On Leadership

When paying more stops paying off

By Elizabeth Dunn and Michael Norton, Published: May 15, 2013 at 8:00 am


(istockphoto)

Everyone likes money. Ask people who say they don't care about money if they've ever turned down a raise. Wait for the awkward pause.

But money is funny, too. However much it can motivate people to work harder and better, it also has curious—and sometimes counterproductive—effects on their performance. A growing body of research shows that, in some cases, paying people more not only fails to change their behavior but actually makes them perform even worse.

Money can be a surprisingly poor incentive. In a series of large-scale experiments with school children, paying kids a reward of as much as $5,000 to maintain at least a B average had absolutely no detectable influence on their performance in school. Other research has even shown that paying kids for good grades leads to *decreased* motivation—it can "crowd out" any natural enjoyment they may have had for those activities. Sure, kids like money as much as anyone, but when faced with the choice between opening those textbooks and opening gaming apps, the money failed to make a difference.

Big bonuses can hurt in yet another way. Behavioral economists asked people in India to play Simon, the electronic memory game that flashes a rapid sequence of colored lights and then asks players to repeat it. People who were promised very little for successfully completing the task (4 rupees) often performed no differently than those who were promised more (40 rupees). More troublingly, those who had at stake a much larger sum (400 rupees) suddenly felt the enormous pressure of failing. They choked under the strain, and consequently did worse than those who were paid less.

So if paying more doesn't always pay off, what can managers dangle as carrots instead of cash? There is in fact another scarce and valued commodity just waiting to be used more often: time.

Research shows that companies that offer flextime—the ability for employees to schedule their own starting and stopping times at the office—are better places to work than those that stick to a more typical 9-to-5 mentality. Not only do employees rewarded with flextime like their jobs more, they also have lower absenteeism and better performance. In fact, firms that adopt employee-centric mindsets and offer flextime have even been shown to be more profitable.

In addition to wanting more flexible time, of course, most of us also wish we simply had more time, period. Some companies have been experimenting with policies that provide just that. While "overworked" academics like us have traditionally been the sole beneficiaries of sabbaticals, the corporate sector is increasingly recognizing the value of making time off an incentive. At Intel, for example, employees are eligible for an eight-week sabbatical every seven years. Yahoo recently announced that it would offer employees eight-week breaks, albeit unpaid, after five years of service.

Managers don't necessarily need to give people extra weeks of vacation to make time off a motivator. In one recent study, researchers convinced (or more accurately, cajoled) consultants at Boston Consulting Group—half of whom reported working at least 65 hours per week, including evenings—to take just one night off per week from writing emails or placing phone calls related to their work. Despite their initial resistance, consultants who did so became more satisfied with and excited about their jobs.

Of course, it's not completely misguided to give employees monetary bonuses. What may be a mistake, however, is to always let them decide how to spend it. Not surprisingly, employees typically use their cash bonuses to buy things for themselves ("I deserve that flat screen TV I've been coveting!"). Such purchases are all well and good, but our own research shows that they provide very little happiness for the buyer. Instead, people gain far more happiness from spending their money on others—friends, family members and charities—than spending their money on themselves.

As a result, we've worked with companies to pilot test the value of giving employees nominal cash bonuses, but then making them give those bonuses away. In one study, we infiltrated teams of Belgian pharmaceutical sales representatives. Like paying kids for grades, giving salespeople small bonuses to spend on themselves did not harm their subsequent performance, but it had no positive impact on sales, either. The company could have just saved the money.

Other salespeople received a different, more unusual reward. We gave them what we call "prosocial" bonuses: cash that they were required to spend on another member of their team, such as by buying lunch or giving a small gift. Despite the fact that these salespeople ended up empty-handed–their money went to benefit a co-worker instead of themselves–these teams increased revenues, perhaps due to improvements in team camaraderie. Our data suggest that cash does work as a reward if employees use that cash to enrich their coworkers instead of to fill their own coffers.

Companies are increasingly experimenting with such rewards. At Google, employees can give any other employee a $150 bonus, with only one catch: they must write at least a sentence explaining what that recipient did to earn their largesse. And while $150 is a small sum compared to the average salary at Google, the company reports that such bonuses are more effective at increasing employee happiness than typical cash rewards are.

We are not suggesting that employees would perform optimally if their rewards came solely in the form of more days off or more money to spend on their colleagues. Salaries and bonuses are generally effective—if limited—motivators. But the nuanced psychology of reward suggests that despite the allure, the power of money can wear off. When it does, providing more time off and more ways to help others may prove to work in its place.

Elizabeth Dunn and Michael Norton are co-authors of "Happy Money: The Science of Smarter Spending" (Simon & Schuster) and professors at the University of British Columbia and Harvard Business School, respectively.

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IHaveAllTheAnswers wrote:

10:24 AM MDT

The studies seem to be funded by big business as they always come back that money is not a motivator. I say BS! If it's not a motivator, then how about we cut CEO salaries to 10%.

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Hkiwa wrote:

10:05 AM MDT

What a ridiculous study....using rupees....You go from 7 cents (US) to 72 cents to a whopping 7 dollars....Intellectual nothing. How much money was wasted producing this garbage?

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KS100H wrote:

7:52 AM MDT

Well the evidence is clear; the productivity of American workers has been rising for decades despite the stagnation of salary/wages since the 1980s. I'm really glad that researchers are digging up more reasons for companies to keep a cap on how much they pay their workers.***

*** "workers" means the lower 90% of their employees. Bonuses and higher salaries for upper management, of course. They've earned it!

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Crickey7 wrote: