

Central Public Sector Enterprises: Performance Linked Incentive Schemes, Employees Stock Option Scheme and Enterprise specific implementation models

Annex 2.5.1

A. Central Public Sector Enterprises (CPSE) - Performance Linked Incentive Scheme

1. The High Level Pay Revision Committee headed by Justice S. Mohan had recommended that payments over and above the ceiling of 50% of basic pay should be entirely in the nature of performance related pay. These performance related payments should be a function of profitability at the level of a particular enterprise and emoluments at the level of the individual executive. The Committee believed that some norms would be desirable and suggested that such performance related payments should not, as a norm, exceed 5% of the distributable profits of the enterprise. Accordingly DPE OM No2 (49)/98-DPE (WC) dated 25-6-1999 lays down this principle with power of implementation being vested in the Board of Directors. The OM provides that "Payment of perquisites and allowances may be upto a maximum of 50 per cent of the basic pay, payments over and above the ceiling of 50 per cent should be entirely in the nature of Performance Related Payments which should not exceed 5 per cent of the distributable profits in an enterprise."

2. The distributable profit is arrived as below:
"Distributable profit represents the profit after tax and providing for transfer to Statutory Reserves such as Foreign Project Reserve, Investment Allowance Reserve, General Reserve (u/s 205 2A of the Companies Act) etc." (DPE OM No 2(49)/98-DPE (WC) GL-XXIX dated 12-9-2000).

B. CPSE - Employees Stock Option Scheme (ESOS)

3. The ESOS offers holding shares to employees. The beneficiaries of the Trust are regular employees of the company who voluntarily contribute to the scheme by investing their savings in the share and other instruments of the company. Each beneficiary may contribute each financial year to the trust a sum not exceeding 1/6th of his annual pay plus DA. The Trustees distribute to the beneficiaries the net earnings in proportion to the beneficiary certificate(s) held by the beneficiary during the year. The Trust normally has an independent existence, an arm's length relationship with management as well as the labour in terms of professional decision making. This scheme is applicable to all cases of disinvestment or fresh issue of equity by the enterprises and is subject to provision of Company Law and SEBI guidelines as applicable from time to time. (OM No: DPE/11(55)/97-Fin. Dated 28-1-1998)

C. CPSE – Enterprise specific implementation models

4. The first Performance Linked Incentive project discussed is the “**Project Construction Incentive Scheme of National Thermal Power Corporation (NTPC) for Barh (3x660 MW) Plant**”. NTPC has been successfully implementing performance related incentive schemes for some time. The incentive plan decided for the Barh project was group based in order to foster team spirit and create a cohesive environment essential for producing quick results. The NTPC experience shows that productivity rise is the highest when all direct and indirect employees are integrated in an incentive scheme which leads to collective collaboration. A set of targets were mutually agreed upon for the grant of incentives on the Barh project which comprised of major milestones that NTPC wanted to achieve in a given time-frame. Project Incentives (PI) were also coupled with generation incentives to incentivize the start of generation and achieve efficiencies in generation. The entitlement was as per categories of employees. The overall limit to PI was capped at 25% of the annual basic pay. However, additional performance related incentives were given in the form of extra incentive payment, if the project was completed ahead of the planned schedule. Thus, if the project was completed one month before schedule, PI cap was raised to 26.25% of the basic pay, and to 27.50% of the basic pay if the project was completed two months ahead of schedule.

Table 1 Details of project incentives

Group / Category	Project Incentive	Generation Incentive
Group – A (O&M Employees)	25 % of Project Incentive applicable to project construction employees as at Group B-II(b) subject to the condition that sum total of Project Construction incentive and generation Incentive (excluding Sp. Oil Incentive) does not exceed 25% of basic pay.	100%
Group-B-II a) Common Services Employees [Excluding Project Construction Employees as given below (b)]	25% of Project Incentive applicable to project construction employees as at Group-B-II(b) subject to the condition that sum total of Project Const. incentive and Generation Incentive will not exceed the amount payable to Group-A employees.	60% of Group-A
b) Project Construction Employees (Civil Construction & Equipment erection)	Incentive admissible as per performance – payment matrix, subject to the condition that total payment including Generation Incentive does not exceed the limits provided for.	50% of Group – B-II(a) i.e. 30% of group-A

5. The second example is the experience of the “**Indian Oil Corporation**” with performance based reward schemes. Indian Oil Corporation operates two schemes i.e. the Productivity Incentive Scheme (PIS) and Performance Linked Incentive (PLI).

i) Productivity Incentive Scheme (PIS)

- a) PIS system has both team performance and individual performance, combined in ratio of 80:20.
- b) For the Team performance incentive component, the constitution of teams and performance parameters for each team are based on business needs.
- c) The earlier scheme (prior to 2004/05) had only Team performance component where the maximum payout under Team Performance with 100% target achievement was 15%. With the team performance and individual performance in the ratio of 80:20. The team performance incentive for achieving 100% targets has been pegged at maximum of 12% (80% of 15%). For lower achievements, the percentage gets reduced according to the parameters.
- d) Payout on individual performance is based on the scores obtained by the individual in the normal performance appraisal.
- e) The individual scores on Key Performance Indicators (KPIs) from the Performance management system are on a scale of 1 to 5, against which the corresponding payout will be determined.
- f) For successful implementation of individual performance based incentive scheme, a robust performance management system with defined roles, KRAs, KPIs, weightages and targets has been introduced.

ii) Performance Linked incentive (PLI)

- a) The PLI continues to be linked to the performance against annual corporate MOU targets.
- b) The MOU rating slabs and percentage of distributable profits to be allocated against each slab have been revised as outlined below. The above percentages have been worked out after considering Indian Oil’s profitability. The distributable profit allocated is divided by the total pay (BP+DA) to arrive at the percentage of the individual of the individual base pay, which can be distributed to all the employees.

Table 2 MOU Rating with Percentage Distribution

MOU Rating	Percentage of distributable profits allocated
1.00 to 1.25	2.0%
1.26 to 1.50	1.5%
1.51 to 1.75	1.0%
1.76 to 1.99	0.5%

- c) Payment of incentive at the existing levels under PLI is guaranteed for every employee in case MOU score is more than a preset standard.

- d) The increase benefits are not admissible to officers and workmen who are rated less than 'Satisfactory' in their annual performance appraisals. Such employees are entitled to receive the amount as per existing (old) scheme.
- e) The incentive payments allocated under PIS & PLI put together does not exceed 5% of the distributable profits in a financial year.

6. The third example is the experience of the “**Bharat Heavy Electricals Limited**” (BHEL) with Plant Performance Payment Scheme (PPPS) and Performance Linked Incentive Scheme. The BHEL PPPS was introduced during 1973-74 to rationalize and replace the diverse production incentive schemes in vogue in the various units. The formula used for evaluation of the performance of the units and the scheme of payment for the same is given below:

Table 3 Evaluation of Performance

	Indices	Formula	Weightage
1	Physical Completion	Actual Physical Completion Budgeted Physical Completion	100
2	Delivery Performance & Project Completion	Actual milestone/important supplies completion during the Quarter (planned Milestone) Important supplies completion during the quarter	15
3	Quality Performance	For every 6% reduction in No. of NCR w.r.t. base year weightage will be 1 sub to max. weightage of 5 for 30% and above reduction in No of NCRs	5
			120*
* For the purpose of computation of % achievement, this will be converted to base of 100.			

The scheme at BHEL covers all categories of employees, including temporary and casual employees and trainees. The performance against the various indices is evaluated quarterly on cumulative basis but the payment in respect of the four quarters is made at the end of the year. The quantum of payment is computed as a percentage of wage (Basic pay + DA) subject to the condition that where an employee's wage/salary exceeds Rs 4000/- per month, performance payment is computed as if the salary or wage were Rs 4000/- per month.

7. The fourth example is the experience of “**The Shipping Corporation of India Limited**” (SCI). The scheme covers all shore based employees of SCI and is administered on the basis of organization's performance and individual measure. Eligibility criteria of Performance Related Incentive Payment at SCI are as under:

- a) Actual distribution not to exceed 5 % of distributable profit as defined by Department of Public Enterprises for one year
- b) While implementing the scheme, the individual's payment will be worked out on the basis of parameters, covering group performance, attendance records and ACR rating for the period.

Table 4 Scheme of payment (II)

Excellent	100%
Very Good	90%
Good	70%
Fair	40%
Poor	Nil

- i. 1st component comprising of 20% incentive amount will be payable to all shore employees
- ii. 2nd component comprising of 40% incentive shall be payable with reference to attendance.
- iii. 3rd component comprising of the remaining 40% of incentive is payable with reference to ACR for the financial year under consideration. The ACR scheme and incentives are paid in following manner:

Table 5 Percentage Payable w.r.t. ACR Average

ACR Average (out of 10)	% Payable
≥ 8.5	100 %
≥ 8.25 < 8.5	95%
≥ 8.00 < 8.25	90%
≥ 7.75 < 8.00	85%
≥ 7.50 < 7.75	80%
≥ 7.25 < 7.5	65%
≥ 7.00 < 7.25	50%
< 7.00	0%

- c) In addition, certain checks and balances have been proposed in the scheme.
 - i. Employees who have an unblemished record during financial year (no penalties) will be only entitled for the incentive for that particular year
 - ii. Employees who have been dismissed/discharged or terminated from the service shall not be entitled for incentive
 - iii. Employees under suspension shall not be entitled for the incentive payment until and unless proved not guilty and suspension order is revoked.
 - iv. In case of leave without pay, there will be pro-rata deduction of the payable PRI.

(Source: Inputs from Department of Public Enterprise's Letter DO No. 2(40)/06-DPE(WC) dated 26th March, 2007 and IIM Ahmedabad 'Synthesis Report on Formulating the Concept, Principles, and Parameters for Performance-Related Incentives (PRI) in Government'.)