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## Putting Together a Workable Incentive Compensation Plan

Attracting and retaining employees whose skills and commitment contribute significantly to the growth and profitability of the business should be a priority for every contractor. While high-performing project managers, supervisors, and engineers are typically driven by their own high standards, a satisfactory compensation package can often motivate them to continue performing at peak levels.

Contractors have found that providing compensation “over and above” base pay has helped retain and motivate key employees. Here’s what you need to know if you think you might want to introduce some form of incentive compensation plan into your workplace.

### What It Is

An incentive compensation plan is designed to tie pay to performance and to achieve gains in worker productivity. A compensation plan can take the form of merit pay, bonuses, profit sharing, corporate stock ownership, and commissions. The reward can be paid currently or deferred to some time in the future, typically at retirement. An incentive compensation plan can be purely discretionary and may be targeted to individual employees, work crews, the organization as a whole, or a combination of these groups.

Irrespective of which approach is chosen, managers and supervisors should understand what’s expected of them to qualify for the incentive compensation. Contractors should clearly spell out minimum performance standards, even in situations where the compensation is purely discretionary. Many contracting firms have found it helpful to link corporate goals to managers’ and supervisors’ performance objectives in order to earn incentive compensation. Indeed, the most successful incentive compensation plans are customized to the contractor’s specific needs and goals.

### Performance-based Plan

A performance-based plan employs objective criteria to determine incentive pay. Generally, the plan gives managers a fixed percentage of profits per division or contract. Some plans establish clearly identified objectives that the manager must accomplish in order to receive the compensation. For instance, since punch lists significantly impact a contractor’s bottom line, some contractors award incentive pay to managers or foremen for minimizing punch lists and/or for resolving them efficiently.

### Discretionary Plans

Contractors value discretionary incentive compensation plans for their flexibility. For example, it’s not always possible to grant incentive pay or to assess the contributions of top performers solely through a set of objective criteria. Since these individuals are often put in charge of the most complex projects, a more subjective analysis of their performance may be warranted. A pure performance-based plan could end up undervaluing a key employee’s overall contributions, particularly on difficult or unusual projects where certain skills may be difficult to measure. However, a discretionary plan would allow a contractor to reward a key employee based on the contractor’s own assessment of the value of the employee’s various contributions.

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### **Deciding on Payment**

The construction industry has traditionally relied on cash bonuses. However, a growing number of privately owned firms are offering top performers the opportunity to receive an equity stake in the business. Typically, ownership interests come in the form of restricted stock. Under this arrangement, the employee is granted an equity interest in the company but would forfeit some or all of the stock if he or she leaves the company prior to a predetermined vesting schedule.

Other contractors who are less willing to give up any actual ownership in their firms rely more on “phantom” stock and on stock appreciation rights to reward key employees. These incentive payment strategies allow recipients to benefit from and share in any increase in the value of the company stock while not actually owning any shares.

### **We Can Help**

We can help if you think that your company could benefit from introducing an incentive compensation plan or if you are dissatisfied with your current plan’s operation.

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