



Incentive Compensation for the Warehouse Team

**By Jason Bader, Principal
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In a previous article I discussed a disconnect between company profitability and company bonus programs. In the example, I talked about a company who had put together a great profit sharing program with their employees. The reward came out monthly and was based on the net profitability of the branch location. The disconnect occurred when employees felt like they had no influence over the size of the bonus or what they could do to improve the payout. Reducing mistakes, paying attention to damage and general efficiency will eventually drive improved net profit, but it is difficult for someone to take such broad practices and create a correlation to improvement in a monthly bonus. In order to make such bonus programs effective, companies need to break down the expectations into very simple and measurable criteria.

Several readers sent me emails appreciating the anecdotal story, but requested more specific details on how they could create programs for their warehouse team. The programs themselves aren't very difficult to set up. I find that the greatest barrier to creating a variable compensation program for the warehouse comes from the executive level. I hear this all the time, "Why should I give them more money to do their job?" Or, "Their incentive is to keep their job." These folks are clearly still deciding what to do with their 8 track tape collection. The times have changed. Naysayers must adapt to the present workforce and leave the "lucky to have a job" mentality behind.

First, we need to start with a reasonable budget. What would motivate your team to become more diligent? Would an additional \$200 per month be meaningful to one of your team members? I may be shooting a bit low here. Remember, fuel is over \$3.00 per gallon in most places. The company I grew up in created pools of incentive dollars for each functional team based on the monthly net profit. The warehouse, including drivers, shared one pool. During times of affluence, typically the second and third quarters of the year, the individual payout was substantial. During the more meager times of the year, the payout diminished. Since it was based on net profitability, the expenses were kept in check.

The pool was distributed based on seniority and position in the team. The manager took the largest percentage and from there the distribution amounts were not very consistent. As you can see, there were a few flaws in the plan. This is the blessing of hindsight and contact with a few hundred distributors over the last 10 years. The plan was well intentioned, but it lacked a connection between effort and reward. In order to set this up properly, I suggest that the monthly distributions should be an equal slice of the pie.

By creating a team incentive, we can simplify our criteria for performance. I generally like to see companies use no more than 5 criteria to measure the team. A smaller set of criteria will allow the team to really focus their effort and it is easier to measure. When we add too many performance measures, the likely hood that they will fail on one or more of the criteria increases. In addition, if we add too many points of measure, the likely hood of management to grow weary

of the program increases exponentially. The criteria can change over time to meet the challenges of the organization.

Essentially, each criteria has a pass / fail grading approach. If any one of the criteria is not met, the incentive is reduced. For example, if they achieve 4 of the 5 goals, the pool is reduced to 80% of the payout. I have seen more ambitious managers try to weigh different criteria based on importance to the company, but frankly I see this as a waste of energy. Simplicity leads to consistency. Consistency leads to longevity. I want the program to become part of the company culture.

Make sure to keep the criteria attainable. Going from an inventory accuracy of 65% to an accuracy rate of 93% in 30 days is not reasonable. Going from 65% to 75% is attainable. I want these folks to reach the goal. I want them to get the full payout. When the participants win, the company is winning big time. Let me ask you this, how many Benjamin Franklins get burned up in your warehouse due to sloppy procedures and general negligence? I think you can afford to do this.

In order to come up with the criteria, make sure that you can measure them reasonably. Keep the monitoring process relatively easy. Here are a few suggestions for your program:

Cleanliness - Cleanliness is next to Godliness in wholesale distribution. I can usually tell how efficient and profitable a warehouse is from the first walk through. It needs to be clean, organized and well lit. A place for everything and everything in its place. This might be a bit subjective, but someone has to set the standard.

Inventory Accuracy – I believe in measuring accuracy by unit variance, not dollar variance. If your accuracy is 95%, this means that I can go count 100 items at random and 95 of those items will match the exact unity quantity that I see in my software package. Measuring by dollar variance simply makes us think we are doing better than we really are.

Product Damage – This is a real killer of profit. Every time we have to replace a damaged item, the costs are astronomical. For most distributors, a \$100 product replacement requires at least \$3000 dollars in additional sales to pay for the mistake.

Shipping Accuracy – This information can be captured by the customer service team. A status code on a replacement order will help the measurement process.

Open Transfers – This was a huge burden in my former career. When we move to multi-location entity, transfers become a part of our vocabulary. Unfortunately, transfer orders are often given lower priority and can fall through the cracks. The consequences of this negligence can be very expensive.

Equipment Repair – With a proper checklist program in place, preventative maintenance can drastically reduce the productivity costs associated with equipment failure.

Employee Safety - A good friend of mine would provide a quarterly bonus to location without any time loss accidents.

Lines Picked Per Hour – For those of you with more sophisticated warehouse software, there are a whole host of productivity measures you could incorporate in your program.

Deliveries Per Hour – This one might not be applicable to all, but isn't it strange how some drivers take 8 hours to deliver 15 orders on one day and 8 hours to deliver 32 orders on another? There just doesn't seem to be a correlation between the number of stops and the time they are away from the shop.

This is just a brief list of thoughts based on my experience, but I am certain that you can come up with several additional criteria that would be more beneficial to your environment. Some of these criteria, like the final one, may seem somewhat unfair to the other team members. After all, doesn't the delivery efficiency rest solely in the hands of the driver?

Let me ask this question – Could the manner in which the orders were loaded (such as the last stop at the front of the truck) affect the efficiency of the delivery run? Would proper labeling by the shipping personnel have aided in the efficiency of the run? If we are going to call ourselves a team, we have to consider how our job performance affects the ability of other team members to perform their specific tasks. Who is my internal customer?

Finally, as I have made reference to several times in this article, try to make this a monthly reward. When you shorten the span between behavior and reward, the motivation becomes more effective. I have heard of companies who give out Christmas bonuses based on company performance, but let's be realistic here: Do you really believe that your order pickers are thinking about a Christmas bonus when the August mercury is cresting over 100 degrees? Keep the span between reward and behavior tight.

I hope this gives you some thoughts on how to start your own incentive program for the warehouse team. Remember, you can take this approach with everyone in the organization. I believe that 20% of everyone's income can become variable in some way. It's not just for salespeople anymore. By the way, money isn't the only reward. Many of your younger generation employees view time off as a greater incentive. Four tens anyone? Good luck and remember that I am always here to help.

About the Author:

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