change within an organisation, or is there some other explanation? For instance, it could be argued that cultural change will encourage employees to work harder to achieve goals that they increasingly believe are in their interests, as well as their employers. The comparatively weaker correlation between commitment and motivation however suggests that it is more than simply a question of the employees' feelings about the employer, influencing their susceptibility to the motivational impact of PRP. It is the changing attitudes and perceptions associated with the Thames Water programme of cultural change which is more strongly associated with the effectiveness of PRP as a motivator. Given that PRP was a central part of the programme of cultural change introduced by Thames Water (see Chapter 8), the results would seem to

support the hypothesis that PRP is more likely to be effective in engineering cultural change in those cases where it is effective as a motivator.

## **Chapter 11**

### **Conclusions**

This thesis has examined the paradox between the continuing popularity of PRP and the widespread scepticism about the effectiveness of PRP as a motivator for employees. The approach adopted has been to use the evidence from a case study of PRP in Thames Water to address the following five questions.

- Why did Thames Water use PRP?
- How effective has PRP been in Thames Water as a motivator for employees?
- Why was PRP not more effective as a motivator for employees?
- How effective was PRP in delivering the other objectives it was originally intended to achieve?
- Why does Thames Water continue to use PRP?

Before bringing together the evidence from the research to address each of these questions it is important to understand the strengths and limitations of the research.

#### **The strengths and limitations of the research design.**

The results of this research into the Thames Water PRP scheme add to the general body of evidence about why firms use PRP and how

successful PRP is, both, in terms of increasing employees' motivation and in terms of some of the other benefits Thames Water hoped to achieve as a result of introducing PRP. The analytical approach adopted, using three theories of motivation as a framework against which to explore the motivational effectiveness of PRP, provides a new way of looking at the possible limitations on the motivational effect of PRP. This thesis touches on the question of whether and how PRP brings about cultural change; this in turn raises complex questions of causation, which call into question the effectiveness of PRP as a mechanism for bringing about cultural change.

The strength of a case study approach is that it is based on real events and gives a direct insight into how PRP is working in practice. However, the first hurdle with field research is getting access; this has proved particularly difficult in this case. The initial access to Thames Water was gained through the local branch of UNISON, the trade union, in 1995. It was not until 1999 Thames Water agreed to co-operate with the research for this thesis. The main research instrument adopted in this thesis, the employee survey, was drafted without the benefit of access to the employer for qualitative research. In the absence of any evidence to the contrary the survey focused on the justification given by Thames Water to the employees and Trade Unions for the introduction of PRP at the time when it was introduced. Thames Water produced 'A Guide for Employees' (circa 1992), which said that PRP was intended to provide a

fairer system of remuneration and increase employee motivation. It has subsequently become apparent after research access was granted by Thames Water that one of the principal and more enduring aims of PRP for Thames Water was as part of a Performance Management Scheme intended to bring about cultural change in the organisation. However, the emphasis in the questionnaire used in that research was on the motivational effectiveness of PRP, and the survey looked at cultural change as a peripheral issue. On reflection and with the benefit of the qualitative research access subsequently granted by Thames Water, somewhat greater emphasis should have been given to cultural change in the research approach that was adopted.

Cultural change is a process that operates at a number of different levels (Schein 1992) indeed Thames Water were relying on a number of different instruments apart from PRP to bring about cultural change in their organisation. This suggests that a longitudinal survey or panel study could have been used to capture some of the changes in attitude, however one of the drawbacks of such studies is that there tends to be a diminishing rate of return on the survey over time (Oppenheim 1992). If the importance of cultural change had been appreciated at the outset, it might have been better to use a repeated cross-sectional study, using questions identified by focus groups. As it was, the problems over access rendered the use of focus groups impracticable and the questions in the initial study did not readily lend themselves to a follow up study looking

at cultural change in Thames Water. The survey asked respondents about how employee attitudes had changed since the introduction of PRP and did not give a clear measure of corporate values and culture at a single point in time against which subsequent survey data from a similarly phrased survey could be compared.

The focus in the quantitative research for this thesis has been on the motivational effectiveness of PRP. Notwithstanding the importance attached to PRP as an agent of cultural change, Thames Water still ought to be concerned about the motivational effectiveness of PRP, both because of the overall cost benefit of PRP and because the motivational effectiveness of PRP may mediate the impact of PRP on corporate culture. After all, if the PRP scheme is not working in one respect, by motivating employees to improve their performance, there is a danger it may not be working, in another respect, by bringing about cultural change. In order to explore how PRP worked as a motivator, the three theories of motivation that seemed most likely to explain the effect of PRP on motivation were applied to the Thames Water PRP scheme. These three theories have been termed the framework of analysis. Each of the theories tends to highlight a particular aspect of the PRP scheme. Expectancy theory focuses on the valence of the outcome, while goal setting theory is concerned with the goals that are set, and equity theory is concerned with both the distributive and procedural fairness of PRP. However, there is an element of overlap between procedural fairness and

expectancy theory in particular. According to expectancy theory to be an effective motivator PRP should be instrumental in producing a valent outcome as a reward for additional effort, but any unfairness in the process can introduce an arbitrary element which may disrupt the chain of causal connection linking PRP with a valent outcome.

The framework provides a useful tool for understanding the way in which PRP works as a motivator. However, the application of the theories to PRP highlighted some practical problems arising from both the way in which the Thames Water scheme was operated and the application of these theories in a field setting. In particular the amount of pay contingent on performance in the Thames Water PRP scheme during the period of this research was so relatively small that it may not have been sufficiently attractive to employees to act as a motivator either in terms of expectancy or equity theory. On examination, it became apparent that the Thames Water PRP scheme operated in such a way that, as long as the level of wage increase in the economy generally remained low, the amount of pay contingent on performance in Thames Water was likely to be relatively small. The very worst performers in the company were denied any pay increase at all, but there were comparatively few in this category and any who remained there for any period of time were at risk of losing their employment. For the vast majority of employees the likelihood was that they would receive a performance payment at or around the rate of inflation. PRP really meant that for a small proportion

of the workforce it was possible to earn one or two percent more than the majority in their pay increase until such time as they reached the top of their grade, when a similar sum might be paid on an unconsolidated basis. Consequently in applying expectancy and equity theories to PRP in Thames Water, the study was in practice looking at how far employees were prepared to put in additional effort to achieve a comparatively small reward.

Goal setting theory turned out to be difficult to operationalise because the problems of measuring an objective variable, goal difficulty, in an attitude survey. Locke and Latham (1990, pp 75-76) say that goal difficulty in an attitude survey is unreliable because it is a confounded measure capturing both the goal difficulty and the respondent's feelings of self-efficacy. In practice it was difficult to identify a robust measure of goal difficulty from the Thames Water survey and this may help to explain the disappointing results obtained from trying to operationalise goal setting theory. Goal setting is a motivational technique, which could potentially justify moving from PRP to a system of goal setting and performance assessment unrelated to any financial incentive. If, as some critics (Kanter 1989, Kohn 1993 and Pfeffer 1998) have suggested the financial reward undermines teamwork and sours the relationship between managers and those they manage, removing the financial element, and focusing on the goal setting process might be an attractive alternative to PRP. Originally it had been hoped that the survey results

would provide an opportunity to explore this possibility in more detail, unfortunately the difficulties of operationalising goal setting have hampered this area of research.

In addition to the issues around research access and the difficulty of operationalising the theoretical framework in a field setting, there have been time constraints on completing the research and writing up the thesis. This thesis has taken some time to finish because it has been completed part time and has necessarily had to compete against a number of other commitments at work and home. The original quantitative primary research on which the thesis is based was conducted in 1995. Relatively speaking little has changed in the Thames Water pay system applied in the utility business in the United Kingdom in the intervening period and the research remains pertinent. The relative stability of the UK utility operation is due in part to the nature of the business, which is focused on providing a consistent quality of service in the supply of water and wastewater services. International developments, including the purchase of Thames Water by the German multi utility group RWE and the expansion of Thames Water into the United States market through the purchase of American Water in 2002, may also have taken some of the focus away from the UK utility operation in the intervening years.

This final Chapter has been used to update the picture of the Thames Water PRP system and compare views of both the company and employees over time, using information from a review of the reward system and an interview with the current Director of Human Resources. Thames Water have recently initiated a review of their reward system, and although the company is not intending to replace the PRP pay system in Thames Water, some of the preparatory work for the review provides an interesting if limited update on employee views regarding PRP. Thames Water established 12 focus groups from across all business units encompassing all grades of employees (the survey conducted for this thesis excluded manual workers); no notes were kept of who attended or of who said what in order to give a degree of anonymity. All views were included in the report prepared of the focus group work, the Reward Framework Project Focus Group Feedback Report (October 2001). Where appropriate information from the Report has been used in this concluding Chapter. Likewise comments from the current European Director of Human Resources, Julia Cherrett have also been included at this stage to give an update on Thames Water's views on PRP.

#### Why did Thames Water introduce PRP?

Even though PRP was introduced by Thames Water ostensibly in order to provide a fairer system of rewards and increase employee motivation, it has been hypothesised that one of Thames Water's principal reasons for

introducing PRP was in order to help bring about cultural change following privatisation. The research evidence supports this hypothesis. Thames Water introduced PRP as part of a process of change aimed at taking what had been a nationalised industry and transforming it into a more commercially focused private company. Much of the drive behind these changes came from Roy Watts the Chairman of Thames Water. As a precursor to privatisation, Thames Water was the first water company to withdraw from national pay bargaining and some 60 or 70 members of the top management team were taken off collectively bargained terms and conditions and given personal contracts. Pay and changes to pay arrangements were clearly seen by Thames Water as sending important messages about the type of company Thames Water wanted to be. Watts also brought in managers from the private sector to give Thames Water what he termed the 'strength of the mongrel', by mixing those managers with experience of the water industry with managers with experience of the private sector.

After Thames Water was privatised a small group of managers looked at the personnel issues facing the company, according to Steve Jay, the then Director of Personnel, the group asked itself two questions. What would you do if you had a 'blank sheet of paper' as far as personnel policies were concerned? And what is stopping you from managing effectively? The group came up with a proposal termed the 'Employee Project', which was signed off by top management and implementation

started in 1990, the year after privatisation. PRP, which was introduced in 1992, formed part of the employee project and was clearly part of a wider strategy aimed at transforming the way the company operated and changing the culture within the company.

Thames Water used pay as a mechanism for helping the company to realise its strategic business objective of getting greater commercial focus by putting performance at the heart of the pay bargain. Pay was being used to achieve a strategic business objective by bringing about cultural change within the organisation. This strategic approach is consistent with the concept of 'new pay' or strategic fit, but as Kessler (2000) observes the reward strategy not only has to fit corporate strategy, in order to be effective it the strategy has to be implemented and operated consistently. The Thames Water reward strategy contained some internal inconsistencies or tensions, which affected the implementation and operation of the strategy and militated against PRP achieving all the objectives it was intended to.

The tensions within the reward strategy become apparent when Thames Water's objectives in introducing PRP are considered. The research shows that Thames Water hoped to achieve five objectives through the introduction of PRP. Those objectives were:

- To motivate employees
- As a way of managing down wages

- To make the system of reward fairer by rewarding contribution
- To encourage managers to manage more effectively
- As a mechanism for achieving cultural change

Initially it was explicitly the hard reasons of wage control (Minute 3 page 2 - minutes of Thames Water Company Council -29<sup>th</sup> May 1992), motivation and fairness that were used to justify the introduction of PRP (Thames Water Utilities – Performance Related Pay – a guide for employees – undated circa 1992). PRP was intended to produce the immediate and hard benefits of controlling wage costs, yet reward contribution and motivate employees. On the face of it these were potentially conflicting objectives, as rewarding contribution and motivating employees might need more money for wages; not less. The contradiction between wage control and motivation is highlighted by the ACAS guidance on pay systems (2003), which advises that it is important to have the necessary finance in order to operate PRP, and goes as far as to warn that paying a small performance payment is unlikely to motivate and may even demotivate employees. It could be argued that, notwithstanding the views expressed by ACAS, the initial costs of introducing PRP with a level of performance payment sufficiently high to motivate employees should be recouped in the longer term through improved performance by the firm as a result of the incentive effects of PRP. However, Thames Water saw PRP as a mechanism for achieving wage control from the start and consequently did not want to put

additional money into the pay bill to fund larger incentive payments even at the outset.

Thames Water hoped that by managing salaries on a matrix that was intended to put average performers on the mid-point of the salary range, wage costs could be managed down. When PRP was introduced headline inflation was running at a relatively high rate and wage increases in general were correspondingly high as pay settlements tended to keep pace with inflation. Thames Water believed that this would give them 'room' in the annual pay awards to both significantly differentiate between the levels of performance achieved and use the performance payment to get employees to their natural level on the pay scale relatively quickly. However, a drop in the rate of inflation led to lower salary settlements, which meant that the pay increases after PRP was introduced were never large enough to allow sufficient differentiation in pay to make any significant impression on the anomalies brought about by salary protection. Thames Water, who already felt that they were paying above the market rate, were reluctant to give pay increases which put them further above what they believed was the market rate. The managers who had been responsible for introducing PRP thought with the benefit of hindsight that it was low inflation that had been a barrier to the effectiveness of PRP as a mechanism for rewarding contribution, motivating employees and controlling wage costs. In retrospect it is clear that predicated pay strategy on continuing high inflation left the strategy

vulnerable to changes outside Thames Water's control.

In any event, on closer examination it is apparent that the use of PRP by Thames Water as a mechanism to manage down wages has been counterproductive in terms of rewarding contribution and motivating employees irrespective of the rate of inflation. Essentially there were two problems: the lack of transparency in the process; and the absence of meaningful incentives. The PRP process was based on employees' performance payment being dependent on their place on the salary matrix so that wages could be managed down as employees gravitated to their so called 'natural' point on the salary matrix. However, the use of the salary matrix made the process so opaque and confusing that irrespective of the amounts involved many employees saw no link between reward and contribution and this undermined the motivational effectiveness of the scheme. The other problem was the apparent contradiction between trying to motivate employees with the promise of additional pay, while at the same time trying to control the pay bill. This meant that Thames Water were reluctant to increase their overall pay bill making it difficult for them to offer any substantial incentives to higher performers, without actually reducing pay for other employees. In practice it was only those few employees whose performance was deemed 'unacceptable' who were denied any pay increase. Consequently the amount of additional pay employees could expect to earn for 'excellent' performance was only one or two percent more than those

employees whose performance was assessed as 'acceptable'.

These contradictions in the original objectives that Thames Water hoped to achieve through PRP were highlighted in a number of the answers given to the open question in the survey conducted for this thesis. The employer's own survey (Viewfinder 94) found that only 13% of respondents thought that PRP rewarded superior performance and commented 'Few of you feel it (PRP) sufficiently rewards good performance, or that it penalises poor performance'. Employees' motivation was soon discarded as an immediate and direct justification for PRP, because as Derek McManus, one of those closely involved with the introduction of PRP, said looking back it could be seen that PRP had not been a particularly effective motivator. This is a view shared in by the Director of Human Resources for Thames Water, Julia Cherrett, who has commented:

"...with the benefit of hindsight it is difficult to be sure how far PRP is helping to motivate employees. For us the importance of PRP is that it underpins our Performance Management processes..."

Julia Cherrett saw PRP not as a direct motivator of employees but as part of a process of Performance Management, which would lead to improved performance. At one level Performance Management is about getting managers to ensure employees are aligned with the organisational objectives, what Harding et al (2000) call 'the line of sight'. The original aim for PRP in Thames Water of getting managers to take responsibility for managing performance was essentially about more than simply

ensuring the cascade of organisational objectives through the performance appraisal process; also it was about changing the way things were done and in consequence organisational culture. These cultural change objectives were not stated so explicitly at the time PRP was introduced, but can be clearly identified from the qualitative research.

Thames Water intended PRP to be a central part of performance management from the outset. The idea was that managers would be forced to address the issue of performance amongst the employees whom they managed. This was important because from the company's point of view it was part of a move away from the old public sector way of doing things. As Steve Jay, who was in charge of employee relations when the PRP scheme was introduced put it:

"...we had management and supervision generally who didn't manage... ....we thought that it (PRP) would bring the linkage with employees and their performance right into the centre of the stage..."

Looking back on the introduction of PRP after ten years, Julia Cherrett the current Director of Human Resources, saw its importance in terms of performance management as key to the original introduction of PRP, and as central to the continued use of PRP by Thames Water.

"For us the importance of PRP is that it underpins our performance management system. We believe that it is the performance management system that is instrumental in improving performance and bringing about a change in culture."

The evidence from those involved at the time was that PRP was introduced as part of a process of cultural change. Even though PRP was not explicitly recognised in the company's published statements as a mechanism for bringing about cultural change, it is clear from this research that the aim was to change the culture of Thames Water from a public sector culture to a more commercially focused one. Ultimately it is this longer term, softer justification for introducing PRP, which has proved most enduring. The harder more immediate benefits of PRP namely wage cost control and increased employee motivation, proved more illusory from the company's point of view and were soon discarded as a justification for using PRP.

How effective has PRP been in Thames Water as a motivator for employees?

The survey evidence from the research conducted for this thesis shows that PRP increased motivation in Thames Water for only a small number of employees. At best, 18% of respondents to the survey said that PRP had increased their motivation the rest either said that it had not or were neutral on the subject. It is difficult to know whether this level of increased motivation constitutes a net benefit to Thames Water. PRP has potential disbenefits as well as potential benefits and the survey attempted to capture information on the disbenefits arising from PRP as well as the benefits. Some of the results from the survey reflect well known arguments about the negative effects of PRP on team working

and relations between managers and the employees they manage (Kanter, 1989 and Kohn 1993). Jealousy amongst employees was identified as a problem by 17% of respondents. Nearly half of respondents said that PRP had eroded their trust in their manager and practically half of respondents said that they had to keep on the right side of the manager to get a good PRP score. These negative effects of PRP need to be weighed against whatever positive impact PRP has on employee motivation, Performance Management and cultural change.

The evidence from the key players involved at the time PRP was introduced and from the current European Director of Human Resources is that Thames Water soon became aware that PRP was not particularly effective as mechanism for increasing employee motivation. The research evidence shows that PRP was viewed by Thames Water as a cornerstone of Performance Management and an important part of a wider programme of cultural change aimed at giving employees a more commercial focus. However this does not mean that the motivational effectiveness of PRP is therefore a redundant or at best peripheral issue. In fact, performance was and remains a central concern for Thames Water, hence their focus on Performance Management and a more commercially orientated culture. Performance is a product of, amongst other things, employee motivation, so for Thames Water employee motivation was not a redundant or peripheral issue; it was at the centre of what they wanted to achieve.

The failure of the PRP scheme to motivate many Thames Water employees may mean that it has not been effective in helping to bring about the change in corporate culture that Thames Water wanted to achieve. Indeed, if PRP is eroding the trust between manager and managed there must be a danger that instead of improving Performance Management and helping to create a more commercially focused culture, PRP will have a negative effect on both Performance Management and culture. Consequently the failure of the Thames Water PRP scheme to motivate over 80% of respondents, is important not just in itself but also in terms of the objectives Thames Water hoped to achieve through PRP.

#### Why was PRP not more effective as a motivator for employees?

The approach adopted in this thesis has been to explore the motivational effectiveness of PRP through a framework of theories of motivation using hypotheses in Appendix F to test the extent to which the Thames Water PRP scheme engages each of the theories. The framework comprises three theories of motivation; expectancy theory, goals setting theory and equity theory on the basis that these are the theories that most closely model the PRP processes. The rationale for this approach is that by seeing how far each of the theories helps to explain the motivational effects of PRP it should be possible to identify which of the theories

explain most the motivational effectiveness of PRP. Then the theory or theories or those parts of the theories that seem most pertinent can be used to identify and explore possible prescriptions for the improvement and strengthening of the Thames Water PRP scheme.

Expectancy theory explains more of the variance in the motivational effects of PRP than the other theories of motivation tested in this thesis. Equity and feedback variables, that is to say variables capturing the perceived fairness of the PRP scheme and the quality of feedback from managers, increase the explanatory power of the expectancy model. Depending on the complexity of the expectancy model used between 13% and 18% of the variance in the motivational effect of PRP is explained by expectancy theory. However, a more parsimonious model, comprising the basic expectancy model of valence, instrumentality and expectancy together with positive feedback explains 16% of the variance in the motivational effectiveness of PRP. It is this more parsimonious model that appears to give the best trade off between explanatory power and parsimony. The relative importance of the expectancy model in explaining the variance in the motivational effectiveness of the PRP scheme highlights the importance of the reward aspect of the scheme and the linkage between performance and reward.

When it comes to the fairness of the PRP scheme, there were substantial differences in the explanatory power of the equity model based on

distributive equity as described by Adams (1965) and procedural fairness. There are problems of specification with the distributive equity model of motivation particularly in relation to the comparator group and the remedial action employees might take if they feel there is an imbalance in effort reward ratios between them and their comparators, which make it difficult to apply. There were also problems with measurement. A single item had to be used to capture employees feelings about how well or badly they were paid in comparison to others in Thames Water and a single item is not a particularly satisfactory measure to use with data from an attitude based survey (Oppenheim 1992). These problems of specification and measurement may in part account for the relatively poor explanatory power (2%) of distributive equity in respect of the motivational effectiveness of the Thames Water PRP scheme. The results in relation to distributive equity are none the less interesting because distributive equity potentially provides an explanation for both the motivating and demotivating effects of PRP. Employees who feel that the amount of effort that they are expending in relation to the rewards that they are receiving is unfair when compared to the reward others are receiving for their efforts may respond by reducing their effort.

Procedural equity in Thames Water, on the other hand, explains more (7%) of the motivational effectiveness of PRP than distributive equity. A number of writers (Greenberg 1987, and Cropanzo & Folger 1991) have suggested that procedural equity may be a more important consideration

than distributive equity in motivation. The concept of procedural equity is also implicit in the expectancy model, which predicts that a valent outcome will have a motivational effect in respect of action that is instrumental in producing that outcome. An action is only likely to be seen as instrumental in producing a valent outcome if the processes by which the outcome are determined are seen as predictable rather than arbitrary and unpredictable. Consequently in the case of PRP it is important that the process of determining the performance payment is fair in order to increase employee motivation both from the point of view of procedural equity and expectancy.

Goal setting theory poses a particularly interesting perspective on PRP, because it focuses principally on the nature and difficulty of the goal set rather than the prospective reward for achieving that goal. Potentially this means that the financial reward associated with PRP could be downplayed or removed and more emphasis placed on the goal setting process, with the same motivational effects being achieved without some of the problems over team working and employee manager relations. However, the problems of measuring goal difficulty in a field setting mean that the results of the analysis of the data from the Thames Water survey need to be treated with caution. At best it would appear that goal setting accounts for no more than 5% of the variance in employee motivation caused by PRP. Notwithstanding the relatively low level of association between goal setting and the motivational effectiveness of

PRP in Thames Water this still appears to be an interesting area for further research. Not only is goal setting a plausible motivational technique; it also mirrors much of the PRP process. There is a substantial body of research evidence from the USA supporting the effectiveness of goal setting as a motivational technique ( Locke & Latham 1990). Furthermore, goal setting models the PRP process, without the reward element, thus potentially addressing some of the performance management issues without contaminating team and employee manager relationships with the problems associated with performance payments (Kanter 1989, Kohn1993 and Pfeffer 1998).

It would be wrong to assume that the analysis provided by the theoretical framework posed in this thesis is a simple prescription for increasing motivation either in Thames Water or any other PRP scheme. There are conceptual and, perhaps more importantly, practical problems in simply assuming that if Thames Water addressed the issues raised in respect of key variables in the models of motivation employee motivation would be increased. First of all of all it is worth considering some of the conceptual problems that apply to all of the theories of motivation tested in this thesis. In each case the theory is explaining the variance in what is a largely negative or neutral measure of motivation, because it turns out that relatively few Thames Water employees report being motivated to work harder by PRP. It may be that whatever improvements were made in the scheme the numbers or level of motivation would not be

increased. There may be other variables either in the workplace or in the employment relationship that make employees reluctant to exert additional effort for Thames Water. For example, employees may feel that their jobs are at risk and resent any additional effort for a firm that they believe is going to make them redundant or they may believe that they are working as hard as they can for Thames Water already irrespective of the promise of an additional increase in salary through the PRP scheme.

Notwithstanding these conceptual problems, it is at least worth considering what 'lessons' can be drawn from the Thames Water case study about the sort of improvements that could be made to the Thames Water PRP scheme in order to improve its motivational effectiveness. The theoretical framework of analysis adopted in this thesis highlights three areas of the PRP scheme that appear to have a stronger effect on employee motivation than other aspects of the scheme. These are essentially:

- The value of the outcome
- Fairness and transparency
- Feedback

Focusing first of all on the value of the outcome, clearly in the case of PRP the explicitly valent outcome is the performance payment, which in Thames Water was in effect the level of the employees annual salary

increase. Members of the Focus Groups used to assist in reviewing the reward system expressed concerns over the small pay differential used to reward different levels of performance in the Thames Water PRP scheme:

'Robbing "Peter to pay Paul" ...only limited budget to be distributed, ...the result was "a done deal" with little reference to actual performance ... PRP distributions are forced and that individuals have no influence over the outcome of their PDR discussions. (The Reward Framework Project Focus Group Feedback Report – October 2001)

In other words the message from the Focus Groups was that the system is incapable of rewarding individual performance fairly, because the financial constraints delimit the total amount available to reward performance.

It would presumably be possible to increase the valence of the Thames Water PRP scheme for employees by increasing the overall wage increase to employees. However, this prescription seems unlikely to appeal to Thames Water, particularly as PRP was originally introduced as a way of controlling pay. Another alternative would be to increase the level of PRP pay increase for those receiving the best performance rating, at the expense of those with a lower level of rating. While this might have the effect of improving the valence of the outcome for a few employees, it seems likely to decrease it for the majority of the others or at least reduce their expectancy of receiving a valent outcome.

Improving the fairness and transparency of the PRP scheme or at least its apparent fairness seems to be more likely to be an effective prescription

for improving the motivational effectiveness of the scheme. There are two reasons for this. First of all fairness is important to the motivational effectiveness of the scheme both because it is relevant to the instrumentality of the scheme and because procedural fairness turns out to be a factor in its own right and as an elaboration on the basic expectancy model. Secondly there are real practical steps that Thames water could take in order to improve the apparent fairness of the PRP scheme. In practical terms fairness and transparency mean that Thames Water needs to be more open and transparent about monitoring and ensure that managers are seen to manage the scheme more fairly. The SPR interviews, for example, provide an important opportunity for managers to give encouraging feedback to the employees that they manage. Without an SPR interview employees are unlikely to feel that they are being supported in achieving the targets set for them or that the manager takes the PRP scheme seriously. The evidence is that it is not so much the number of SPR interviews as the quality of the management support and feedback in those interviews that was important. Feedback, at least in so far as it is supportive of the employee in achieving the targets that they have been set is an important element in the motivational effectiveness of PRP in its own right. The role of supportive feedback in the explaining the motivational effects of PRP seems to reflect the importance of self-efficacy (Bandura 1986) in employee motivation. Managers need to make sure that they are not just giving feedback, but that the feedback is appropriate. The advantage from the

company's point of view in addressing issues of transparency, fairness and feedback rather than question of relative level of reward is that taken at face value this looks like a relatively inexpensive improvement to the scheme. In addition the idea of making the scheme fairer, more transparent and more supportive of employees appears to be non-contentious.

How effective was PRP in delivering the other objectives it was originally intended to achieve?

Thames Water came to see PRP as primarily a mechanism for bringing about cultural change within the organisation. However, it is far from clear how successful PRP has been in achieving this goal. There are three reasons for this. The first is that organisational culture is a complex web that operates at a number of different levels and so is subject to a number of different influences (Schein 1992). Consequently, it is difficult to know how far PRP as opposed to say the introduction of more managers from the private sector (another mechanism explicitly used by Thames water to bring about cultural change) actually accounts for cultural change in Thames Water. Indeed it seems not only possible but likely that other developments such as the privatisation of the company will have had a more significant impact on the organisational culture within Thames Water.

The second problem in identifying how far PRP has contributed towards a change in organisational culture is that there is no clear prescription as to how PRP would change organisational culture. While pay is seen as an important tool in changing culture (Drennan 1992, Kessler 1994, and Brown 1995) the mechanism by which a PRP pay system might bring about cultural change is less clear. The process suggested in this thesis comprises three stages. Firstly, PRP cascades corporate objectives to employees, and those employees who have been motivated by PRP in particular will tend to accept as valid and therefore adopt as their own the corporate objectives set for them. Secondly, employees who buy into the corporate objectives will also become more committed to the employer. Thirdly, the PRP scheme should be more likely to increase the motivation of employees who become more committed to the employer, through the programme of cultural change. This suggests a virtuous circle of an effective PRP scheme increasing employee commitment, leading to cultural change, which in turn improves the effectiveness of the PRP scheme. This analysis matches the view expressed by those involved in introducing PRP and the current Director of Human Resources, that PRP was essentially a key part of Performance Management, and that effective Performance Management would in turn help to produce a more commercially focused corporate culture. However, it may be that PRP far from encouraging employees to adopt the corporate objectives makes employees more suspicious of those objectives because they are seen as part of a commercial transaction

where the company is trying to buy the employees' commitment. Indeed in the case of an essential public service such as the supply of water and wastewater services, employees may have a stronger sense of public service and so react more adversely to being offered more money to do a job that they feel is intrinsically worthwhile, than elsewhere.

The third problem is one of causation. While the model for cultural change suggested in this thesis may appear credible, it does not describe a clear causal mechanism. It is based on the hypothesis that successful cultural change should reduce internal transaction costs and is therefore concerned with increasing employee commitment (Denison 1990). But it is difficult to be certain from the results how the process works. Do changes in organisational culture lead to increased commitment, or does change in commitment lead to a change in culture, or is the relationship between commitment and culture endogenous? Just as importantly the model cannot identify the extent to which the PRP scheme is causing either increased employee commitment or a change in organisational culture. It seems more likely the PRP scheme will be effective in increasing employee commitment and changing culture in those cases where the employee accepts the objectives set during the SPR process and sees the benefit in working to achieve those objectives. That is to say PRP is more likely to be an effective agent of change where it is effective in motivating employees. However, it seems equally plausible that those employees who are most committed to the employer, at least

as a commercial organisation, or who feel that there has been the greatest shift in organisational culture, are more likely to sign on to the precepts that make PRP an effective motivator. Alternatively, employees, who are committed to water supply and the treatment of waste water as a public service, might find the commercial approach adopted by Thames Water reflected in their PRP objectives and consequently find it difficult to reconcile those PRP objectives with their commitment to public service (Deci 1972). Consequently it is difficult to be sure how far the association between the motivational effectiveness of PRP, employee commitment and changes in corporate culture reflect a causal linkage.

Each of these three concerns needs to be borne in mind when looking at the results from the Thames Water case study. The evidence of successful cultural change was in any event patchy. Nearly 80% of respondents thought that the feeling of 'them and us' remained unchanged, yet at the same time about a quarter of respondents thought that there was greater identification with the core values of Thames Water. Only 21% of respondents thought that there had been an increase in the unitarist views of employees since PRP was introduced, the majority either thought that there had been no change or were neutral on the subject. This suggests that any change in culture that had taken place in the period since the introduction of PRP had only limited effect in reducing the transactional costs within Thames Water.

Thames Water took the view that PRP, as an essential part of their Performance Management scheme, would ensure that managers and employees were more focused on performance and that this would in turn help change Thames Water from a traditional public service organisation into a more commercially orientated company. Cascading corporate objectives through the PRP scheme would give employees, what has been termed (Harding et al 2000), a clear 'line of sight' to the company's objectives and that employees would adopt these objectives as their own leading to a change in culture in Thames Water. There were practical problems with the operation of this model. Research showed that 22% of employees reported not having had an SPR (the interview at which goals are set and performance is reviewed by the manager) in the last twelve months. Julia Cherrett the European Human Resources Director thought that it might be the rate of change of managers in post that accounted for the high proportion of respondents reporting that they had not had an SPR in the last twelve months. Even so, if those respondents who said that they had no SPR during the previous twelve months are filtered out of the data, 20% of respondents reported being unclear about how they could achieve the objectives set for them (another 10% were not sure whether they were clear or not). Likewise 24% of respondents who had an SPR in the previous twelve months said that their manager did not take the SPR seriously (18% were not sure). Even leaving aside the fifth of employees who reported not having had an SPR interview in the last twelve months, it is not clear that PRP was

having the sort of proselytising effect that Thames Water hoped. Nearly half of all respondents said PRP undermined the trust between employees' and their managers and it seems unlikely that employees whose trust in their manager has been undermined by PRP will be inclined to adopt the values and objectives promoted by PRP.

#### Why does Thames Water continue to use PRP?

Thames Water continues to use PRP and there is no public indication that they intend to stop using PRP. Taken at face value this may signify a continuing belief both in the efficacy of PRP as a performance management tool and in its longer-term role in making the culture in Thames Water more performance orientated. But it is also worth considering what pressure there is on Thames water to change from using PRP and what options are available in order to get a full picture of why the company continues to use PRP.

Thames Water is again reviewing the employee reward system. There is no suggestion that PRP will be dispensed with by Thames Water. The comments from the Reward Framework Project Focus Group Feedback Report (October 2001) are interesting in this respect. PRP was described as the 'hottest topic' and it was said that in the main members of focus groups:

"Agreed with need to link pay and performance but did not like the current system."

This comment fits in with the results of the survey of Thames Water employees conducted for this thesis (66% thought PRP was a fair way of paying employees) and the results of a number of other surveys of employees in other organisations (Marsden & Richardson 1994 and Marsden & French 1998). Support for the principle of a performance pay system and the 'heat' that such systems generated amongst Thames Water employees illustrates the difficulty in putting this seemingly straightforward concept of relating pay to performance into practice.

It seems more likely from the evidence of this research that a PRP scheme will command the support of employees, if those employees perceive it to be both fair and objective. This is more difficult than it at first appears, as individual employees may have inflated or unrealistic opinions of their own performance and may feel that any assessment to the contrary is in some way subjective or unfair. After all it is a rare gift to see ourselves as others see us:

"O wad some power the giftie gie us --  
To see ousrels as itheres see us!"

-- From Ode to a Louse  
*Robbie Burns*

Even the focus group identified the lack of objective managerial assessment of performance as a defect in the scheme.

"...(PRP) System only works well if managed well, good managers make the system work, but is dependant on subjective opinion of manager...."

PRP was seen by employees, at least those in the focus groups, as being not so much about performance management, as dependent, for its fair and effective use, on good management. PRP was seen not as a management aid, but as a test of management. Amongst the solutions suggested by the focus group to this particular problem were the following two:

**"Proposed Solutions:**

- *Remove the PRP system completely*
- *Replace system with one that doesn't rely upon management judgment..."*

Dispensing with PRP seems unlikely to be an attractive proposition for a company like Thames Water where there is a continuing focus on improving performance. After all taking performance out of the effort reward equation might send the wrong message to employees. Any pay system may have a certain amount of inertia against change and because of the messages PRP sends about performance, a company like Thames Water may well be even more reluctant to change PRP than it would another pay system. Pay is seen as sending a strong message to employees because of its importance to them, consequently from the employer's point of view this suggests that basing pay on corporate objectives is one way of highlighting the importance of those objectives. Whatever the reality of PRP in terms of its impact on employee

motivation or corporate culture, perhaps the message that Thames Water is a performance-orientated company outweighs any problems associated with PRP.

Equally many of the alternatives to PRP may seem less attractive to Thames Water. Incremental pay or paying a rate for the job would both send the wrong message about the link between performance and reward as far as Thames Water is concerned, other alternatives such as capability based pay might well prove as controversial as PRP. One alternative to individual PRP suggested by Pfeffer (1998) is the use of group based reward schemes, such as profit sharing, stock ownership, gain sharing and group bonuses. In a group based reward scheme reward is not contingent on the performance of the individual but on the performance of the wider group. According to Pfeffer (1998, p. 223) 'individual incentive schemes erode teamwork and trust and set people against one another in a competition for rewards'. Adopting a group reward approach overcomes these problems by emphasising the importance of the group and the value of team-working, while at the same time giving an incentive for improved performance. Thames Water already has share ownership and profit sharing schemes for all employees, indeed these schemes were introduced at the same time as PRP. For Thames Water the prescription offered by Pfeffer would mean abandoning the individual PRP scheme and either relying on the existing group reward schemes or perhaps even moving to some form of group

bonus scheme, with bonus payments based on work group performance. Thames Water seem unlikely to adopt this approach for a number of reasons. One of the challenges with group PRP schemes is identifying a team against which meaningful team objectives can be set where employees will feel that their individual performance has a direct impact on team performance, Director of Human Resources Julia Cherrett saw this as major drawback for group PRP. A group PRP scheme would also be seen by Thames Water as diluting the Performance Management element of PRP. Individual PRP also gives a degree of consistency with the individual merit payment received by top management in Thames Water. Given the sensitivity (Hodgson, Kirkwood & Smith 1999) over top management pay, it may suit Thames Water to be able to argue that a consistent approach is adopted to employee reward, even if the magnitude of the reward is substantially different depending on the employees position in the hierarchy.

## Conclusion

The link between pay and performance, explicit in PRP, turns out in this case study not to be particularly effective as a mechanism for improving employee performance. Over 80% of the Thames water employees surveyed said that PRP was not an incentive for increased effort by employees. The amount of money employees could potentially earn as a performance payment was relatively small and it may be that employees

felt that it was insufficient incentive. However it is clear that Thames water originally intended to use PRP to manage down wage costs and were unlikely to be in a position where they would offer employees large performance payments. Essentially the contradiction inherent in both motivating employees and controlling wages meant that the PRP scheme was unlikely to achieve either of these objectives.

From Thames water's point of view it could be argued that the most important and enduring objectives they hoped to achieve were Performance Management and a more commercially orientated corporate culture. However, it seems unlikely that a PRP scheme that does not work in its own terms will operate effectively as either a Performance Management scheme or as an agent of successful cultural change. In addition, the survey evidence shows that there were a number of unintended consequences of the Thames Water PRP scheme, including an erosion of the trust between Managers and employees, which may well have undermined its effectiveness in terms of Performance Management or as an agent for bringing about cultural change.

The survey evidence shows that employees like the idea of PRP in the abstract, but do not like the practical application of PRP to them. Perhaps the problem is one of perception, employees may like the idea of PRP, assuming that they will do well from any assessment, but be alienated by a scheme which in practice gives them a lower level of assessment than

they believe that they deserve. It is difficult to see how such problems of perception can be addressed. The evidence from the Thames water case study suggests that Thames Water would be well advised to focus their efforts on making the scheme more transparent and fair, at least in the eyes of their employees. To be more effective the scheme also needs to be properly managed so that employees get supportive feedback on their performance, a large number of employees reported receiving no formal feedback on their performance. Even if Thames Water addressed these issues there still remains a fundamental problem with the detrimental effect that PRP appears to be having on employees' trust in their managers. Some commentators have suggested that trust is a prerequisite to the effective operation of PRP (Lawler 1981, and Siegall & Worth 2001) in which case the damage to the relationship between the employee and manager done by PRP may also make the PRP scheme less effective as a motivator. But from the Thames Water's perspective the more worrying issue may be the effect this erosion of trust has on Performance Management and corporate culture, given that Thames Water does not believe that PRP is an effective motivator.

Thames Water continues to use PRP and there is no evidence to suggest that they will adopt a different reward system as a result of their current review of reward systems. Thames Water is aware of the concern amongst employees about PRP, both from their own survey evidence and from what employees have said to them. All of the managers

interviewed for this thesis also recognised that PRP was not effective as a motivator for employees. So why do Thames Water continue to use PRP? Thames Water believed that PRP would support Performance Management and help make the company's corporate culture more commercially focused. This thesis suggests that PRP may not have been particularly effective in changing corporate culture in Thames Water. Although Thames Water appears to have given some thought to the effectiveness of PRP as a motivator it is not clear how far they have gone in assessing PRP as an instrument of Performance Management or cultural change. Thames Water's continued use of PRP may, however, also reflect the lack of alternative pay system that is as attractive as PRP to Thames Water. PRP puts performance at the heart of the employment relationship in a way that other pay systems do not. Thames Water wants to be seen as a commercially focused organisation and using PRP sends a message about the type of company Thames Water is. Perhaps the answer to the paradox between the continuing popularity of PRP and the ineffectiveness of PRP as a motivator is that it is the message that PRP sends about the company that is more important than the effectiveness of PRP in either, motivating employees, Performance Management or bringing about a change in corporate culture.

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## APPENDIX A.i

Sources for this research included a survey of Thames Water employees in receipt of PRP and structured interviews with some of those managers responsible for the introduction of PRP to Thames Water. Other source material included internal documentation and Thames Water's published Annual Report.

### The Survey

There was some difficulty at first over obtaining access to Thames Water managers and employees for this thesis. Thames Water initially refused to co-operate with the research for this thesis. Nevertheless it was decided to go ahead with the research and a survey of white-collar employees, who were members of UNISON and who were receiving PRP, was conducted in May 1995. Although Thames Water would not agree to actively co-operate with the research, they did not seek to stop or hinder it either. This meant that it was possible to conduct a survey of UNISON white-collar members who were in receipt of PRP using the internal mail, thanks to the co-operation of the Thames Water Branch of UNISON. The questionnaire comprised a number of closed questions, where the responses could be coded and turned into quantitative information and an open question about PRP, which provided some qualitative information.

The survey questionnaire was distributed with the assistance of UNISON to 1,500 white-collar members of UNISON working for Thames Water at the end of March 1995. The Thames Water Branch of UNISON maintains a computerised record of their membership. The branch distributed 1,500 questionnaires to the white-collar members on their register. Thames Water had approximately 3,000 white-collar employees in 1995, so questionnaires were distributed to about 50% of the white-collar workforce. Thames Water were in the process of introducing PRP for manual workers, at the time of the survey, but as the scheme had not been in place long enough for manual employees to have fully experienced its operation, only white collar employees were surveyed.

There were 489 usable questionnaires returned a response rate of about 33%. That response rate is not as high as either that achieved by Thompson (1993), which varied over three organisations between 54% and 82%, or that obtained by Marsden and Richardson (1991), of 60% amongst Revenue staff. However, it is worth noting that both those surveys were carried out with the support of the employers. When Marsden and French (1998) conducted a further survey of Revenue staff, without the employer's assistance, they obtained a usable response rate of 30%. Oppenheim (1992) says that sponsorship of a survey by a relevant agency can be powerful tool in increasing response rates. It seems likely that the surveys conducted by Thompson, and Marsden and

Richardson, were able to obtain a higher response rate because of the employer's sponsorship of those survey. Unfortunately, Thames Water declined the invitation to co-operate with the thesis survey.

The majority of the respondents were men (71%). About 38% of the white collar staff covered by PRP in Thames were women in 1993, which suggests that there was a slightly higher response rate from men to the questionnaire. Most of the respondents were between 25 and 55 years of age. Only 15 were under 25, and only 36 were over 55. The age profile may reflect the process of downsizing in Thames Water, where there has been little recruitment in some areas to bring in younger employees and, at the other end of the scale, a loss of older employees, who have left taking advantage of the early retirement provisions in the company's redundancy scheme. The number of years of service with Thames Water ranged from less than a year to 36 years, and the average length of service was 13.79 years (st. dev 8.6). There were only 18 part time workers amongst the respondents. Most of the respondents were in the job grades c to g.

### Questionnaire Design

The Questionnaire comprised a number of distinct Sections, each one of which was concerned with a particular aspect of employment. Section A asked respondents for their views about PRP in general, as opposed to

their views about the Thames Water PRP scheme in particular. Section B contains Cook and Wall's (1980) commitment Questionnaire, which is concerned with the employee's commitment to their employer.

Thames Water's PRP scheme requires managers to set employees' performance targets at their Staff Performance Review (SPR), and performance is then judged, for PRP purposes, against those performance targets. Goal setting theory predicts that the goal setting process, as in the case of SPR, will be of critical importance in determining employee motivation. Questions about the SPR were set out in Sections C and D of the questionnaire. It has also been hypothesised that feedback will play an important part in determining employee motivation, and Section E contains a number of questions about feedback.

Expectancy theory, on the other hand, predicts that it is the relationship between performance and reward that will determine employee motivation. Respondents were asked in Section F how they felt about their latest assessment, and the extent to which it accurately reflected their effort. The replies to questions about the relationship between assessment and effort are also relevant to equity issues.

The motivational effectiveness of the Thames Water PRP scheme needs to be judged on the basis of the outcomes for the organisation. It is

notoriously difficult to measure performance outcomes of PRP without conflating the direct effects of PRP with the impact of other variables, such as the impact of market changes. Two different approaches have been used in this research. Firstly self-reporting of the motivational effectiveness of PRP; the relevant questions were set out in Section H of the questionnaire. Secondly, employees were asked in Section G, what their last performance rating was and where they stood on the salary scale. On the face of it, this is a more robust measure of performance than self-reporting, because it gives a third party assessment of the individual's performance. However, this thesis is concerned with motivation not performance. Performance is the product of ability and effort on a particular task. Information about the performance rating and salary does not distinguish effort from ability. Consequently, an employee could receive a better performance rating, when compared to another employee, even though they are not trying as hard as that other employee, simply because they are more able. The self-report of the motivational effectiveness of PRP is therefore more relevant to this research, but the performance assessment's and salary are none the less interesting.

Section I of the questionnaire is concerned with organisational changes over the last two or three years. The employee's perceptions about changes in the organisation over the last two to three years helps to give an insight into cultural change in the organisation. The effectiveness of

PRP as a motivator for individuals can then be compared with the extent to which they believe that there has been cultural change over the last two to three years, to see how far PRP and cultural change are linked. The evidence from the qualitative research suggests that Thames Water saw PRP as a key mechanism for achieving cultural change in the organisation.

Section J asks for biographical detail. And Section K of the questionnaire is an open question inviting respondents to say something about their experience of PRP. A copy of the Questionnaire is at Appendix A. Each of the items within the questionnaire has been identified firstly by the letter indicating which Section of the questionnaire it belongs to and then by sequential numbering within in each Section.

## Structured Interviews

There was some difficulty at first over obtaining access to Thames Water managers and employees for this thesis. Thames Water initially refused to co-operate with the research for this thesis. One of the Thames Water personnel managers supplied additional qualitative information on the PRP scheme prior to the survey being conducted, on the understanding that his name would not be quoted in the thesis. Even though Thames Water has subsequently decided to co-operate with the research for this thesis, the personnel manager's request for anonymity has been respected, and the information supplied has been attributed to a 'Personnel Manager'

After Thames Water agreed to assist with the research, it was possible to interview a number of the key players from the company. Structured interviews were conducted with Steve Jay, Derek McManus and Malcolm Carr. Each of the interviews followed a format similar to that used with the Personnel Manager, each interviewee was asked their history with Thames Water, about the lead up to the introduction of PRP, the reasons for the introduction of PRP, and for their views on the outcomes from PRP. The interviews were recorded and transcribed and each of the interviewees was given an opportunity to correct and amend the record of their interview. Steve Jay had worked for Unilever as a personnel

manager for ten years, after completing a postgraduate course in Personnel Management and Industrial Relations at the LSE. He joined Thames Water in about 1989 and occupied a number of important personnel posts, including that of Employee Relations Manager and Head of Personnel for the Utility, throughout the period during which PRP was being introduced. He subsequently became Personnel Director for Thames Water PLC. He has now left the company. Derek McManus transferred in to Thames Water Authority when it was formed in 1974, and became Employers Side Secretary of the three negotiating machines in Thames Water in about 1987. Derek McManus took over as Employee Relations Manager from Steve Jay. He has since left the company. Malcolm Carr has been with Thames Water for about 20 years and has worked in employee relations since about 1990. He took over from Derek McManus as Employee Relations Manager and Employer's Side Secretary on the Company pay and conditions negotiating machine in 1997.

Julia Cherrett, the European Director of Human Resources, was also interviewed. She had succeeded Derek McManus and before becoming European Director of human Resources. Julia Cherrett was able to give an update on Thames Water's approach to PRP and was asked to comment on the first draft of the final Chapter.

Thames Water have recently initiated a review of their reward system, and although the company is not intending to replace the PRP pay

system in Thames Water, some of the preparatory work for the review provides an interesting if limited update on employee views regarding PRP. Thames Water established 12 focus groups from across all business units encompassing all grades of employees (the survey conducted for this thesis excluded manual workers); no notes were kept of who attended or of who said what in order to give a degree of anonymity. All views were included in the report prepared of the focus group work, the Reward Framework Project Focus Group Feedback Report (October 2001).

#### Documentary Sources

The following documents produced by Thames Water were relied on:

**Thames Water (1991)** 'Annual Report & Accounts 1990/91' - Reading: Thames Water PLC

**Thames Water (1991)** 'Pay and Conditions Statement 91/92' - Thames Water Company Council papers

**Thames Water (1992)** 'Thames Water Company Council Minutes 25/5/1992' - Thames Water Company Council papers

**Thames Water (1994)** 'Annual Report & Accounts 1993/94' - Reading: Thames Water PLC

**Thames Water (1994)** 'JET Guidelines for Managers' - Reading: Thames Water PLC

**Thames Water (1994)** 'Presentation to the Thames Water Company Council' – Thames Water Company Council papers

**Thames Water (1994)** 'Viewfinder 94' – International Survey Research Limited - Reading: Thames Water PLC

<b>Thames Water (1995)</b>	'Annual Report & Accounts 1994/95' - Reading: Thames Water PLC
<b>Thames Water (1995)</b>	'Assessor Training Manual' - Reading: Thames Water PLC
<b>Thames Water ( circa 1995)</b>	'Performance Related Pay – A Guide for Employees' - Reading: Thames Water PLC
<b>Thames Water (1999)</b>	'Annual Report & Accounts 1998/99' - Reading: Thames Water PLC
<b>Thames Water (2001)</b>	'The Reward Framework Project Focus Group Feedback Report' (October 2001).- Internal Thames Water Report

## APPENDIX A.ii

**The London School of Economics and Political Science.**  
Houghton Street,  
London WC2A 2AE

Qu1.vii - 3 95

**SURVEY  
QUESTIONNAIRE**

**This Questionnaire has been sent to you as part of a Survey being conducted for academic research at the London School of Economics.**

- The Survey is designed to examine the motivational effectiveness of linking pay to performance.
- All answers to the questionnaire are anonymous and will be treated in strict confidence; they will only be used for the purposes of overall analysis of the attitudes of employees.
- The survey is being conducted with the agreement and assistance of the Thames Water No.1 Branch of UNISON.
- Please return the completed Questionnaire to:  
Jane Carless, or UNISON,  
4th Floor, FREEPOST (RG3143),  
Nugent House. Reading RG1 1BR  
In the attached envelope
- Thank you for your help. With the Questionnaire.

## Section A

In this section you are asked for your views on the use of performance related pay by employers in general. This section deals the general principles underlying performance related pay and not the specific scheme which applies in your organisation.

**Do you agree with the following statements? Please tick the appropriate box.**

	agree strongly	agree	not sure	disagree	disagree strongly
In general relating pay to performance is a fair way of paying staff. <sup>a1</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Employers benefit from having a well designed performance related pay scheme, because employees work harder. <sup>a2</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Employers run the risk that if they use performance related pay it will damage teamwork. <sup>a3</sup>	<input type="checkbox"/> 1	<input type="checkbox"/> 2	<input type="checkbox"/> 3	<input type="checkbox"/> 4	<input type="checkbox"/> 5
Performance related pay can easily damage staff morale. <sup>a4</sup>	<input type="checkbox"/> 1	<input type="checkbox"/> 2	<input type="checkbox"/> 3	<input type="checkbox"/> 4	<input type="checkbox"/> 5

## Section B

**In this section we look at what it means to you being a member of your organisation. Some people feel themselves to be just an employee, there to do a job of work, while others feel more personally involved in the organisation they work for. The following items express what people might feel about themselves as members of their organisation.**

**Please tick the appropriate box.**

I am quite proud to be able to tell people who it is I work for. <sup>b1</sup>	No, I disagree strongly	<input type="checkbox"/> 1
	No, I disagree quite a lot	<input type="checkbox"/> 2
	No, I disagree just a little	<input type="checkbox"/> 3
	I am not sure	<input type="checkbox"/> 4
	Yes, I agree just a little	<input type="checkbox"/> 5
	Yes, I agree quite a lot	<input type="checkbox"/> 6
	Yes, I strongly agree	<input type="checkbox"/> 7

I sometimes feel like leaving this employer for good. <sup>b2</sup>	No, I disagree strongly	<input type="checkbox"/> <sup>1</sup>
	No, I disagree quite a lot	<input type="checkbox"/> <sup>2</sup>
	No, I disagree just a little	<input type="checkbox"/> <sup>3</sup>
	I am not sure	<input type="checkbox"/> <sup>4</sup>
	Yes, I agree just a little	<input type="checkbox"/> <sup>5</sup>
	Yes, I agree quite a lot	<input type="checkbox"/> <sup>6</sup>
	Yes, I strongly agree	<input type="checkbox"/> <sup>7</sup>
I am not willing to put myself out just to help the organisation. <sup>b3</sup>	No, I disagree strongly	<input type="checkbox"/> <sup>1</sup>
	No, I disagree quite a lot	<input type="checkbox"/> <sup>2</sup>
	No, I disagree just a little	<input type="checkbox"/> <sup>3</sup>
	I am not sure	<input type="checkbox"/> <sup>4</sup>
	Yes, I agree just a little	<input type="checkbox"/> <sup>5</sup>
	Yes, I agree quite a lot	<input type="checkbox"/> <sup>6</sup>
	Yes, I strongly agree	<input type="checkbox"/> <sup>7</sup>
Even if the firm were not doing too well financially, I would be reluctant to change to another employer. <sup>b4</sup>	No, I disagree strongly	<input type="checkbox"/> <sup>1</sup>
	No, I disagree quite a lot	<input type="checkbox"/> <sup>2</sup>
	No, I disagree just a little	<input type="checkbox"/> <sup>3</sup>
	I am not sure	<input type="checkbox"/> <sup>4</sup>
	Yes, I agree just a little	<input type="checkbox"/> <sup>5</sup>
	Yes, I agree quite a lot	<input type="checkbox"/> <sup>6</sup>
	Yes, I strongly agree	<input type="checkbox"/> <sup>7</sup>
I feel myself to be part of the organisation. <sup>b5</sup>	No, I disagree strongly	<input type="checkbox"/> <sup>1</sup>
	No, I disagree quite a lot	<input type="checkbox"/> <sup>2</sup>
	No, I disagree just a little	<input type="checkbox"/> <sup>3</sup>
	I am not sure	<input type="checkbox"/> <sup>4</sup>
	Yes, I agree just a little	<input type="checkbox"/> <sup>5</sup>
	Yes, I agree quite a lot	<input type="checkbox"/> <sup>6</sup>
	Yes, I strongly agree	<input type="checkbox"/> <sup>7</sup>

In my work I like to feel I am making some effort, not just for myself but for the organisation as well.	<sup>b6</sup>	No, I disagree strongly	<input type="checkbox"/> <sub>1</sub>
		No, I disagree quite a lot	<input type="checkbox"/> <sub>2</sub>
		No, I disagree just a little	<input type="checkbox"/> <sub>3</sub>
		I am not sure	<input type="checkbox"/> <sub>4</sub>
		Yes, I agree just a little	<input type="checkbox"/> <sub>5</sub>
		Yes, I agree quite a lot	<input type="checkbox"/> <sub>6</sub>
		Yes, I strongly agree	<input type="checkbox"/> <sub>7</sub>
The offer of a bit more money with another employer would not seriously make me think of changing my job.	<sup>b7</sup>	No, I disagree strongly	<input type="checkbox"/> <sub>1</sub>
		No, I disagree quite a lot	<input type="checkbox"/> <sub>2</sub>
		No, I disagree just a little	<input type="checkbox"/> <sub>3</sub>
		I am not sure	<input type="checkbox"/> <sub>4</sub>
		Yes, I agree just a little	<input type="checkbox"/> <sub>5</sub>
		Yes, I agree quite a lot	<input type="checkbox"/> <sub>6</sub>
		Yes, I strongly agree	<input type="checkbox"/> <sub>7</sub>
I would not recommend a close friend to join our staff.	<sup>b8</sup>	No, I disagree strongly	<input type="checkbox"/> <sub>1</sub>
		No, I disagree quite a lot	<input type="checkbox"/> <sub>2</sub>
		No, I disagree just a little	<input type="checkbox"/> <sub>3</sub>
		I am not sure	<input type="checkbox"/> <sub>4</sub>
		Yes, I agree just a little	<input type="checkbox"/> <sub>5</sub>
		Yes, I agree quite a lot	<input type="checkbox"/> <sub>6</sub>
		Yes, I strongly agree	<input type="checkbox"/> <sub>7</sub>
To know that my own work had made a contribution to the good of the organisation would please me.	<sup>b9</sup>	No, I disagree strongly	<input type="checkbox"/> <sub>1</sub>
		No, I disagree quite a lot	<input type="checkbox"/> <sub>2</sub>
		No, I disagree just a little	<input type="checkbox"/> <sub>3</sub>
		I am not sure	<input type="checkbox"/> <sub>4</sub>
		Yes, I agree just a little	<input type="checkbox"/> <sub>5</sub>
		Yes, I agree quite a lot	<input type="checkbox"/> <sub>6</sub>
		Yes, I strongly agree	<input type="checkbox"/> <sub>7</sub>

## Section C

**This section asks about your Staff Performance Review. You should have been given a copy of your last Staff Performance Review form.**

How many Staff Performance Review interviews have you had in the last twelve months?.....   <sub>c1</sub>

**Please answer the following questions using information from the last Staff Performance Review you had, even if that Staff Performance Review took place more than twelve months ago.**

How many Objectives were set for you at your last Staff Performance Review?.....   <sub>c2</sub>

Was it clear to you at the Staff Performance Review how you could achieve the Objectives which had been set?

very clear.....	<input type="checkbox"/> <sub>5</sub>
quite clear.....	<input type="checkbox"/> <sub>4</sub>
not sure.....	<input type="checkbox"/> <sub>3</sub>
quite unclear.....	<input type="checkbox"/> <sub>2</sub>
very unclear.....	<input type="checkbox"/> <sub>1</sub> <sub>c3</sub>

### **a) Quantifiable Objectives:**

How many of the Objectives which were set for you related to the achievement of quantifiable targets?.....   <sub>c4</sub>

How specific were the quantifiable Objectives that were set for you at your last Staff Performance Review?

very specific.....	.. <input type="checkbox"/> <sub>5</sub>
quite specific.....	<input type="checkbox"/> <sub>4</sub>
not sure.....	<input type="checkbox"/> <sub>3</sub>
quite general.....	<input type="checkbox"/> <sub>2</sub>
very general.....	<input type="checkbox"/> <sub>1</sub> <sub>c5</sub>

### **b) Qualitative Objectives:**

How many of the Objectives which were set for you relate to the achievement of targets of a qualitative nature, that is relate to how well work is done?.....   <sub>c6</sub>

How specific were the qualitative Objectives that were set for you at your last Staff Performance Review?

very specific.....	<input type="checkbox"/> 5
quite specific.....	<input type="checkbox"/> 4
not sure.....	<input type="checkbox"/> 3
quite general.....	<input type="checkbox"/> 2
very general.....	<input type="checkbox"/> 1 c7

How long did your last Staff Performance Review interview last

less than 30 minutes	<input type="checkbox"/> 1
30 - 59 minutes	<input type="checkbox"/> 2
1 - 2 hours	<input type="checkbox"/> 3
over 2 hours	<input type="checkbox"/> 4 c8

Did your last Staff Performance Review lead to any of the following outcomes or activities?

the offer of training/development.....	<input type="checkbox"/> 4
a dispute over the interview record.....	<input type="checkbox"/> 3
further counselling regarding your performance.....	<input type="checkbox"/> 2
none of the above.....	<input type="checkbox"/> 1 c9

If you were offered further training or development as a result of the last Staff Performance Review has that training or development taken place?

Yes  2 No  1 c10

## Section D

**You are now asked how you feel about the objectives that were set for you at the last Staff Performance Review.**

**Do you agree with the following statements? Please tick the appropriate box.**

	agree strongly	agree	not sure	disagree	disagree strongly
--	-------------------	-------	----------	----------	----------------------

Your manager takes your Staff Performance Review very seriously. <sup>d1</sup>

5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
----------------------------	----------------------------	----------------------------	----------------------------	----------------------------

You had the right amount of influence over setting the Objectives that were set in your Staff Performance Review. <sup>d2</sup>

5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
----------------------------	----------------------------	----------------------------	----------------------------	----------------------------

The Objectives which were set for you at the Staff Performance Review are relevant to your job. <sup>d3</sup>

5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
----------------------------	----------------------------	----------------------------	----------------------------	----------------------------

		agree strongly	agree	not sure	disagree	disagree strongly
You have all the skills and ability necessary to perform the Objectives that have been set for you in the Staff Performance Review.	d4	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
It will be necessary to increase your effort at work to achieve the Objectives that have been set for you.	d5	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
You are personally committed to achieving the Objectives that were set for you at the Staff Performance Review.	d6	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
It will be difficult to achieve the Objectives set at the Staff Performance Review.	d7	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
It would improve your job security if you achieved the Objectives set for you.	d8	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
It would improve the prospect of future pay increases if you achieved the goals set for you.	d9	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
It would be advantageous for your promotion prospects if you achieved the goals set for you.	d10	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
Attaining the goals set for you would increase your sense of self confidence at work.	d11	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>

## Section E

**These questions are concerned with feedback, that is what you have been told about how well or badly you are doing at work.**

**Do you agree with the following statements? Please tick the appropriate box.**

	agree strongly	agree	not sure	disagree	disagree strongly
Your manager is bad at giving you feedback on your performance. <sup>e1</sup>	<input type="checkbox"/> 1	<input type="checkbox"/> 2	<input type="checkbox"/> 3	<input type="checkbox"/> 4	<input type="checkbox"/> 5

You receive frequent informal feedback from your manager regarding your progress towards the Objectives set at the Staff Performance Review. <sup>e2</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
--	----------------------------	----------------------------	----------------------------	----------------------------	----------------------------

The feedback you have had has <u>not</u> been encouraging. <sup>e3</sup>	<input type="checkbox"/> 1	<input type="checkbox"/> 2	<input type="checkbox"/> 3	<input type="checkbox"/> 4	<input type="checkbox"/> 5
--	----------------------------	----------------------------	----------------------------	----------------------------	----------------------------

You feel a sense of achievement when you receive feedback to the effect that you are on target to attain the Objectives set for you. <sup>e4</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
--	----------------------------	----------------------------	----------------------------	----------------------------	----------------------------

Feedback is important in helping you to attain your job Objectives. <sup>e5</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
---	----------------------------	----------------------------	----------------------------	----------------------------	----------------------------

How many times have you received informal feedback on your performance during the last year?.....   <sup>e6</sup>

## Section F

**The next set of questions are concerned with your feelings about the assessment of your performance for the Performance Related Pay scheme.**

How well do you understand your employers performance related pay scheme?	very well.....	<input type="checkbox"/> 5
	quite well.....	<input type="checkbox"/> 4
	not sure.....	<input type="checkbox"/> 3
	only in part.....	<input type="checkbox"/> 2
	not at all.....	<input type="checkbox"/> 1

**Do you agree with the following statements? Please tick the appropriate box.**

	agree strongly	agree	not sure	disagree	disagree strongly
1. Performance related pay has eroded some of the trust which existed between you and the manager responsible for assessing you. <sup>f2</sup>	1 <input type="checkbox"/>	2 <input type="checkbox"/>	3 <input type="checkbox"/>	4 <input type="checkbox"/>	5 <input type="checkbox"/>
Your manager knows enough about you and your work to be able to assess your performance accurately. <sup>f3</sup>	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
Your most recent assessment was a fair reflection of your performance. <sup>f4</sup>	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
You have to keep on the 'right side' of your manager to get a good assessment rating. <sup>f5</sup>	1 <input type="checkbox"/>	2 <input type="checkbox"/>	3 <input type="checkbox"/>	4 <input type="checkbox"/>	5 <input type="checkbox"/>
The performance criteria against which you were assessed were fair. <sup>f6</sup>	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
Staff are often denied the assessment they deserve because there is a quota system for assessments which predetermines the number of people in each assessment level. <sup>f7</sup>	1 <input type="checkbox"/>	2 <input type="checkbox"/>	3 <input type="checkbox"/>	4 <input type="checkbox"/>	5 <input type="checkbox"/>
The trouble with performance pay is that a good assessment by the reporting officer is too often overruled by someone higher up. <sup>f8</sup>	1 <input type="checkbox"/>	2 <input type="checkbox"/>	3 <input type="checkbox"/>	4 <input type="checkbox"/>	5 <input type="checkbox"/>
It is easier to get a higher performance assessment in other parts of the organisation. <sup>f9</sup>	1 <input type="checkbox"/>	2 <input type="checkbox"/>	3 <input type="checkbox"/>	4 <input type="checkbox"/>	5 <input type="checkbox"/>

	agree strongly	agree	not sure	disagree	disagree strongly
If you achieve the goals set for you at the last Staff Performance Review it is likely that you will receive a better performance assessment. <sup>f10</sup>	5 <input type="checkbox"/>	4 <input type="checkbox"/>	3 <input type="checkbox"/>	2 <input type="checkbox"/>	1 <input type="checkbox"/>
You do less well out of performance pay than some of your colleagues. <sup>f11</sup>	1 <input type="checkbox"/>	2 <input type="checkbox"/>	3 <input type="checkbox"/>	4 <input type="checkbox"/>	5 <input type="checkbox"/>
You are poorly paid for the work that you do. <sup>f12</sup>	1 <input type="checkbox"/>	2 <input type="checkbox"/>	3 <input type="checkbox"/>	4 <input type="checkbox"/>	5 <input type="checkbox"/>

## Section G

**In this section you are asked about your last performance assessment for Performance Related Pay. You should have details of your last overall assessment and your resultant position in relation to Scale Salary.**

What was your last overall assessment?	Excellent.....	<input type="checkbox"/> 6
	Very Good.....	<input type="checkbox"/> 5
	Fully Acceptable.....	<input type="checkbox"/> 4
	Needs Improvement....	<input type="checkbox"/> 3
	Unacceptable.....	<input type="checkbox"/> 2
	Not Known.....	<input type="checkbox"/> 1G1
What percentage of Scale Salary have you been paid since the last assessment?	over 115%.....	<input type="checkbox"/> 7
	107.6% - 115%.....	<input type="checkbox"/> 6
	101% - 107.5%.....	<input type="checkbox"/> 5
	Scale Salary.....	<input type="checkbox"/> 4
	92.6% - 99%.....	<input type="checkbox"/> 3
	85% - 92.5%.....	<input type="checkbox"/> 2
	less than 85%.....	<input type="checkbox"/> 1g2

## Section H

**In this part of the questionnaire you are asked how you feel about Performance Related Pay in Thames Water.**

Do you believe that by trying harder to achieve <u>the Objectives that are set for you at the Staff Performance Review</u> it would be possible to increase the amount of pay that you earn?	yes....	<input type="checkbox"/> 3
	no...	<input type="checkbox"/> 2
	Do not know.	<input type="checkbox"/> 1h1

Do you believe that by trying harder to improve your performance in relation to the Performance Criteria it would be possible to increase the amount of pay that you earn?

yes...  <sub>3</sub>  
no ...  <sub>2</sub>  
Do not know.  <sub>1 h2</sub>

**Do you agree with the following statements? Please tick the appropriate box.**

	agree strongly	agree	not sure	disagree	disagree strongly
It is important for your <sup>h3</sup> sense of self confidence at work for you to get a performance payment.	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Performance related pay has encouraged you to work harder. <sup>h4</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Performance related pay has generally encouraged other employees at your work to work harder. <sup>h5</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
You personally have been paid more fairly as a result of the introduction of performance related pay. <sup>h6</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Hard work is adequately rewarded by your employer. <sup>h7</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Performance related pay has had no effect on the quality of your work because it was already at the appropriate standard. <sup>h8</sup>	<input type="checkbox"/> 1	<input type="checkbox"/> 2	<input type="checkbox"/> 3	<input type="checkbox"/> 4	<input type="checkbox"/> 5
The existence of <sup>h9</sup> performance related pay has made you willing to improve the <u>quality</u> of your work.	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
The existence of <sup>h10</sup> performance related pay has made you willing to improve the <u>quantity</u> of your work.	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1

	agree strongly	agree	not sure	disagree	disagree strongly
h11 Performance related pay has to be substantially increased before it will improve performance.	5□	4□	3□	2□	1□
h12 Performance related pay has given you the incentive to work beyond the requirements of your job.	5□	4□	3□	2□	1□
h13 Performance related pay has encouraged you to give sustained performance at work.	5□	4□	3□	2□	1□
h14 Performance related pay has given you a greater incentive to get your work priorities right.	5□	4□	3□	2□	1□
h15 Performance related pay has caused jealousies between staff.	1□	2□	3□	4□	5□

## Section I

**This section asks about some of the other things that have been happening at work in the last two or three years.**

**Do you agree with the following statements? Please tick the appropriate box.**

	agree strongly	agree	not sure	disagree	disagree strongly
11 The core values which are promoted by the organisation are now supported by a larger proportion of the workforce than they used to be.	5□	4□	3□	2□	1□
12 The pressure on employees to work harder has increased substantially.	5□	4□	3□	2□	1□
13 There are unlikely to be any further significant reductions in the size of the workforce.	1□	2□	3□	4□	5□

		agree strongly	agree	not sure	disagree	disagree strongly
There is less of a feeling of 'us' and 'them' between employees and management than there used to be.	<sup>14</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Employees are more likely to be treated as individuals by the organisation than they were in the past.	<sup>15</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Employees feel more confident about being flexible in their approach to changes in their work than in the past.	<sup>17</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Communication between the management and employees is generally improving.	<sup>18</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Management generally are more inclined to listen to the views of employees than they used to be.	<sup>19</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
Trade unions have less an important role to play in protecting employees than they used to have.	<sup>110</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1
It seems inevitable that performance related pay will lead to an increasingly individualised approach to the employment relationship by your employer.	<sup>111</sup>	<input type="checkbox"/> 5	<input type="checkbox"/> 4	<input type="checkbox"/> 3	<input type="checkbox"/> 2	<input type="checkbox"/> 1

## Section J

**This section asks for some information about you.**

How long have you been working for the company and its predecessors?  
.....   <sub>11</sub>

[Please state the number of completed years.]

Which of the following age categories do you fall into:

- under 25...  1
- 25 to 34...  2
- 35 to 44...  3
- 45 to 55...  4
- over 55...  5 <sub>12</sub>

Are you?

Male  1 or Female  2 <sub>3</sub>

Are you? full time.....  2  
part time....  1 <sub>4</sub>

What grade are you on?

Band.....  <sub>5</sub>

### Section K

**Finally, this section gives you the opportunity to make any comment you want to about your experience of Performance Related Pay.**

There are a lot of different claims made for performance related pay, for instance it is sometimes claimed that performance related pay motivates employees to work harder, but on the other hand it is also said that performance related pay may cause jealousies between staff and damages teamwork, could you summarise your own experience of performance related pay in Thames Water in your own words?

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**Thank you for your assistance in completing this questionnaire.**

**APPENDIX B**  
**Chapter 8**  
Outcome Frequencies

1/5

F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
i	"In general relating pay to performance is a fair way of paying staff"	8.2%	58.4%	15%	13.3%	4.7%
ii	"You personally have been paid more fairly as a result of the introduction of performance related pay"	0%	10.7%	16.3%	45.5%	26.6%
iii	"Hard work is adequately rewarded by your employer."	0.9%	6.9%	10.7%	52.8%	27.9%
iv	"Performance related pay has encouraged you to work harder."	3%	14.6%	12.4%	49.8%	20.2%
v	"Performance related pay has given you the incentive to work beyond the requirements of your job."	1.3%	7.3%	9%	55.8%	25.8%

**APPENDIX B**  
**Chapter 8**  
**Outcome Frequencies**

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F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
vi	"Performance related pay has encouraged you to give sustained performance at work."	0.4%	14.6%	9.4%	52.4%	22.3%
vii	Performance related pay has generally encouraged other employees at your work to work harder.	0.9%	6.9%	27.5%	46.4%	18%
viii	"The existence of performance related pay has made you willing to improve the <u>quality</u> of your work."	0.9%	15%	12%	53.2%	18.5%
ix	"The existence of performance related pay has made you willing to improve the <u>quantity</u> of your work."	0.9%	17.6%	10.3%	52.4%	18.5%
x	"Performance related pay has given you a greater incentive to get your work priorities right."	0.9%	16.7%	8.6%	51.1%	22.3%

**APPENDIX B**  
**Chapter 8**  
**Outcome Frequencies**

F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
xi	"The pressure on employees to work harder has increased substantially."	42.5%	49.8%	3.9%	2.6%	0.9%
xii	"There are unlikely to be any further significant reductions in the size of the workforce."	0.9%	3.4%	19.3%	45.1%	30.9%
xiii	"Communication between management and employees is generally improving."	0.9%	29.2%	13.7%	34.3%	21%
xiv	"Management generally are more inclined to listen to the views of employees than they used to be."	1.3%	27.5%	16.7%	31.8%	22.3%
xv	"The core values which are promoted by the organisation are now supported by a larger proportion of the workforce than they used to be."	0.9%	25.3%	35.2%	28.8%	9%

**APPENDIX B**  
**Chapter 8**  
**Outcome Frequencies**

F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
xvi	"There is less of a feeling of 'us' and 'them' between employees and management than there used to be."	0.9%	11.2%	9.9%	47.2%	30.5%
xvii	"Employees are more likely to be treated as individuals by the organisation than they were in the past."	2.1%	11.6%	14.2%	39.9%	31.8%
xviii	"It seems inevitable that performance related pay will lead to an increasingly individualised approach to the employment relationship by your employer."	9%	44.2%	30.9%	12%	3%
xix	"Employees feel more confident about being flexible in their approach to changes in their work than in the past."	2.1%	37.8%	18.9%	27%	13.7%
xx	"Trade unions have a less important role to play in protecting employees than they used to have."	13.7%	36.5%	6.9%	25.8%	16.7%

**APPENDIX B**  
**Chapter 8**  
**Outcome Frequencies**

F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
xxi	"Employers run the risk that if they use performance related pay it will damage teamwork."	2.1%	23.6%	16.7%	41.2%	15.5%
xxii	"Performance related pay has caused jealousies between staff."	2.1%	14.6%	23.2%	36.5%	23.2%
xxiii	"Performance related pay has eroded some of the trust which existed between you and the manager responsible for assessing you."	15.9%	27.9%	18.9%	32.6%	3%
xxiv	"You have to keep on the 'right side' of your manager to get a good assessment rating."	17.6%	30.9%	21%	25.8%	3.9%

**APPENDIX C**  
**Chapter 9**  
**Process Frequencies**

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F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
i	'Your manager takes your Staff Performance Review seriously.'	15%	39.1%	16.3%	15.5%	10.3%
ii	'You had the right amount of influence over setting the Objectives that were set in your Staff Performance Review.'	7.3	43.3%	15%	22.3%	8.6%
iii	'The Objectives which were set for you at the Staff Performance Review are relevant to your job.'	15.5%	67%	5.2%	6.9%	1.7%
iv	'You are personally committed to achieving the Objectives that were set for you at the Staff Performance Review.'	21.5%	54.9%	8.6%	8.6%	2.6%
v	'It would improve the prospects of future pay increases if you achieved the goals set for you.'	6.4%	21%	15.9%	30.5%	24.3%

**APPENDIX C**  
**Chapter 9**  
**Process Frequencies**

F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
vi	'You have all the skills and ability necessary to perform the objectives that have been set for you.'	18.9%	58%	10.7%	7.3%	0.9%
vii	'It will be necessary to increase your effort at work to achieve the Objectives that have been set for you.'	11.2%	37.3%	17.2%	26.2%	4.3%
viii	'It would be advantageous for your promotion prospects if you achieved the goals set for you.'	4.3%	16.3%	24.5%	35.2%	15.5%
ix	'It would improve your job security if you achieved the Objectives set for you.'	6.4%	21%	15.9%	30.5%	22.3%
x	'Attaining the goals set for you would increase your sense of self confidence at work.'	14.2%	42.1%	9%	24%	6%

**APPENDIX C**  
**Chapter 9**  
**Process Frequencies**

F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
xi	'Your most recent assessment was a fair reflection of your performance.'	6.9%	52.4%	14.2%	15.9%	9.4%
xii	'You have to keep on the 'right side' of your manager to get a good assessment rating.'	17.6%	30.9%	21%	25.8%	3.9%
xiii	'The trouble with performance pay is that a good assessment by the reporting officer is too often overruled by someone higher up.'	27.5%	27%	30.5%	13.7%	1.3%
xiv	'Staff are often denied the assessment they deserve because there is a quota system for assessments which predetermines the number of people in each assessment level.'	42.9%	24%	21.9%	7.7%	3.4%

**APPENDIX C**  
**Chapter 9**  
Process Frequencies

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F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
xv	'Hard work is adequately rewarded by your employer.'	0.9%	6.9%	10.7%	52.8%	27.9%
xvi	'It is easier to get a higher performance assessment in other parts of the organisation.'	18.9%	18%	54.9%	6.9%	0.9%
xvii	'You do less well out of performance pay than some of your colleagues.'	13.7%	25.3%	34.8%	22.7%	3%
xviii	'You receive frequent informal feedback from your manager regarding your progress towards the Objectives set for you at your Staff Performance Review.'	1.7%	23.2%	9.9%	42.5%	22.3%
xix	'You feel a sense of achievement when you receive feedback to the effect that you are on target to attain the objectives set for you.'	11.2%	57.1%	12.4%	11.2%	3%

**APPENDIX C**  
Chapter 9  
Process Frequencies

F		AGREE STRONGLY	AGREE	NOT SURE	DISAGREE	DISAGREE STRONGLY
xx	'Feedback is important in helping you to attain your objectives.'	31.3%	49.4%	7.7%	8.6%	2.1%

**APPENDIX C**  
**Chapter 9**  
**Process Frequencies**

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F		AGREE	DON'T KNOW	DISAGREE
xxi	I am quite proud to be able to tell people who it is I work for. (b1)	67%	5%	29%
xxii	I feel myself to be part of the organisation. (b5)	62%	4%	34%
xxiii	I would not recommend a close friend to join our staff. (b8)	31%	14%	55%
xxiv	I sometimes feel like leaving this employer for good.	55%	5%	40%
xxv	Even if the firm were not doing too well financially. I would be reluctant to change to another employer.	47%	18%	36%
xxvi	The offer of a bit more money with another employer would not seriously make me think of changing my job.	39%	15%	47%
xxvii	I am not willing to put myself out just to help the organisation.	19%	4%	77%
xxviii	In my work I like to feel I am making some effort, not just for myself but for the organisation as well.	90%	3%	7%
xxix	bTo know that my own work had made a contribution to the organisation would please me. (b9)	94%	2%	4%

## Appendix D

### Variable Definitions

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Label	Definition	Mean
MOTIVATION	<p>Measure of the motivational effectiveness of PRP comprising seven items. <math>\alpha = .99</math></p> <p>(h13)'Performance related pay has encouraged you to give sustained Performance at work.'</p> <p>Factor Loading .86 (from factor analysis)</p> <p>(h10)'The existence of performance related pay has made you willing to improve the quantity of your work.'</p> <p>Factor Loading .82</p> <p>(h9)'The existence of performance related pay has made you willing to improve the quality of your work.'</p> <p>Factor Loading .82</p> <p>(h14)'Performance related pay has given you a greater incentive to get your work priorities right.'</p> <p>Factor Loading .82</p> <p>(h12)'Performance related pay has given you the incentive to work beyond the requirements of your job.'</p> <p>Factor Loading .82</p> <p>(h4)'Performance related pay has encouraged you to work harder.'</p> <p>Factor Loading .78</p> <p>(h5)'Performance related pay has generally encouraged other employees at your work to work harder.'</p> <p>Factor Loading .64</p> <p>Based on a five item scale where 5 = high level of motivation and 1 = low level of motivation (N = 482)</p>	2.2

## Appendix D

### Variable Definitions

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Label	Definition	Mean
INSTRVAL	<p>The instrumentality and valence comprising three items, <math>\alpha = .8</math></p> <p>(d9) 'It would improve the prospect of future pay increases if you achieved the goals set for you.'</p> <p>Factor Loading .84</p> <p>(d10) 'It would be advantageous for your promotion prospects if you achieved the goals set for you.'</p> <p>Factor Loading .80</p> <p>(d8) 'It would improve your job security if you achieved the objectives set for you.'</p> <p>Factor Loading .78</p> <p>Based on a five item scale where 5 =high level of instrumentality and valence and 1 = low level of instrumentality and valence (N=469)</p>	2.6
EXPECTANCY	<p>The expectancy of a valent outcome comprising two items. <math>\alpha = .7</math></p> <p>(h12) 'Do you believe that by trying harder to improve your Performance in relation to the Performance Criteria it would be possible to increase the amount of pay that you earn?'</p> <p>Factor Loading .83</p> <p>(h1) 'Do you believe that by trying harder to achieve the Objectives that were set for you at the Staff Performance Review it would be possible to increase the amount of pay that you earn?'</p> <p>Factor Loading .76</p> <p>Based on a five item scale where 5 =high level of expectancy and 1 = low level of expectancy (N=488)</p>	21
FAIRA	<p>The employee's feelings about the fairness of the assessment of the employee's performance by the manager comprising three items. <math>\alpha = .66</math></p> <p>(f4) 'Your most recent assessment was a fair</p>	3.23

## Appendix D

### Variable Definitions

Label	Definition	Mean
	<p>reflection of your performance.'</p> <p>Factor Loading .79</p> <p>(f3) 'Your manager knows enough about you and your work to be able to assess your performance accurately.'</p> <p>Factor Loading .58</p> <p>(f6) 'The criteria against which you were assessed were fair.'</p> <p>Factor Loading .53</p> <p>Based on a five item scale where 5 =high level of feeling the assessment was fair and 1 = low level of feeling the assessment was fair (N=476)</p>	
INTERFERA	<p>Employee's feelings about interference in the manager's assessment of the employee's performance comprising three items. <math>\alpha = .68</math></p> <p>(f8) 'The trouble with performance pay is that a good assessment by the reporting officer is too often overruled by someone higher up.'</p> <p>Factor Loading .72</p> <p>(f7) 'Staff are often denied the assessment they deserve because there is a quota system for assessments which predetermines the number of people in each assessment level.'</p> <p>Factor Loading .70</p> <p>(f9) It is easier to get a higher performance assessment in other parts of the organization</p> <p>Factor Loading .51</p> <p>Based on a five item scale where 5 =high level of feeling the assessment was not interfered with and 1 = low level of confidence that the assessment was not interfered with (N=484)</p>	2.32
GOODF	<p>The employee's feelings about feedback from their manager regarding the employee's performance comprising three items. <math>\alpha = .6</math></p>	2.9

## Appendix D

### Variable Definitions

Label	Definition	Mean
	<p>(e1) – reverse scored - 'Your manager is bad at giving you feedback on your performance.'</p> <p>Factor Loading .74</p> <p>(e2) 'You receive frequent informal feedback from your manager regarding your progress towards the Objectives set at the Staff Performance Review.'</p> <p>Factor Loading .64</p> <p>(e3) – reverse scored - 'The feedback you have had has <u>not</u> been encouraging.'</p> <p>Factor Loading .51</p> <p>Based on a five item scale where 5 = good feedback and 1 = poor feedback (N=455)</p>	
POSITIVEF	<p>A measure of the employee's need for positive feedback comprising three items. <math>\alpha = .65</math></p> <p>(e5) 'Feedback is important in helping you to attain your Objectives.'</p> <p>Factor Loading .71</p> <p>(e4) 'You feel a sense of achievement when you receive feedback to the effect that you are on target to attain the Objectives set for you.'</p> <p>Factor Loading .59</p> <p>(d11) 'Attaining the goals set for you would increase your sense of self confidence at work.'</p> <p>Factor Loading .51</p> <p>Based on a five item scale where 5 = most need for positive feedback and 1 = least (N=455)</p>	3.23
DIFFICULTG	<p>The employee's perception of goal difficulty comprising two items. <math>\alpha = .58</math></p> <p>(d5) 'It will be necessary to increase your effort at work to achieve the objectives which</p>	3.03

## Appendix D

### Variable Definitions

Label	Definition	Mean
	<p>have been set for you.'</p> <p>Factor Loading .76</p> <p>(d7) 'It will be difficult to achieve the objectives set at the Staff Performance Review.'</p> <p>Factor Loading .64</p> <p>Based on a five item scale where 5 = most difficult and 1 = least (N=463)</p>	
SPECIFICG	<p>Goal specificity comprising three items. <math>\alpha = .82</math></p> <p>(c7) 'How specific were the qualitative Objectives that were set for you at your last Staff Performance Review?'</p> <p>Factor Loading .84</p> <p>(c5) 'How specific were the quantifiable Objectives that were set for you at your last Staff Performance Review?'</p> <p>Factor Loading .80</p> <p>(c3) 'Was it clear to you at the Staff Performance Review how you could achieve the Objectives which had been set?'</p> <p>Factor Loading .67</p> <p>Based on a five item scale where 5 = most specific and 1 = least (N=380)</p>	3.42
RELEVANTG	<p>A measure of the employee's perception of goal appropriateness comprising three items. <math>\alpha = .56</math></p> <p>(d3) 'The Objectives which were set for you at the Staff Performance Review are relevant to your job.'</p> <p>Factor Loading .76</p> <p>(d2) 'You had the right amount of influence over setting the Objectives that were set for you in your Staff</p>	3.7

## Appendix D

### Variable Definitions

Label	Definition	Mean
	Performance Review.'	
	Factor Loading .68	
	(d4)'You have the skills and ability necessary to perform the objectives that have been set for you in the staff performance review.'	
	Factor Loading .61	
	Based on a five item scale where 5 = most appropriate and 1 = least (N=464)	
UNITARY	A measure of the employee's perception about the changing nature of the employment relationship over the period that PRP had been in operation comprising six items. $\alpha = .84$ (i9) 'Management generally are more inclined to listen to the views of employees than they used to be.'	2.53
	Factor Loading .83	
	(i8) 'Communication between management and employees is generally improving.'	
	Factor Loading .81	
	(i5) 'Employees are more likely to be treated as individuals by the organisation than they were in the past.'	
	Factor Loading .77	
	(i7) 'Employees feel more confident about being flexible in their approach to changes in their work than in the past.'	
	eigenvvalue .72	
	(i4) 'There is less a feeling of 'us' and 'them' between employees and management than there used to be.'	
	Factor Loading .72	
	(i1) 'The core values which are promoted by the organisation are now supported by a larger proportion of the workforce than they used to be.'	

## Appendix D

### Variable Definitions

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Label	Definition	Mean
	<p><b>Factor Loading .57</b>            Based on a five item scale where 5 = more unitarist over period since the introduction of PRP and 1 = least (N=483)</p>	
BELONG	<p>A measure of the employee's feelings of identification and loyalty – based on Cook &amp; Wall's (1980) standard commitment questions - comprising six items. <math>\alpha = .82</math></p> <p>(b2) reverse scored - 'I sometimes feel like leaving this employer for good.'</p> <p><b>Factor Loading .76</b></p> <p>(b4) 'Even if the firm were not doing well financially, I would be reluctant to change to another employer.'</p> <p><b>Factor Loading .71</b></p> <p>(b8) – reverse scored - 'I would not recommend a close friend to join our staff.'</p> <p><b>Factor Loading .69</b></p> <p>(b5) 'I feel myself to be part of the organisation.'</p> <p><b>Factor Loading .69</b></p> <p>(b1) 'I am quite proud to be able to tell people who it is I work for.'</p> <p><b>Factor Loading .68</b></p> <p>(b7) 'The offer of a bit more money with another employer would not seriously make me think of changing my job.'</p> <p><b>Factor Loading .63</b></p> <p>Based on a seven item scale where 7 = greatest feelings of loyalty and identification and 1 = least (N=485)</p>	3.25
INVOLVEMENT	<p>A measure of the employee's feelings of involvement – based on Cook &amp; Wall's (1980) standard commitment questions - comprising three items. <math>\alpha = .67</math></p> <p>(b9) 'To know that my own work had made a</p>	4.41

## Appendix D

### Variable Definitions

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Label	Definition	Mean
	contribution to the good of the organisation would please me'	
	Factor Loading .81	
	(b6) 'In my work I like to feel I am making some effort, not just for myself but for the organisation as well.'	
	Factor Loading .79	
	(b3) – reverse scored 'I am not willing to put myself out just to help the organisation.'	
	Factor Loading .64	
	Based on a seven item scale where 7 = greatest feelings of involvement and 1 = least (N=485)	

## Appendix E

Correlation Matrix – Latent Variables – Spearman's rho 2tailed sig. \*\*>.01 \*>.05

	1	2	3	4	5	6	7	8	9	10	11	12
<b>1 MOTIVATION</b>												
<b>2 INSTVAL</b>	.35**											
<b>3 EXPECTANCY</b>	.12*	.20**										
<b>4 FAIRA</b>	.18**	.28**	.15**									
<b>5 INTERFAREA</b>	.20**	.23**	.15**	.25**								
<b>6 GOODF</b>	.23**	.27**	.17**	.58**	.31**							
<b>7 POSITIVEF</b>	.27**	.35**	.08	.18**	.05	.18**						
<b>8 DIFFICLTG</b>	.03	.12**	.09	.02	-.05	.04	.04					
<b>9 SPECIFICG</b>	.12*	.20**	.15**	.33**	.07	.40**	.23*	.02				
<b>10 RELEVANTG</b>	.16**	.22**	.12**	.36**	.14**	.37**	.20**	-.08	.39**			
<b>11 UNITARY</b>	.42**	.36**	.12**	.36**	.27**	.39**	.31**	.05	.23**	.29**		
<b>12 BELONG</b>	.24**	.35**	.13**	.29**	.27**	.30**	.25**	.03	.16**	.26**	.49**	
<b>13 INVOLVEMENT</b>	.17**	.22**	.14**	.21**	.19**	.18**	.26**	.03	.04	.13**	.34**	.47**

## Appendix F Hypotheses

No.	Hypotheses	Outcome
<u>Hypothesis 1.</u>	'Thames Water introduced PRP in order to achieve a number of objectives, but principally in order to achieve a change in corporate culture following privatisation.'	The qualitative evidence from structured interviews with key players supports this hypothesis – see Chapter 7.
<u>Hypothesis 2(a)(I)</u>	'Individual employee motivation will tend to increase as a result of PRP, where the employee has an expectancy that improved performance will be instrumental in leading to a valent outcome."	Regression analysis confirms this association, R .36 (Table 10.i). N.B. However, while motivation in Thames Water increases in response to these variables, it is still only the minority in Thames Water who report that they are motivated by PRP.
<u>Hypothesis 2(a)(ii).</u>	'The explanatory powers of expectancy theory in respect of the motivational effectiveness of PRP will be improved by factoring in Equity considerations'	Equity variables increase the explanatory power of the expectancy model, so that R.39 (Table 10.ii). This is only a marginal improvement in the explanatory power of the model and it is suggested that is because instrumentality already comprises some equity considerations
<u>Hypothesis 2(a)(iii)</u>	'The explanatory powers of expectancy theory in respect of the motivational effectiveness of PRP will be improved by factoring in feedback.'	Feedback further increases the explanatory power of the expectancy model so that R.43 (Table 10.iii). Manipulation of the model then suggests a more parsimonious expectancy model R.42 (Table 10.iv) where equity variables are removed but feedback variables are retained.

## Appendix F Hypotheses

### Hypothesis 2 (b)

'In so far as goal setting theory explains the motivational effectiveness of a PRP scheme, individual employee motivation will be directly and positively related to goal difficulty for specific goals to which the employee is committed.'

Regression analysis suggests a relatively lower level of association between goal setting variables and motivation, R.23 (Table 10.v). There were problems in identifying a measure for commitment and goal relevance and difficulty both had poor scale reliability. The literature also suggests problems with operationalising this theory in a field setting. Consequently it is difficult to be confident about the results.

### Hypothesis 2 (c)

'Goal setting and expectancy theory will not be cumulative in the extent to which they explain the motivational effectiveness of the Thames Water PRP scheme.'

Goal setting and expectancy do not have a cumulative explanatory effect on the results of the Thames Water survey (Table 10.vi) and these results support this hypothesis.

### Hypothesis 2 (d)(i).

'Where employees believe that other employees of the same firm are being paid comparatively more for their effort, they will be demotivated.'

Distributive equity was not identified as an underlying variable by factor analysis, consequently it was necessary to rely on a single item in the questionnaire. There turned out to be a relatively poor association between this item and motivation R.15 (Table 10.vii).

### Hypothesis 2 (d)(ii).

'Where employees perceive that there is procedural inequity in the PRP scheme they will be less motivated.'

Procedural equity was more highly associated with motivation, R.27 (Table 10.viii) than distributive equity. This suggests that hypothesis 2 (d)(ii) is a more robust explanation of motivation in Thames Water than hypothesis 2 (d)(i).

## Appendix F Hypotheses

### Hypothesis 3(a)

The Thames Water programme of cultural change will have brought about a change for some employees in their view of the relationship with their employer, and that will in turn have increased the commitment of those employees to the employer.

The two commitment variables identified in this research are associated with measures of cultural change, R.50 (Table 10.x) and R.37 (Table 10.xi). These results support this hypothesis, however it is difficult to be confident about the flow of causation, and these results should be treated with caution.

### Hypothesis 3(b)

Employees who are more committed to their employer will be more highly motivated by PRP than employees who are less committed to their employer.'

There is a relatively weak association between commitment and motivation, R.26 (Table 10.xiii). This suggests either that PRP may not be a particularly effective mechanism for bringing about cultural change or that the proposed model for explaining its effectiveness is not particularly robust.

### Hypothesis 3(c)

'PRP will be more effective in changing organisational culture where the PRP scheme is also successful in motivating employees.'

There is an association between cultural change and motivation, R.44 (Table 10.xiii). These results support this hypothesis, however it is difficult to be confident about the flow of causation, and these results should be treated with caution. However the issues raised about the effectiveness of PRP as an agent of cultural change would provide an interesting avenue for further research.