Pay for performance risks discouraging motivated employees

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Incentive schemes, which rely on monitoring technologies, are becoming increasing popular as a means to foster productivity in public sector organisations. A legitimate question to ask is whether they improve service delivery or, instead, they force already motivated workers to waste time dealing with monitoring/reporting systems.

Two examples help us understand the kind of situations we have in mind. First consider a hospital director who wants to improve the quality of patient care that depends on the number of hours doctors work and on the quality of the care they provide, among other things. It is easy to observe the number of hours that doctors work, but immediately assessing the quality of their care is not. In order to improve doctors' incentives to provide better care, the director may consider linking their compensation not only to the hours they spend in the hospital, but also to the quality of the care.

Since the latter is not directly measurable, the hospital can set up a costly monitoring and reporting technology, which requires doctors to report how they take care of each patient, and make part of the doctors' pay linked to the quality of these reports. Of course, filling a detailed report detracts precious time from actual patient care and hence can negatively impact on the quality of the service provided. This means that the decision of whether to adopt a PFP contract and a monitoring technology (and how to design both of them) should carefully weigh costs and benefits.

Similarly, consider the case of a school principal who cares about students' learning, which depends on the number of hours kids are taught and on the quality of teaching. As before, assume that hours are observable, but the quality (of teaching) is not. In order to improve teachers' incentives to teach well, the principal may consider linking teachers' compensation to the results of a proficiency test that students are asked to take. Since the results of such a test are an imperfect measure of what kids have actually learned at school, and the preparation of such tests is costly (in terms of hours subtracted from actual teaching), we are again in the presence of trade-offs.

Clearly, the more doctors are committed to patients' care or the more teachers are committed to education, the higher is the opportunity cost of having them spend time filling reports or preparing for the tests. An additional, important cost is the one associated with the possibility that the more committed professionals may consider leaving workplaces where too much effort is devoted to costly performance measurement. This may explain why US private schools, where there is no testing, may not only attract highly qualified teachers, but can also pay them lower wages than public schools where test preparation is becoming an increasing burden. In other words, the fact that more motivated professionals are ready to accept pay cuts to avoid wasting time with the monitoring technology may hint at the presence of adverse selection problems.

The fact that the decision of whether to adopt — and how subsequently to design— PFP contracts and monitoring technologies depends on the interaction between employees' motivations and the quality of the available monitoring and reporting technology should warn against one-size-fits-all solutions. More precisely, managerial and technological solutions that allow measuring the effort of poorly motivated employees at a reasonable cost, and paying them accordingly, are definitely part of the solution, as New Public Management (NPM) advocates argue. However, these solutions become part of the problem when the contribution of the different tasks to the creation of value is difficult to measure and/or when employees are committed to the goals of the organisation (and thus already have incentives to work hard).

Our findings can also help explain the mixed results associated with NPM reforms and e-government initiatives, and call for a more critical approach to the adoption of monitoring and reporting technologies. Reformers should pay at least as much attention to employees' commitment to public service delivery as to the "measurability" of their daily activities.

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Notes:

- *This blog post is based on the paper Motivations, monitoring technologies, and pay for performance (2017), Journal of Economic Behavior & Organization, 133. 236-255. ISSN 0167-2681*
- *The post gives the views of its authors, not the position of LSE Business Review or the London School of Economics and Political Science.*
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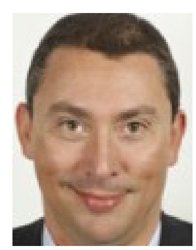

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