15
Reward Management

Key concepts and terms

- Analytical job evaluation
- Analytical matching
- Base rate
- Contingent pay
- External relativities
- Going rate
- Grade and pay structure
- Internal relativities
- Intrinsic motivation
- Job-based pay
- Job evaluation
- Market rates
- Person-based pay
- Reward system

Learning outcomes

On completing this chapter you should be able to define these key concepts. You should also know about:

- The nature and aims of reward management, the framework within which it operates and the characteristics of reward systems
- The constituents of individual reward packages
- The concepts of strategic reward and total rewards
- The nature of financial and non-financial rewards
- How jobs are valued through job evaluation and market pricing
- The characteristics of grade and pay structures and methods of pay progression within them
- The nature of recognition schemes and employee benefits

Introduction

The reward management strategies and practices of an organization contribute to the improvement of organizational performance by developing and operating reward systems which help to attract, retain and engage the people upon which the business relies. This chapter begins with a definition of reward management and its aims, and an analysis of the reward framework and systems. The key components of the reward system are then described, starting with the basic requirement to value jobs by means of job evaluation and market pricing, and continuing with the use of the information on job values to design and manage grade and pay structures. As explained in the following section, such structures usually provide for pay progression through either contingent pay (pay for performance, contribution, competency or skill) or pay related to service. In addition, as covered in the final two sections, organizations may have formal recognition schemes and will provide a range of employee benefits including pensions.

Reward management defined

Reward management is concerned with the strategies, policies and processes required to ensure that the value of people and the contribution they make to achieving organizational, departmental and team goals is recognized and rewarded. It is about the design, implementation and maintenance of reward systems (interrelated reward processes, practices and procedures) which aim to satisfy the needs of both the organization and its stakeholders, and to operate fairly, equitably and consistently. These systems include arrangements for assessing the value of jobs through job evaluation and market pricing, the design and management of grade and pay structures, performance management processes, schemes for rewarding and recognizing people according to their individual performance or contribution and/or team or organizational performance, and the provision of employee benefits.

It should be emphasized that reward management is not just about pay and employee benefits. It is equally concerned with non-financial rewards such as recognition, learning and development opportunities and increased job responsibility.

Aims of reward management

In the words of Ghoshal and Bartlett (1995), the overall aim of reward management should be to 'add value to people'. It is not just about attaching value to them. More specifically, the aims are to:

- support the achievement of business goals through high performance;
- develop and support the organization's culture;
- define what is important in terms of behaviours and outcomes;

- reward people according to the value they create;
- reward people according to what the organization values;
- align reward practices with employee needs;
- help to attract and retain the high-quality people the organization needs;
- win the engagement of people.

The reward management framework

Reward management is a complex process with many interconnecting elements and underpinning concepts. The reward management framework expressed as a concept map is shown in Figure 15.1.

The reward package

The foundation of an individual's reward package is the base or basic rate. This is the amount of pay (the fixed salary or wage) constituting the rate for the job. It may be varied according to the grade of the job or, for manual and some service workers, the level of skill required.

Base pay is influenced by internal and external relativities (going rates). The internal relativities may be measured by some form of job evaluation. External relativities are assessed by tracking market rates. Alternatively, levels of pay may be agreed through collective bargaining with trade unions or by reaching individual agreements.

Base pay may be expressed as an annual, weekly or hourly rate. The last of these is sometimes called a time rate system of payment. The base rate may be adjusted to reflect increases in the cost of living or market rates, by the organization unilaterally or by agreement with a trade union. Pay that is related entirely to the value of the job rather than the person is called job-based pay. Where the base rate can be enhanced by payments related to a person's level of competency or skill it is known as person-based pay. This term can be extended to include contingent pay, which rewards people for their performance or contribution.

Reward systems

Reward systems consist of the interrelated processes and practices which combine to ensure that reward management is carried out effectively to the benefit of the organization and the people who work there. How a reward system operates is shown in Figure 15.2.

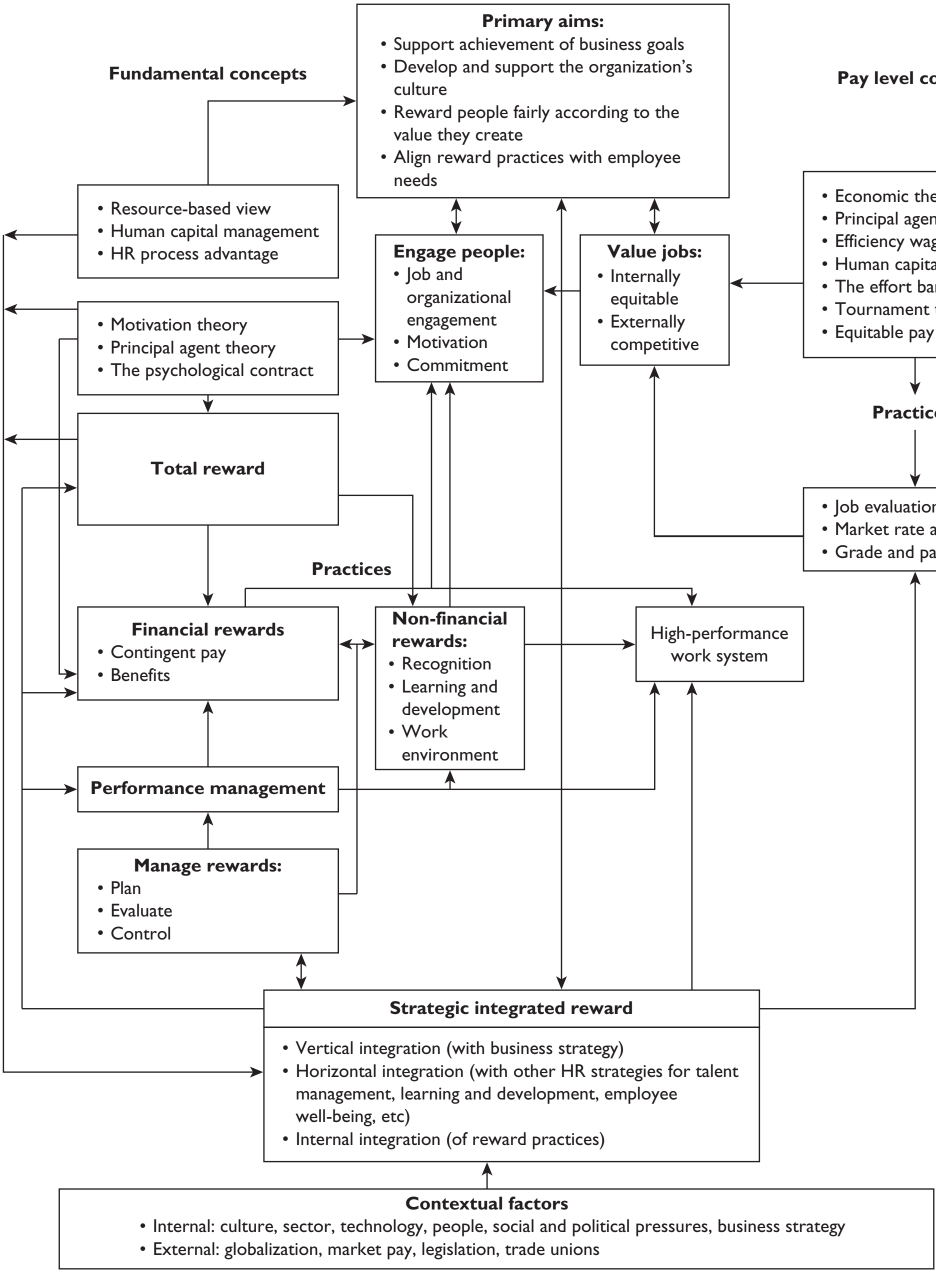

Figure 15.1 The reward management framework

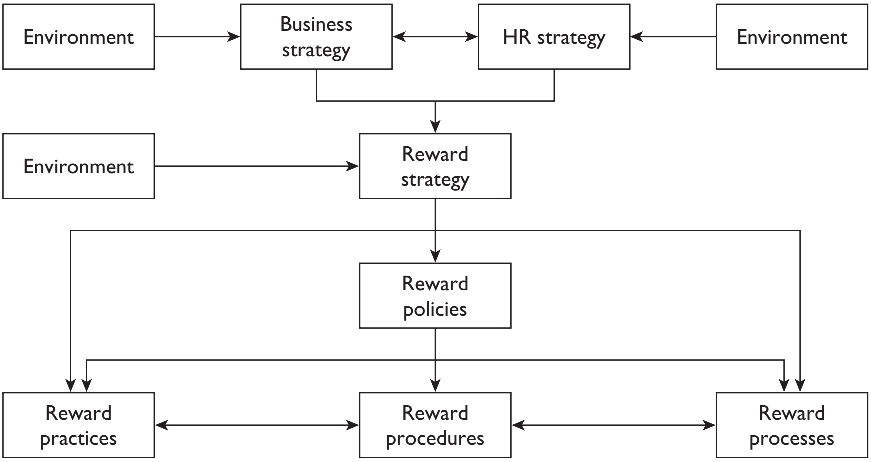

Figure 15.2 How a reward system operates

Reward systems are based on the reward strategy, which flows from the business strategy, for example to gain competitive advantage, and the HR strategy, which is influenced by the business strategy but also influences it. The HR strategy may, for example, focus on resourcing but it should also be concerned with satisfying the needs of employees as well as those of the business. All aspects of strategy are affected by the environment. Reward strategies direct the development and operation of reward practices and processes, and also form the basis of reward policies, which in turn affect reward practices, processes and procedures.

Components of a reward system

The components of a reward system and the interrelationships between them are shown in Figure 15.3. The remaining sections of this chapter describe the following key components of a reward system:

- strategic reward;
- total rewards;
- financial and non-financial rewards;
- valuing jobs through job evaluation and market pricing;
- grade and pay structures;
- pay progression through contingent and service-related pay schemes;
- recognition schemes;
- employee benefits and pensions.

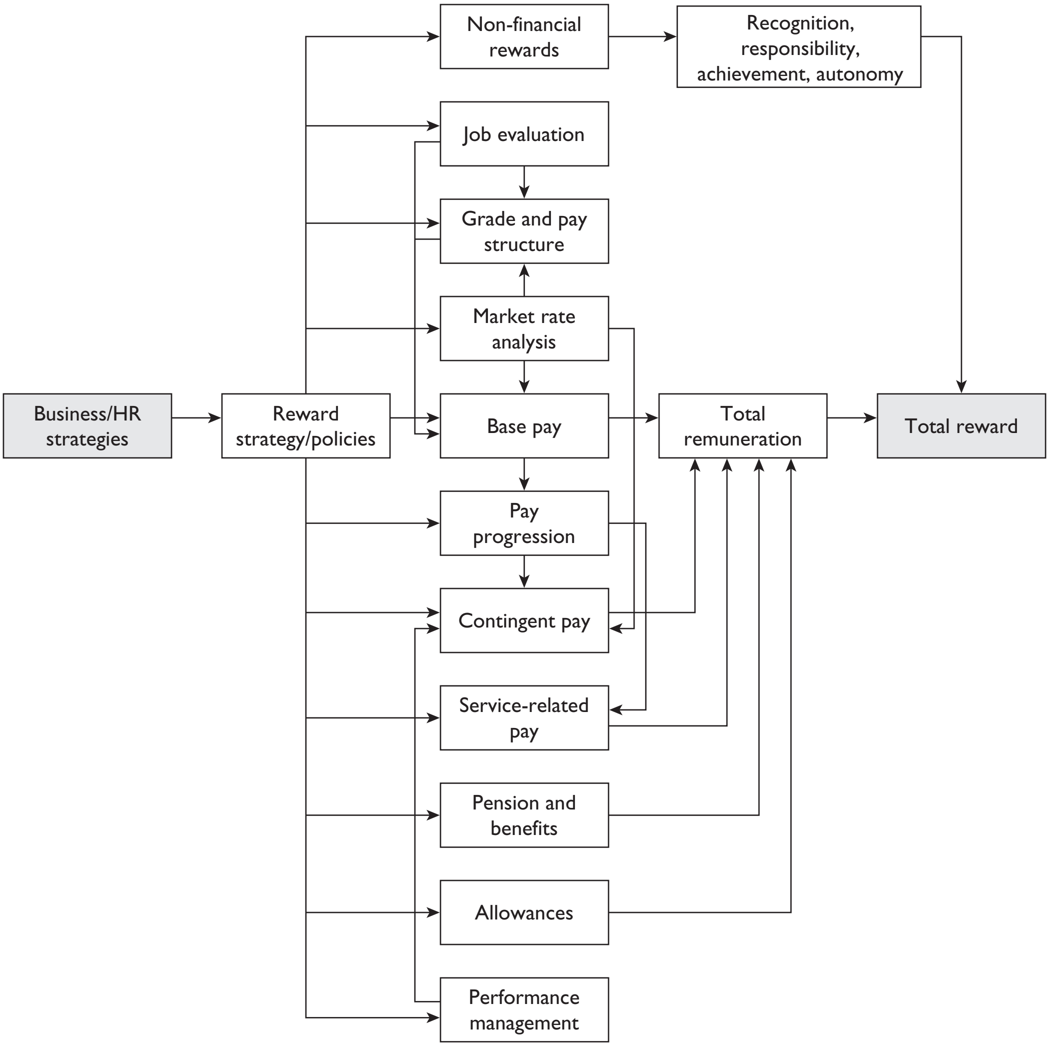

Figure 15.3 Reward system components and interrelationships

Strategic reward

Strategic reward management is the process of planning the future development of reward practices through the formulation and implementation of reward strategies. Armstrong and Brown (2006) describe how it provides answers to two basic questions: first, 'Where do we want our reward practices to be in a few years' time?' and second, 'How do we intend to get there?' It therefore deals with both ends and means. As an end it describes a vision of what reward processes will look like in a few years' time. As a means, it shows how it is expected that the vision will be realized. Strategic reward can be described as an attitude of mind – the view that it is necessary to plan ahead and make the plans happen.

Strategic reward is based on beliefs about what the organization values and wants to achieve. It does this by aligning reward practices with both business goals and employee values. As Duncan Brown (2001) emphasizes, the 'alignment of your reward practices with employee values and needs is every bit as important as alignment with business goals, and critical to the realization of the latter'. Strategic reward should be based on an articulated reward philosophy which is expressed in a set of guiding principles. It will be based on a total rewards approach.

Reward philosophy

A reward philosophy consists of belief in the need to operate in accordance with the principles of distributive and procedural justice. Reward strategies in the past have sometimes focused exclusively on business needs and alignment. Yet unless employees see and experience fairness and equity in their rewards, the strategy is unlikely to be delivered in practice.

The philosophy recognizes that reward management is a key factor in establishing a positive employment relationship, one in which there is mutuality – the state that exists when management and employees are interdependent and both benefit from this interdependency. Such a relationship provides a foundation for the development of a climate of trust.

Guiding principles

A reward philosophy can be expressed through a set of guiding principles that define the approach an organization takes to dealing with reward. They are the basis for reward policies and provide guidelines for the actions contained in the reward strategy. Importantly, they can be used to communicate to employees how the reward system operates and takes into account their interests as well as those of the business.

Reward guiding principles are concerned with matters such as:

- operating the reward system justly, fairly, equitably and transparently in the interests of all stakeholders;
- developing reward policies and practices that support the achievement of business goals;
- rewarding people according to their contribution;
- recognizing the value of everyone who is making an effective contribution, not just the exceptional performers;
- creating an attractive employee value proposition;
- providing rewards which attract and retain people and enlist their engagement;
- helping to develop a high-performance culture;

- maintaining competitive rates of pay;
- maintaining equitable rates of pay;
- allowing a reasonable degree of flexibility in the operation of reward processes and in the choice of benefits by employees;
- devolving more responsibility for reward decisions to line managers.

Developing reward strategies

Reward strategists rarely start with a clean sheet. They have to take note, and keep taking note, of constant changes in organizational requirements. They must track emerging trends and modify their views accordingly, as long as they do not leap too hastily onto the latest bandwagon. They have to ensure that reward strategy can be implemented at a pace the organization can manage and people can deal with. The fundamental change in culture often inherent in such projects takes a lot of time – and trouble – to achieve.

It may be helpful to define reward strategy formally for the record and as a basis for planning and communication. But this should be regarded as no more than a piece of paper that can be modified when needs change – as they will – not a tablet of stone. Reward strategy, like business strategy, is likely to be formulated and reformulated as it is used. An HR director told Duncan Brown and Stephen Perkins (2007) that 'We deliberately didn't have a reward strategy, it would have been a nine day wonder… we let it evolve, step-by-step.' Brown and Perkins also noted that 'Truly strategic reward approaches are not about supposed best practice or quick fixes or quick wins.'

Total rewards

The concept of total rewards describes an approach to reward management which emphasizes the need to consider all aspects of the work experience of value to employees, not just a few such as pay and employee benefits. It aims to blend the financial and non-financial elements of reward into a cohesive whole. A total rewards approach recognizes that it is necessary to get financial rewards (pay and benefits) right. But it also appreciates the importance of providing people with rewarding experiences which arise from the work they do, their work environment, how they are managed and the opportunity to develop their skills and careers. It contributes to the production of an employee value proposition which provides a clear, compelling reason why talented people should work for a company.

It is a holistic view of reward which looks at the overall reward system in order to determine how its elements should be integrated so that they provide mutual support in contributing to the overall effectiveness of the system. Reliance is not placed on one or two reward mechanisms operating in isolation; instead, account is taken of every way in which people can be rewarded and obtain satisfaction through their work. The whole is greater than the sum of its parts. The aim is to maximize the combined impact of a wide range of reward initiatives on motivation, commitment and job engagement.

The elements of total rewards are modelled in Figure 15.4.

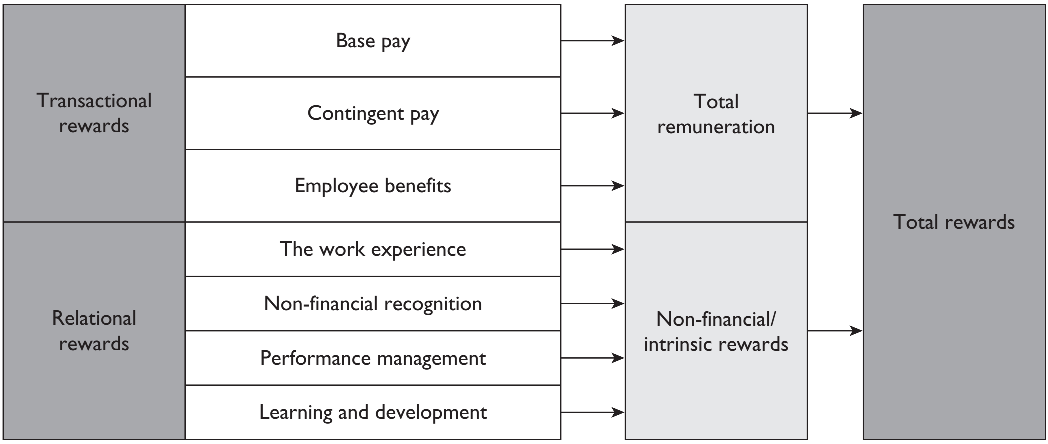

Figure 15.4 The elements of total rewards

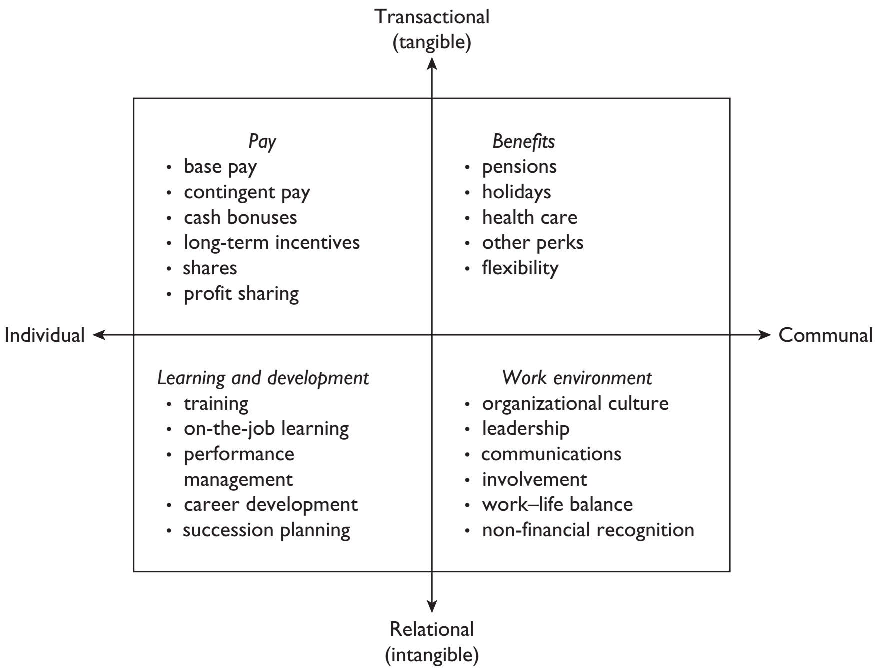

Figure 15.5 Model of total rewards: Towers Perrin

The Towers Perrin model shown in Figure 15.5 is frequently used as the basis for planning a total rewards approach. It consists of a matrix with four quadrants. The upper two quadrants – pay and benefits – represent transactional or tangible rewards. These are financial in nature, and are essential to recruit and retain staff, but can be easily copied by competitors. By contrast, the relational or intangible non-financial rewards represented in the lower two quadrants cannot be imitated so readily and can therefore create both human capital and human process advantage. They are essential to enhancing the value of the upper two quadrants. The real power, as Thompson (2002) states, comes when organizations combine relational and transactional rewards. The model also makes a useful distinction between individual and communal rewards.

The total rewards concept emphasizes the importance of both financial and non-financial rewards, and the considerations affecting them are discussed below.

Financial rewards

Financial rewards comprise all rewards that have a monetary value and add up to total remuneration – base pay, pay contingent on performance, contribution, competency or skill, pay related to service, financial recognition schemes, and benefits such as pensions, sick pay and health insurance. They are the core elements in total rewards.

The management of a reward system requires decisions on levels of pay, how jobs should be valued, the design and operation of grade and pay structures, and the choice of benefits. Such decisions can be complex and difficult, but the problems pale by comparison with the issues surrounding the use of contingent financial rewards.

Labour economists distinguish between the incentive effect of financial rewards (generating more engagement and effort) and the sorting effect (attracting better-quality employees). The fundamental issue is the extent to which financial rewards provide an incentive effect. The sorting effect is important but creates less controversy, perhaps because it is more difficult to pin down.

A vociferous chorus of disapproval has been heard on the incentive effect. One of the best-known and most influential voices was that of Alfie Kohn (1993), who stated in the *Harvard Business Review* that 'bribes in the workplace simply can't work'. He asserted that 'Rewards, like punishment, may actually undermine the intrinsic motivation that results in optimal performance. The more a manager stresses what an employee can earn for good work, the less interested that employee will be in the work itself.' Jeffrey Pfeffer (1998) concluded in his equally influential *Harvard Business Review* article 'Six dangerous myths about pay' that 'Most merit-pay systems share two attributes: they absorb vast amounts of management time and make everybody unhappy.'

There is a strong body of opinion, at least in academic circles, that financial rewards are bad – because they do not work and indeed are harmful, while non-financial rewards are good, at least when they provide intrinsic motivation – that is, motivation by the work itself. But the critics are mainly referring to financial incentives. They do not appear to recognize that incentives are not the same as rewards. They can be distinguished as follows.

Rewards offer tangible recognition to people for their achievements and contribution. Financial rewards consist of job-based pay, which provides base pay related to the value of the job, and person-based pay, which provides rewards which recognize the individual's performance, contribution, competence or skill. Rewards can also be non-financial: for example, recognition. If rewards are worth having and attainable and people know how they can attain them, they can act as motivators.

Incentives are intended to encourage people to work harder and achieve more. They are supposed to provide direct motivation: 'Do this and we will make it worth your while.' Incentives are generally financial but they can promise non-financial rewards such as promotion or a particularly interesting assignment.

If this distinction is not made it may be assumed that financial rewards only exist to provide an incentive. They might do this or, as the nay-sayers contend, they might not. But financial rewards can be justified because they are a form of tangible recognition – they are a means of informing people that they have done well, and they accord with the reasonable and generally accepted belief that people who do better should be valued more highly. However, the use of financial rewards in the shape of contingent pay has aroused strong feelings amongst those who support and those who oppose them. The arguments for and against are set out below.

Arguments for financial rewards

The most powerful argument advanced for financial rewards is that those who contribute more should be paid more. It is right and proper to recognize achievement with a financial and therefore tangible reward. This is in accordance with the principle of distributive justice which, while it states that rewards should be provided equitably, does not require them to be equal except when the value of contribution is equal. Financial rewards can also be used to highlight key performance areas and generally to emphasize the importance of high performance.

Arguments against financial rewards

The main arguments against financial rewards are that:

- The extent to which contingent pay schemes motivate is questionable – the amounts available for distribution are usually so small that they cannot act as an incentive.
- The requirements for success are exacting and difficult to achieve.
- Money by itself it will not result in sustained motivation; intrinsic motivation provided by the work itself goes deeper and lasts longer.

- People react in widely different ways to any form of motivation – it cannot be assumed that money will motivate all people equally, yet that is the premise on which contingent pay schemes are based.
- Financial rewards may possibly motivate those who receive them, but they can demotivate those that do not, and the numbers who are demotivated could be much higher than those who are motivated.
- Contingent pay schemes can create more dissatisfaction than satisfaction if they are perceived to be unfair, inadequate or badly managed.
- Employees can be suspicious of schemes because they fear that performance bars will be continuously raised; a scheme may therefore only operate successfully for a limited period.
- Schemes depend on the existence of accurate and reliable methods of measuring performance, contribution, competence, or skill, which might not exist.
- Individuals are encouraged to emphasize only those aspects of performance that are rewarded.
- Contingent pay decisions depend on the judgement of managers, which, in the absence of reliable criteria, can be partial, prejudiced, inconsistent or ill-informed.
- The concept of contingent pay is based on the assumption that performance is completely under the control of individuals when in fact it is affected by the system in which they work.
- Contingent pay, especially performance-related pay, can militate against quality and team work.

Another powerful argument against contingent pay is that it has proved difficult to manage. Organizations, including the UK Civil Service, rushed into performance-related pay in the 1980s without really understanding how to make it work. Inevitably problems of implementation arose. Studies such as those conducted by Bowey and Thorpe (1982), Kessler and Purcell (1992), Marsden and Richardson (1994) and Thompson (1992a, 1992b) have all revealed these difficulties. Failures may arise because insufficient attention has been made to fitting schemes to the context and culture of the organization, but are often rooted in implementation and operating difficulties, especially those of inadequate performance management processes, the lack of effective communication and involvement, and line managers who are not capable of or interested in carrying out the actions involved properly. Vicky Wright (1991) summed it up: 'Even the most ardent supporters of performance-related pay recognise that it is difficult to manage well.'

Criteria for effectiveness

The effectiveness of financial rewards in the shape of contingent pay depends on the following factors:

- There is accurate, consistent and fair assessment of performance or contribution.

Pay differences can be related to performance or contribution differences and can be seen to be related.

- The principles of procedural and distributive justice are upheld.
- There is a climate of trust in the organization – as Thompson (1992b) commented. 'Where there is trust, involvement and a commitment to fairness, the (PRP) schemes work.'
- Performance management systems function well.
- Line managers have the necessary skills and commitment.
- Stakeholders, including line managers, employees and employee representatives, have been involved in the design of the scheme.
- The scheme is appropriate to the context and culture of the organization.
- The scheme is not unduly complex.
- The purpose, methodology and effect of the scheme have been communicated and understood.
- There is a clear line of sight between effort and reward.
- Rewards are attainable and worth attaining.

These are demanding criteria and difficult to meet. It may be right to reward people for their contribution, and there is plenty of research evidence that financial rewards can improve performance. For example, in the United Kingdom this was established by Booth and Frank (1999), Thompson (1998), Marsden (2004) and Prentice *et al* (2007). In the United States, Gupta and Shaw (1998), Jenkins *et al* (1998), Lazear (1999) and Prendergast (1999) among others all found positive relationships between financial incentives and performance.

Critical evaluation of financial rewards

The argument that people should be rewarded in accordance with the value of their contribution is a powerful one, but it stands alone. The evidence that incentives improve performance is conflicting. In some circumstances it works, as demonstrated by a number of research projects, but in others it does not. Certainly, typical performance-related pay schemes are unlikely to provide a direct incentive simply because they do not match the demanding requirements, for example line of sight, for this to happen. Their main purpose is to recognize the level of contribution, and even this is questionable because of the difficulty of making fair and consistent assessments of performance as a basis for pay decisions. Such schemes can demotivate more people than they motivate.

But what is the alternative? Should everyone be paid the same rate in a job however well they perform? Or should pay be progressed in line with length of service – paying people for being there? For all its problems, the balance of the argument is in favour of some scheme for relating pay to contribution. But the difficulties of doing this should be recognized, and every attempt should be made to ensure that pay decisions are fair, consistent and transparent. Involving staff in the development and monitoring of contribution pay schemes can be a great help.

However, non-financial rewards, especially those intrinsic to the work being carried out, can have a longer and deeper effect, and this is the premise upon which the concept of total rewards is based.

Non-financial rewards

Non-financial rewards are those that focus on the needs people have to varying degrees for recognition, achievement, responsibility, autonomy, influence and personal growth. They incorporate the notion of relational rewards, which are the intangible rewards concerned with the work environment (quality of working life, the work itself, work–life balance), recognition, performance management, and learning and development.

Non-financial rewards can be extrinsic such as praise or recognition, or intrinsic, associated with job challenge and interest, and feelings that the work is worthwhile.

It can be said that money will motivate some of the people all of the time, and perhaps all of the people some of the time. But it cannot be relied on to motivate all of the people all of the time. To rely on it as the sole motivator is misguided. Money has to be reinforced by non-financial rewards, especially those that provide intrinsic motivation. When motivation is achieved by such means it can have a more powerful and longer-lasting effect on people, and financial and non-financial rewards can be mutually reinforcing.

Reward systems should therefore be designed and managed in such a way as to provide the best mix of all kinds of motivators according to the needs of the organization and its members.

Job evaluation

Job evaluation is a systematic and formal process for defining the relative worth or size of jobs within an organization in order to establish internal relativities. It is carried out through either an analytical or a non-analytical scheme.

Analytical job evaluation schemes

Analytical job evaluation is based on a process of breaking whole jobs down into a number of defined elements or factors such as responsibility, decisions and the knowledge and skill required. These are assumed to be present in all the jobs to be evaluated but to different degrees. In point-factor and fully analytical matching schemes, jobs are then compared factor by factor, either with a graduated scale of points attached to a set of factors, or with grade or role profiles analysed under the same factor headings.

The advantages of an analytical approach are that first, evaluators have to consider each of the characteristics of the job separately before forming a conclusion about its relative value, and second, evaluators are provided with defined yardsticks or guidelines which help to increase the objectivity and consistency of judgements. It can also provide a defence in the United Kingdom against an equal pay claim. The main analytical schemes as described below are point-factor rating and analytical matching.

Point-factor rating

Point-factor schemes are the most common forms of analytical job evaluation. They were used by 70 per cent of the respondents with job evaluation schemes to the e-reward 2007 job evaluation survey.

The basic methodology is to break jobs down into factors. These are the elements in a job such as the level of responsibility, knowledge and skill or decision making which represent the demands made by the job on job holders. For job evaluation purposes it is assumed that each of the factors will contribute to the value of the job, and is an aspect of all the jobs to be evaluated but to different degrees.

Each factor is divided into a hierarchy of levels, typically five or six. Definitions of these levels are produced to provide guidance in deciding the degree to which the factor applies in the job to be evaluated. A maximum points score is allocated to each factor. The scores available may vary between different factors in accordance with beliefs about their relative significance. This is termed 'explicit weighting'. If the number of levels varies between factors this means that they are implicitly weighted because the range of scores available will be greater in the factors with more levels.

The total score for a factor is divided between the levels to produce the numerical factor scale. The complete scheme consists of the factor and level definitions and the scoring system (the total score available for each factor and distributed to the factor levels). This comprises the 'factor plan'.

Jobs are 'scored' (that is, allocated points) under each factor heading on the basis of the level of the factor in the job. This is done by comparing the features of the job with regard to that factor with the factor level definitions to find out which definition provides the best fit. The separate factor scores are then added together to give a total score which indicates the relative value of each job and can be used to place the jobs in rank order.

Analytical job matching

Like point-factor job evaluation, analytical job matching is based on the analysis of a number of defined factors. Profiles of roles to be evaluated which have been analysed and described in terms of job evaluation factors are compared with grade, band or level profiles which have been analysed and described in terms of the same job evaluation factors. The role profiles are then 'matched' with the range of grade or level profiles to establish the best fit and thus grade the job.

Analytical matching can be used to grade jobs or place them in levels following the initial evaluation of a sufficiently large sample of benchmark jobs – representative jobs that provide a valid basis for comparisons. This can happen in big organizations when it is believed that it is not necessary to go through the whole process of point-factor evaluation for every job, especially where 'generic' roles are concerned.

Non-analytical job evaluation

Non-analytical job evaluation schemes enable whole jobs to be compared in order to place them in a grade or a rank order – they are not analysed by reference to their elements or factors. They can operate on a job-to-job basis in which a job is compared with another job to decide whether it should be valued more, less or the same (ranking and 'internal benchmarking' processes). Alternatively, they may function on a job-to-grade basis in which judgements are made by comparing a whole job with a defined hierarchy of job grades (job classification) – this involves matching a job description to a grade description. Non-analytical schemes are simple to introduce and operate but provide no defined standards of judgement. Differences between jobs are not measured and they do not provide a defence in an equal value case.

Market pricing

Market pricing is the process of obtaining information on market rates (market rate analysis) to inform decisions on pay structures and individual rates of pay. It is called 'extreme market pricing' when market rates are the sole means of deciding on internal rates of pay and relativities and conventional job evaluation is not used. An organization that adopts this method is said to be 'market driven'.

This approach has been widely adopted in the United States. It is associated with a belief that 'The market rules, OK', disillusionment with what was regarded as bureaucratic job evaluation, and the enthusiasm for broad-banded pay structures (structures with a limited number of grades or bands). It is a method which often has appeal at board level because of the focus on the need to compete in the marketplace for talent.

Market rate analysis as distinct from extreme market pricing may be associated with formal job evaluation. The latter establishes internal relativities and the grade structure, and market pricing is used to develop the pay structure – the pay ranges attached to grades. Information on market rates may lead to the introduction of market supplements for individual jobs or the creation of separate pay structures (market groups) to cater for particular market rate pressures.

The acceptability of either form of market pricing is dependent on the availability of robust market data, and when looking at external rates, the quality of the job-to-job matching process, in other words comparing like with like. It can therefore vary from analysis of data by job titles to detailed matched analysis collected through bespoke surveys focused on real market equivalence. Extreme market pricing can provide guidance on internal relativities even if these are market driven. But it can lead to pay discrimination against women where the market has traditionally been discriminatory, and it does not satisfy UK equal pay legislation.

Grade and pay structures

Grade and pay structures provide a framework within which an organization's pay policies can be implemented. They enable the organization to determine where jobs should be placed in a hierarchy, define pay levels and the scope for pay progression, and provide the basis upon which relativities can be managed, equal pay achieved, and the processes of monitoring and controlling the implementation of pay practices can take place. Grade and pay structures also enable organizations to communicate the career and pay opportunities available to employees.

Grade structures

A grade structure consists of a sequence or hierarchy of grades, bands or levels into which groups of jobs which are broadly comparable in size are placed. There may be a single structure which is defined by the number of grades or bands it contains. Alternatively the structure may be divided into a number of career or job families consisting of groups of jobs where the essential nature and purpose of the work are similar but it is carried out at different levels.

Pay structures

A grade structure becomes a pay structure when pay ranges, brackets or scales are attached to each grade, band or level. In some broad-banded structures reference points and pay zones are placed within the bands, and these define the range of pay for jobs allocated to each band.

Pay structures are defined by the number of grades they contain, and especially in narrow- or broad-graded structures, the span or width of the pay ranges attached to each grade. *Span* is the scope the grade provides for pay progression, and is usually measured as the difference between the lowest point in the range and the highest point in the range as a percentage of the lowest point. Thus a range of £20,000 to £30,000 has a span of 50 per cent.

Guiding principles for grade and pay structures

Grade and pay structures should:

- be appropriate to the culture, characteristics and needs of the organization and its employees;
- facilitate the management of relativities and the achievement of equity, fairness, consistency and transparency in managing gradings and pay;
- enable jobs to be graded appropriately and not be subject to grade drift (unjustified upgradings);
- be flexible enough to adapt to pressures arising from market rate changes and skill shortages;
- facilitate operational flexibility and continuous development;
- provide scope as required for rewarding performance, contribution and increases in skill and competence;
- clarify reward, lateral development and career opportunities;
- be constructed logically and clearly so that the basis upon which they operate can readily be communicated to employees;
- enable the organization to exercise control over the implementation of pay policies and budgets.

Types of grade and pay structures

The main types of grade and pay structures and their advantages and disadvantages are summarized in Table 15.1.

Criteria for choice

There is always a choice of structures and the criteria are given in Table 15.2.

Table 15.1 Summary description of different grade and pay structures

Type of structure	Features	Advantages	Disadvantages
Narrow-graded	• A sequence of job grades – 10 or more. • Narrow pay ranges, eg 20–40 per cent. • Progression usually linked to performance.	• Clearly indicate pay relativities. • Facilitate control. • Easy to understand.	• Create hierarchical rigidity. • Prone to grade drift. • Inappropriate in a delayered organization.
Broad-graded	• A sequence of between six and nine grades. • Fairly broad pay ranges, eg 40–50 per cent. • Progression linked to contribution and may be controlled by thresholds or zones.	As for narrow graded structures but in addition: • the broader grades can be defined more clearly; • better control can be exercised over grade drift.	• Too much scope for pay progression. • Control mechanisms can be provided but they can be difficult to manage. • May be costly.
Broad-banded	• A series of often five or six 'broad' bands. • Wide pay bands – typically between 50 and 80 per cent. • Progression linked to contribution and competence.	• More flexible. • Reward lateral development and growth in competence. • Fit new-style organizations.	• Create unrealistic expectations of scope for pay rises. • Seem to restrict scope for promotion. • Difficult to understand. • Equal pay problems.

Table 15.1 *continued*

Type of structure	Features	Advantages	Disadvantages
Career family	• Career families identified and defined. • Career paths defined for each family in terms of key activities and competence requirements. • Same grade and pay structure for each family.	• Clarify career paths within and between families. • Facilitate the achievement of equity between families and therefore equal pay. • Facilitate level definitions.	• Could be difficult to manage. • May *appear* to be divisive if 'silos' emerge.
Job family	• Separate grade and pay structures for job families containing similar jobs. • Progression linked to competence and/or contribution.	• Can appear to be divisive. • May inhibit lateral career development. • May be difficult to maintain internal equity between job families unless underpinned by job evaluation.	• Facilitate pay differentiation between market groups. • Define career paths against clear criteria.
Pay spine	• A series of incremental pay points covering all jobs. • Grades may be superimposed. • Progression linked to service.	• Easy to manage. • Pay progression not based on managerial judgement.	• No scope for differentiating rewards according to performance. • May be costly as staff drift up the spine.

Table 15.2 Grade and pay structures: criteria for choice

Type of structure	Criteria for choice – the structure may be considered more appropriate when:
Narrow-graded	• the organization is large and bureaucratic with well-defined and extended hierarchies; • pay progression is expected to occur in small but relatively frequent steps; • the culture is one in which much significance is attached to status as indicated by gradings; • some but not too much scope for pay progression is wanted.
Broad-graded	• it is believed that if there is a relatively limited number of grades it will be possible to define and therefore differentiate them more accurately as an aid to better precision when grading jobs; • an existing narrow-graded structure is the main cause of grade drift; • it is considered that pay progression through grades can be related to contribution and that it is possible to introduce effective control mechanisms.
Broad-banded	• greater flexibility in pay determination and management is required; • it is believed that job evaluation should no longer drive grading decisions; • the focus is on rewarding people for lateral development; • the organization has been delayered.
Career family	• there are distinct families and different career paths within and between families that can be identified and defined; • there is a strong emphasis on career development in the organization; • robust methods of defining competencies exist.
Job family	• there are distinct market groups that need to be rewarded differently; • the range of responsibility and the basis upon which levels exist vary between families; • it is believed that career paths need to be defined in terms of competence requirements.
Pay spine	• this is the traditional approach in a public or voluntary sector organization and it fits the culture; • it is believed to be impossible to measure different levels of contribution fairly and consistently; • ease of administration is an important consideration.

Pay progression

Pay progression takes place when base pay advances through pay brackets in a grade and pay structure or through promotions or upgradings. Progression through pay brackets may be determined formally by means of a contingent pay scheme or by fixed increments, as described below. Informal progression takes place when there is no contingent or incremental pay scheme and increases are arbitrary.

Contingent pay progression is typically but not inevitably governed by performance ratings which are often made at the time of the performance management review but may be made separately in a special pay review.

Contingent pay schemes

The features, advantages and disadvantages and the appropriateness of individual contingent pay schemes and service-related pay are set out in Table 15.3.

Criteria for success

The following are the five criteria for effective contingent pay:

- Individuals have a clear line of sight between what they do and what they will get for doing it.
- Rewards are worth having.
- Fair and consistent means are available for measuring or assessing performance, competence, contribution or skill.
- People are able to influence their performance by changing their behaviour and developing their competencies and skills.
- The reward follows as closely as possible the accomplishment that generated it.

These requirements are exacting and few schemes meet them in full. That is why contingent pay arrangements can often promise more than they deliver.

Service-related pay

Service-related pay is supported by many unions because they perceive it as being fair – everyone is treated equally. It is felt that linking pay to time in the job rather than performance or competence avoids the partial and ill-informed judgements about people which managers are prone to make. Some people believe that the principle of rewarding people for loyalty through continued service is a good one. It is also easy to manage; in fact, it does not need to be managed at all. But essentially service-related pay means that people are rewarded just for being there and not for the level of their contribution.

Table 15.3 Summary of contingent pay schemes

Type of scheme	Main features	Advantages	Disadvantages	When appropriate
Performance-related pay (PRP)	Increases to basic pay or bonuses are related to assessment of performance.	● May motivate (but this is uncertain). ● Links rewards to objectives. ● Meets the need to be rewarded for achievement. ● Delivers message that good performance is important and will be rewarded.	● May *not* motivate. ● Relies on judgements of performance which may be subjective. ● Prejudicial to teamwork. ● Focuses on outputs, not quality. ● Relies on good performance management processes. ● Difficult to manage well.	● For people who are likely to be motivated by money. ● In organizations with a performance-oriented culture. ● When performance can be measured objectively.
Competency-related pay	Pay increases are related to the level of competency.	● Focuses attention on need to achieve higher levels of competency. ● Encourages competency development. ● Can be integrated with other applications of competency-based HR management.	● Assessment of competency levels may be difficult. ● Ignores outputs – danger of paying for competencies that will not be used. ● Relies on well-trained and committed line managers.	● As part of an integrated approach to HRM where competencies are used across a number of activities. ● Where competency is a key factor and it may be inappropriate or hard to measure outputs. ● Where well-established competency frameworks exist.
Contribution-related pay	Increases in pay or bonuses are related both to inputs (competency) and outputs (performance).	Rewards people not only for what they do but how they do it.	As for both PRP and competence-related pay, it may be hard to measure contribution and it is difficult to manage well.	When it is believed that a well-rounded approach covering both inputs and outputs is appropriate.
Skill-based pay	Increments related to the acquisition of skills.	Encourages and rewards the acquisition of skills.	Can be expensive when people are paid for skills they do not use.	On the shop floor or in retail organizations.

Recognition schemes

Recognition schemes as part of a total reward package enable appreciation to be shown to individuals for their achievements either informally on a day-to-day basis or through formal recognition arrangements. They can take place quietly between managers and individuals in their teams, or be visible celebrations of success.

A recognition scheme can be formal and organization-wide, providing scope to recognize achievements by gifts or treats or by public applause. Typically, the awards are non-financial but some organizations provide cash awards. Importantly, recognition is also given less formally when managers simply say 'well done', 'thank you' or 'congratulations' face to face or in a brief note of appreciation.

Employee benefits

Employee benefits consist of arrangements made by employers for their employees which enhance the latter's well-being. They are provided in addition to pay, and form important parts of the total reward package. As part of total remuneration, they may be deferred or contingent like a pension scheme, insurance cover or sick pay, or they may be immediate like a company car or a loan. Employee benefits also include holidays and leave arrangements which are not strictly remuneration. Benefits are sometimes referred to dismissively as 'perks' (perquisites) or 'fringe benefits', but when they cater for personal security or personal needs they could hardly be described as 'fringe'.

Flexible benefit schemes give employees a choice within limits of the type or scale of benefits offered to them by their employers.

Employee benefits are a costly part of the remuneration package. They can amount to one-third or more of basic pay costs and therefore have to be planned and managed with care.

Reward management: key learning points

Reward management defined

Reward management is concerned with the strategies, policies and processes required to ensure that the value of people and the contribution they make to achieving organizational, departmental and team goals is recognized and rewarded.

Key aims of reward management

- Support the achievement of business goals through high performance.
- Reward people according to the value they create.
- Help to attract, retain and engage the high-quality people the organization needs.

Content of individual reward packages

The base rate for the job plus contingent pay (where applicable) and employee benefits.

Strategic reward

Strategic reward management is the process of planning the future development of reward practices through the development and implementation of reward strategies.

Total rewards

The aim of total rewards is to blend the financial and non-financial elements of reward into a cohesive whole.

Financial rewards

All rewards that have a monetary value and add up to total remuneration – base pay, contingent pay and employee benefits.

Non-financial rewards

Rewards not involving the payment of salaries, wages or cash which focus on the needs people have to varying degrees for achievement, recognition, responsibility, autonomy, influence and personal growth.

Job evaluation

A systematic and formal process for defining the relative worth or size of jobs within an organization in order to establish internal relativities.

Market pricing

The process of establishing market or going rates.

Grade and pay structures

A hierarchy of job grades to which are attached pay ranges which provide scope for pay progression based on performance, contribution, competence or service.

Pay progression

The basis upon which pay increases within a pay structure. It may be contingent on performance, contribution or skill or it may take place in the form of fixed increments related to service.

Recognition schemes

An arrangement to recognize a person's achievement publicly or by a gift or a treat.

Employee benefits

Arrangements for providing personal security, financial assistance, or company cars and for satisfying personal needs.

Questions

1. In his influential book, *Strategic Pay* (1990), Ed Lawler wrote that 'The challenge is to develop pay programmes that support and reinforce the business objectives of the organization and the kind of culture, climate and behaviour that are needed for the organization to be effective.' How can reward policies and practices support the achievement of business goals?
2. Duncan Brown wrote that 'The alignment of your reward practices with employee values and needs is every bit as important as alignment with business goals, and critical to the realization of the latter.' How can this advice be put into effect in the development and operation of a reward system?
3. Marc Thompson claimed in 1992 that 'It is possible that performance pay may be more successful in demotivating the very employees it needs to stimulate most – the average performers – and may, in practice, contribute to a downward spiral of motivation among such employees.' Evaluate the evidence on the extent to which this applies.
4. Using examples from contemporary organizational practice show how performance pay can be used effectively to support changes in employee behaviour.
5. Make the business case for a switch from multi-graded pay spines to broadbanding in a government agency which has 'delayered' its organization, intends to operate more flexibly and wants to develop a performance culture. It is in position to take advantage of the freedom offered under the 'delegated pay' policy to determine its own pay structures.
6. Duncan Brown wrote that 'The alignment of your reward practices with employee values and needs is every bit as important as alignment with business goals, and critical to the realization of the latter.' How can this advice be put into effect in the development and operation of a reward system?

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