

Motivation, Evaluation and Incentives

Mahmoud M. Nourayi

Department of Accounting, Loyola Marymount University, Los Angeles, USA.

**Corresponding Author:* Mahmoud M. Nourayi, , Department of Accounting, Loyola Marymount University, Los Angeles, USA.

ABSTRACT

In this article I describe the importance of relationship between the organizational goals and performance evaluation and reward system. Such a relationship plays a significant role in motivating the decision maker to make the "right" choice for advancement of the organization and achievement if its goals. In this article, I discuss the issues relevant to motivation factors in the choice process as well factors to be considered in designing an incentive system. The article addresses issues related the assessment and measurement of the results of the decision maker's choice are and explain the design flaws that may result in dysfunctional behavior by the decision maker

Keywords: Incentive structure, Motivation, Assessment

INTRODUCTION

Individuals choose to act in order to achieve some objectives. In general, the common denominator of one's objectives, I propose, is one's happiness. Therefore, individual decision making processes are driven by factors that provide physical satisfaction and or emotional fulfillment.

In this perspective the choice process is motivated by economic rewards/penalties, social acceptability, natural needs, and emotional aspirations. Clearly, the intrinsically-driven choices do not require direct outside influences from. However, choices that impact other individuals, or society as a whole, are motivated by external factors and are subject to social or private contractual terms.

Behavioral choices motivated by external factor are economic based and subject to rational selection process. However, some behavioral psychologists believe individual judgment and choice process are subject to cognitive biases due to mental shortcuts and may result in the departure of the choice from a strictly rational process [1]. Kahneman and Tversky[2] challenged the notion of rationality and suggested that choice processes driven by unstructured heuristic reasoning subject to individual biases departing from strict rational behavior. Accordingly, following research suggested bonded rationality in the choice process [3], [4]. Other researchers suggest heuristic reasoning may depend on an

abbreviated decision process and less complete information yet be considered rational, that is, less demanding mental faculty.. According to this perspective heuristic reasoning often motivate choices that are better than results produced by the theoretically optimal choice process [5], [6].

This paper emphasizes the choice processes motivated extrinsically with positive and negative incentives. In such a decision framework, individual actions rewarded by those who are benefited directly or indirectly due to the related consequences while actions with potentially undesirable consequences are discouraged in punitive way by those who are impacted by such results.

While tangible and intangible societal rewards, such as recognition and respect by the members of one's social circle or tax incentive promoting certain socially desirable behavior, punitive measure may be formulated by laws to discourage an act or to prevent the undesirable consequence of an act in a collective setting.

Private interests may be promoted and protected through an economic incentive structure and contracting. While formulation of all contractual terms is the matter of agreement between and among individuals, assuming the terms do not violate existing laws, enforcement of the contact will be subject to the legal framework.

The remainder of this article present the individual choice and element of uncertainty in section 2 followed by a general Decision

Motivation, Evaluation and Incentives

Making Framework followed by a description of decision environment. I will discuss assessment and reward as well as incentive design issue that may cause dysfunctional behavior and divergence from intended objectives in section 4. Concluding comment in the final section.

INDIVIDUAL CHOICE AND UNCERTAINTY

Individual choices are fundamentally driven by human's emotional forces based on survival instinct and social needs. Individual's actions and preferences are motivated by both intrinsic and extrinsic influences. However, the forces that intrinsically motivate the choice process are less defined, less structured, and more complex. On the other hand, actions driven by extrinsic incentives are better understood and can be better defined based on the rational expectation framework.

Therefore, I limit my discussion of individual choice and underlying incentives to observable processes within the economic framework. In this context, I assume that individuals are economically rational in that they enjoy availability of various alternative course of actions they can choose from and the freedom to make such choices. The decision setting described here affords all members of the society the same level of freedom to choose subject to the rules of laws and regulations set by various institutions as prescribed by social constitution.

An individual's welfare and happiness is impacted by the consequence of his/her action not the action per se. As such, an element of uncertainty is introduced due to pervasive time lag in observing the consequence selected action. Furthermore, the uncertainty present in the choice process is intensified by inherent differences and conflicts among individuals' with different preference ordering.

DECISION MAKING FRAMEWORK

Decision makers facing uncertainty of the choice process experience different level of discomfort depending on their understanding of the decision environment and available choices. The decision makers specialized knowledge, skill-set, and ability to identify relevant information about the various alternatives, and other factor influencing the effect and consequence of each available alternative reduce the uncertainty and improves the quality of the outcome.

I therefore assume the improvement in the quality of the choice, the outcome, and the likelihood achieving the objective is positively

correlated with the level decision maker's knowledge and wisdom. Individuals are enticed by positive rewards to behave congruently with stated objectives such that the likelihood of achieving those objectives is increased.

Incentives are intended to align the interest of the decision maker, an agent, with that of another entity, the principal, by prompting the agent's action towards the outcome acceptable to the principal. An effective incentive arrangement between decision maker and the principal is expected to influence and guide the agent's behavior and choice process in meeting the timing and other conditions for an acceptable outcome in accordance with the assessment process and measurement approach as formulated by the agreement between the parties to the incentive contract. It is important to note that an effective incentive arrangement must take into account the decision makers intrinsic motivational forces in order to insure plausibility of the expected outcome.

Figure 1 represents the basic framework for the choice process under uncertainty and as described above where the objective for the choice process is specified by someone other than the decision maker. This framework assumes an assessment process provide a clear cut relationship between decision maker's choice process and outcome

ASSESSMENT AND REWARD

For an incentive system to be effective, the decision maker must be directed to behave in choosing the action(s) driven by extrinsic reward structure. The decision maker's control over the choice process must be coupled a method of accountability that influences and motivates the most optimal behavior in line with the conditions of a desirable outcome. As such the outcome and the conditions for the reward must be clearly defined. Furthermore, the expected outcome should be subject to a refined measurement process. In some cases where the outcome may not be easily measureable, an observable surrogate measure that is closely associated with the outcome may be used for assessment purposes. The reward is determined based on the acceptability the actual outcome based on the measured result. This mean the decision maker must meet, a target, the exact expectation of the outcome. It is possible for the incentive system to allow for a range of acceptable

Motivation, Evaluation and Incentives

outcome measure where the reward is either fixed for any outcome measure within the acceptable range or proportional to the outcome measure within that range. In the

latter form, the reward varies with the quality of the choice and or the level of effort in some functional form.

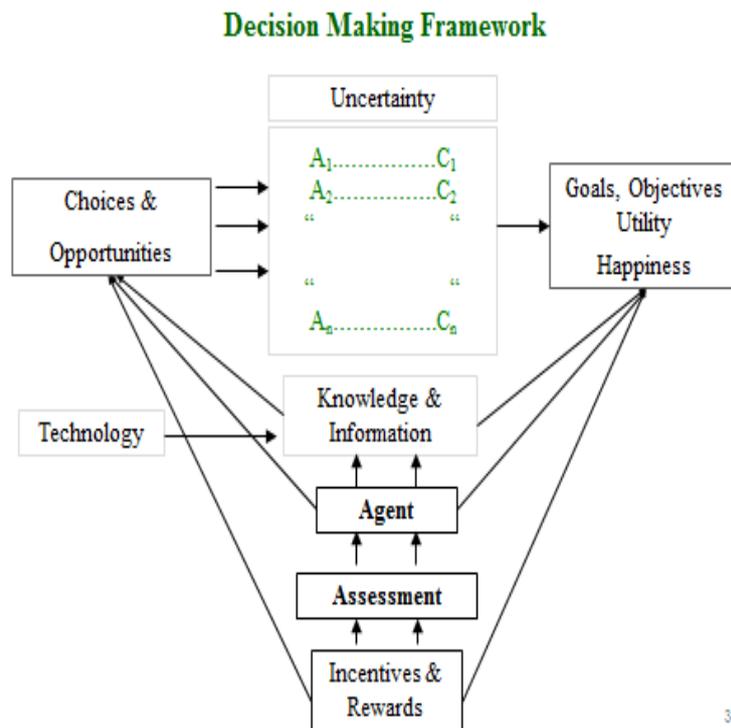


Fig1. Decision Making Framework

The acceptable range may be at any positive level or impose a minimum (threshold) and maximum (cap) level referred to as “Incentive Zone” [7]. One must be cognizant of potential for dysfunctional behavior in such a structure relative to the decision maker’s ability to adjust his/her choice process without regard to the intent of the reward system assuming the decision maker can potentially benefit from such behavior in the future.

Regardless of how the variable portion is assessed, an allowance for fixed reward may be added to the rewards to account for random events and or choices by others that may impact the outcome measure. This arrangement may be more enticing for the decision maker who is more risk averse.

CONCLUDING REMARKS

Designing an incentive system requires a fundamental consideration of the decision maker’s intrinsic motivational factors in order to understand the influence of such factors on objectives of the decision process. Considerable attention should be paid in

identifying the external reward structure and potential dysfunctional behavior that may be prompted by the incentives. Additionally, it is essential to provide a clear definition of objective(s) and expected outcome(s). Defining the measurement process for evaluating the decision maker’s choices is a critical component of an effective incentive system design. Clearly the timing and other conditions of acceptable outcome are important aspects of reward structure.

REFERENCES

- [1] Simon, H. (1991) Bounded Rationality and Organizational Learning. *Organization Science*, 2 (1): 125–134.
- [2] Kahneman, D., and Tversky, A. (1973) On the Psychology of Prediction. *Psychological Review*. American Psychological Association, 80 (4): 237–51.
- [3] Kahneman, D. (2003) Maps of bounded rationality: psychology for behavioral economics. *The American Economic Review*, 93 (5): 1449–75.
- [4] Fiedler, K., and von Sydow, M. (2015). Heuristics and Biases: Beyond Tversky and Kahneman's (1974) Judgment under Uncertainty, In Eysenck, Michael W.; Groome, David.

Motivation, Evaluation and Incentives

- Cognitive Psychology: Revising the Classical Studies, Sage, London. pp. 146–161.
- [5] Gigerenzer, G. and Selten, R. (2002). Bounded Rationality. Cambridge: MIT Press.
- [6] Gigerenzer, G. (1996). On narrow norms and vague heuristics: A reply to Kahneman and Tversky. Heuristic. Psychological Review, 103 (3): 592–596.
- [7] Murphy, K. J., (2001) Performance standards in incentive contracts. Journal of Accounting and Economic, 30:245-278.

Citation: Mahmoud M Nourayi. "Motivation, Evaluation and Incentives." *International Journal of Research in Business Studies and Management*, vol 5, no. 2, 2018, pp. 20-23.

Copyright: © 2018 Mahmoud M Nourayi. This is an open-access article distributed under the terms of the Creative Commons Attribution License, which permits unrestricted use, distribution, and reproduction in any medium, provided the original author and source are credited.