Banding - The New Pay Structure for the Transformed Organization

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An increasing number of fast-changing organizations are experiencing the dilemma of a traditional pay system that is ill-suited for the needs of the 1990s. Management still classifies its work force within a pay grade structure that was developed during an era when hierarchy and job specialization were highly valued. Most large, bureaucratic organizations still maintain job analysis, documentation, evaluation and grading systems that attempt to differentiate job worth based on fine distinctions using criteria that are weighted on management responsibilities. A pay grade structure is constructed to fit a vertical organization strategy. However, the modem organization is looking less like a pyramid, and some outfits are abandoning those support systems that do not align.

Similar to the trend affecting blue-collar workers in both unionized and non-unionized America - resulting in substantially fewer job classifications and levels - a growing number of organizations are opting for fewer pay grades for all types of jobs, and more horizontal (lateral) movement. Some employers no longer are satisfied with workers who have great depths of experience and knowledge in one functional area - the "chimney" model. Rather, they see advantages in having some specialists in a few highly technical fields, and more generalists who possess a breadth of cross-functional skills and perspective. Moreover, the new paradigm places less emphasis on the old command-and-control approach to management. Instead, management layers and jobs are being eliminated and participative management processes introduced. Decision-making and problem solving are no longer the exclusive domain of upper management. Team- and self-directed work forces are emerging rapidly, especially in the manufacturing sector. These changes have resulted in flatter and more empowered organizations.

These frame-breaking changes in organization design and effectiveness now challenge compensation professionals to develop alternative approaches to pay. Banding is one response. A banded pay structure has radically fewer vertical levels and job titles, and wider salary range boundaries. Although no studies have been conducted to determine trends and averages, companies that have introduced a banded structure use one-half to two-thirds fewer vertical grades and salary range spreads (from minimum to maximum), which are up to twice the normal width. Thus, "banding" is a flatter and broader pay structure - fitting well with the needs of the modern organization, which is less concerned with level and more concerned with involvement.

DESIGN FEATURES

There are four key design features to banding:

- Fewer grade levels (bands) and titles;

- Alternative career tracks, especially for non- managers;
- Wider salary ranges with no midpoints; and
- Two or more market-based pay ranges per band.

Because these major features are so different from the classic compensation systems, banding also requires that the pay delivery, job evaluation and market-pricing techniques be reassessed. As the banding model is just now emerging, it should be noted that this is but one version. However, the discussion that follows hopefully will serve as an important benchmark to firms engaged in a study of the topic.

BANDS

There is not an optimum, or ideal, number of bands to fit all organizations. In developing the vertical structure, the most relevant consideration is the number of management layers required. The height of the structure, after all, represents an organization's hierarchy. In multi-billion-dollar organizations with more than 20,000 employees, seven or fewer management layers is often the goal. Five or fewer layers in a comparably sized organization is uncommonly lean, but hierarchy is understood to vary by industry (especially service versus manufacturing) and function (especially line versus staff.) One band for each management layer is advisable, meaning that two adjacent layers should not occupy the same band.

A second and equally compelling consideration in setting the total number of bands is the number of levels felt to be minimally necessary in the individual-contributor (non-manager) job families. If the current system provides four to six levels (and grades) per job family, how many should remain? Which could be logically combined to yield jobs with clearly discernible differences? A banded structure will have no more than three job-family levels, though one or two levels is more typical and desirable. This limit obviously excludes any levels included in a dual-career ladder, which generally begin at a point equivalent to the first or second level of management.

An organization with 40 to 45 total (exempt and non-exempt) pay grades should end up with 10 to 20 bands after determining managerial layers and job family levels. However, the actual number is not nearly as important as the goal, which is to eliminate excess and redundant levels in a system that originally was created to sustain hierarchy and vertical movement.

TITLES

Once the vertical structure is reduced, it will be necessary to rationalize job titles, since two or more (former) jobs with different titles will occupy the same new band. Combining existing titles or identifying new ones are best accomplished with involvement from job holders. Titles give important organizational identity to people. Since banding reduces opportunities for upward mobility in level and title, it is critical that the titling scheme used is both descriptive of the job and valued by the incumbents. There should be no more than one title prefix (i.e., manager, director, specialist, etc.) for each band. However, a dual-career system with managers and individual contributors in the same band generally would provide two title prefixes - one for each track.

DUAL-CAREER TRACKS

The dual-career system is not a new idea. What is new is the increased incidence of management restructuring, resulting in fewer management layers and jobs. This trend leaves fewer traditional avenues for growth in responsibility, development and pay for employees who have been socialized to think of promotion into management as the only way to get ahead. A dual-career structure provides employees with greater opportunities for vertical growth without becoming a manager.

DUAL-CAREER TRACKS

Diagram 1

Band	Managerial	Individual Contributor
13	President	
12	Executive Vice-President	
11	Vice President	Executive Consultant
10	Assistant Vice President	Senior Consultant
9	Director	Consultant
8	Senior Manager	Senior Advisor
7	Manager	Advisor
6		Senior Specialist
5		Specialist
4		Senior Technician
3		Senior Administrative Support, Technician
2		Administrative Support, Senior Manufacturing Associate
1		Clerical Support, Manufacturing Associate

One track is designed for managers of people and another for individual contributors. A dual-career system can be integrated into most compensation structures, not just banding. However, without a dual-track feature, banding can generate concern about future career growth opportunities, as it reduces management grades and leaves fewer advancement opportunities.

Designing a dual-career system into banding begins with establishing boundaries. An individual-contributor dual-career track most often starts at a level parallel with the first or second level of management and tops out at or just before the executive ranks. The most challenging task associated with constructing the system is defining the lines of distinction between each individual contributor band, which ultimately becomes the basis for promotion and internal equity

Diagram 1 illustrates a 13-band structure, commencing at the non-exempt entry level, "clerical support/manufacturing associate" and continuing to the top executive position, "president." Seven managerial and individual-contributor levels and bands are shown. However, five of the individual-contributor track levels are parallel dual-career bands, leaving only two conventional job family ladder steps. (The exempt individual contributor job family levels are in bands 5 and 6, titled "specialist" and "senior specialist.") The dual-career track begins with the first level of management, band 7, and ends at band 11.

The non-exempt bands are shaded and contain two titles each-one for office and administrative jobs, and another for manufacturing and technical jobs. As with the exempt, there are two job family levels

RANGES WITHIN BAND

Most traditional pay structures relate a grade to a specific pay range. Also, it is typical for differences in grade to be established based on labor market differences in pay rate. (A 1989 ACA survey revealed that the most common evaluation technique was a combination of market-pricing and point-factor.) For example, an engineering job family often ends up in a grading sequence that is one or two grades higher than that of accounting on the basis of market supply and demand, reflected by salary survey data, which is noticeably higher for engineers. It is more difficult to associate a band with one pay range, as it is not possible to correct for external market forces by placing a highly priced job family (or job) on a higher band. There simply are not enough vertical levels available for such an adjustment. Banding results in the placement of entry-level engineers and accountants into the same "specialist" band (#5 in Diagram 1.) If there is only one "specialist" pay range, some engineers will be underpaid and some accountants will be overpaid. Banding can be adapted to respond to market conditions by installing two or more pay ranges for each band. In this approach, jobs are assigned to a band on the basis of internal job evaluation factors and to a pay range on the basis of external labor market factors. Thus, the engineer and accountant can occupy the same band but be compensated within two different pay ranges.

Diagram 2 illustrates the addition of two pay ranges per band for non-executive jobs to the 13-band structure presented earlier in Diagram 1. The two ranges are denoted as “A” an“B”.

DUAL CAREER TRACKS

Diagram 2

Band	Managerial	Individual Contributor		
13	President			
12	Executive VP, General VP			
11	Vice President	Executive Consultant		
10	Assistant VP, General Manager	Senior Consultant		
9	Director	Consultant		
8	Senior Manager	Senior Advisor		
7	Manager	Advisor		
6		Senior Specialist		
5		Specialist		
4		Senior Technician		
3		Senior Administrative Support Technician		
2		Administrative Support Senior Manufacturing Associate		
1		Clerical Support Manufacturing		
			A	**B**

Market Pay Lines

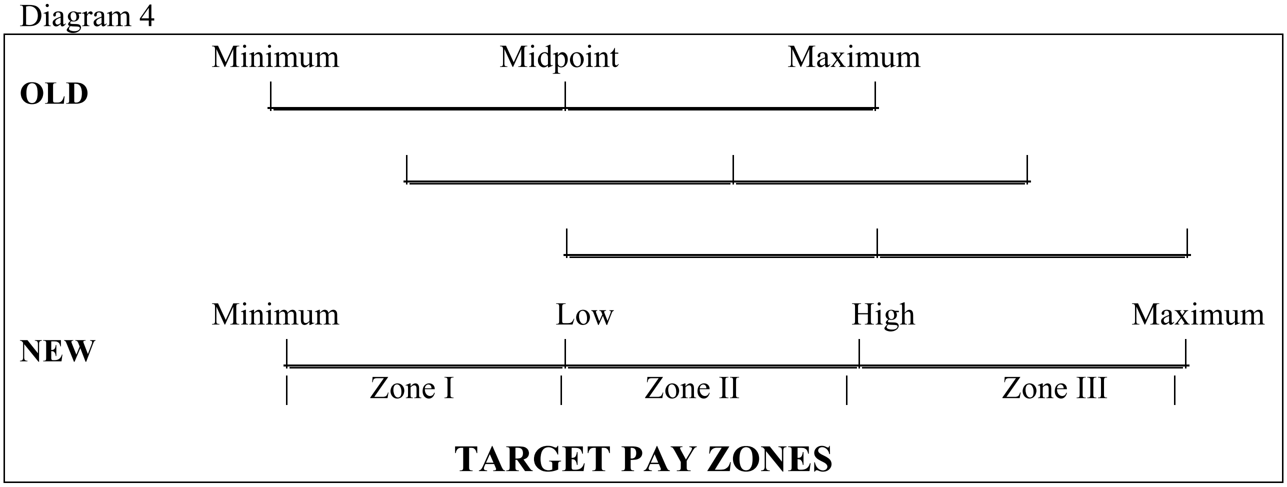
SALARY RANGE COMPONENTS

Salary ranges in a banded pay structure are much wider than in a conventional pay structure. A wider range is necessary to ensure that when multiple grades are combined into a single band, each still can be competitively priced. A typical job-family grade-to-band conversion is presented in Diagram 3, which illustrates that a banded pay range (band 5 in the diagram) must be wide enough to accommodate accountants at both the "entry" and "intermediate" levels. Similarly, one band (band 6) must be wide enough to pay both the "senior" and "master levels." A banding range spread for exempt jobs will approximate 100 percent. For non-exempt jobs, banding will result in salary range maximums, which are 60 to 70 percent above range minimums. A banded salary range is shown with three standard pay (grade) ranges in Diagram 4 to highlight the differences in range width. Because the range is so wide, and more than one job family level is contained within a band, the midpoint concept is not as helpful. Rather than targeting to price a job and pay for an experienced, competent employee at the "middle point," banded jobs and people are priced according to zones. Three pay range zones are shown in the diagram: zone I represents the bottom third, beginning at the minimum; zone II captures the middle third; and zone III spans the upper third, bounded by the maximum. The experienced, competent individual is targeted to be paid within zone ll. Range control can be achieved within banding without midpoints and compa-ratios simply by differentiating pay treatment eligibility according to the zone occupied. An employee's zone describes his or her position in range.

Diagram 3

Traditional Structure			Banded Structure	
Grade	Title		Band	Title
14	Senior Accountant	}	6	Senior Accountant
12	Accountant III	}		
10	Accountant II	}	5	Accountant
8	Accountant I	}		

Diagram 4



PAY DELIVERY

Some aspects of traditional pay administration can be imported into banding with few, if any, modifications. The concept of merit pay fits banding as well as it does systems with numerous pay grades and narrower pay ranges. In fact, performance-based pay assumes greater prominence in a system that de-emphasizes grade-to-grade-type promotions. An exempt "specialist" might only achieve one promotion to a higher band during his or her career as an individual contributor (not considering opportunities on a dual-career system), but he or she likely will receive ongoing merit reviews. Yet, when band-to-band promotions do occur, they typically yield greater promotional pay increases than in a gradebased system. If there are half as many bands as there were grades, promotional pay increase percentages for band changes are often twice the marketplace average. But, the objective of banding cannot be met with these traditional pay delivery vehicles.

It should be remembered that a key rationale for banding is lateral (horizontal) career development. Yet neither merit nor promotion pay are designed to stimulate or even reinforce developmental moves. Reconfiguring the structure changes the lines on the playing field, but it may not convince employees that the game also has changed. Too many of them have been conditioned to envision only a vertical career path, with few, if any, planned deviations. The idea of accepting two or three moves across before aspiring upward is counter-cultural.

Career development pay is a new delivery mechanism that helps to communicate the new message about career growth and pay. It is awarded for certain (inband) lateral moves. As lateral moves are not all alike, pay treatment can be varied according to the type and/ or value of the change in job. Transferring within a function like marketing is not as significant (or risky) a change as moving from marketing to sales. Similarly, moves within business units are less developmental than moves between business units. Minor changes in job assignment that do not develop new skills and competencies need not be compensated at all. Funding career development pay should not be difficult if an organization has been absorbing the cost of frequent grade-to-grade promotions. Payroll costs avoided due to significantly fewer promotions can be allocated to career development. However, budgeting career development dollars is as tricky as budgeting promotion dollars, since moves are difficult to forecast.

With career development pay, the compensation system is properly aligned to meet the more complex needs of the modem organization. Merit pay continues to reward for in-band, in-job performance. Promotion pay is available to encourage the acceptance of greater responsibility, as an employee moves vertically, band-to-band. And career development pay is available to stimulate in-band, job-to-job skill development.

JOB EVALUATION

Banding does not require a change in the job evaluation system. But a sophisticated job evaluation process, with all its precision (points), paperwork and controversy, may not be worth the investment or hassle when there are so few vertical levels (bands). An elaborate point-factor system can be dismantled in favor of a simple benchmarking and slotting process. Additionally, with all the pressure to cut head count, budgets and layers, it might be a good time to re-think evaluation criteria, especially the traditional command and control metrics (e.g., number of people supervised, reporting level, financial scope of responsibility, etc.). Whatever factors are selected should recognize the role of the professional knowledge worker. Identifying distinctions in competency and work requirements between non-manager bands, especially in a dual-career track model, should be the focus of attention in a banding job evaluation system. After all, individual contributor knowledge workers greatly outnumber managers.

MARKETING PRICING

Salary survey submission and interpretation is a challenge once jobs are banded. As there are no known surveys that are calibrated to a model with radically fewer grade levels matching a banded job to a survey benchmark is a problem. For example, the "entry-level" survey benchmark cannot be solidly matched to a particular, band since "entry level" and "intermediate level" and intermediate level positions have been family blended into a single band. Fortunately, salary survey interpretation is not as difficult after translations are made. The average rates of pay for the "entry" and "intermediate" benchmark positions, for instance, can be compared to the band that contains these two traditional levels - the band 5 "specialist."

As depicted in Diagram 5, range minimum can be compared to the lowest reported rate (or 25th percentile) for the smallest surveyed job in the band (e.g., "entry level"). Range maximum can be compared to the highest reported rate (or 90th percentile) for the largest surveyed job in the band (e.g., "intermediate level"). The same basic comparison technique can be employed with zone II low and high, except different survey statistics are needed. This middle zone should be set against the market based on an organization's pay competitiveness policy. An average position can be achieved by setting zone II boundaries at or near the 50th percentile for the two benchmark jobs that occupy the band. A richer policy would be pegged off the 7th percentile survey dates. Jobs commanding pay rates that are substantially higher than other jobs within the same band can be placed on higher market-priced pay lines.

Diagram 5

Typical Banding Market Competitiveness Study
Target Pay Zones

I		II		III

$20,000 Minimum ↑	$25,500 (Low) ↑	$32,500 High ↑	$41,500 Maximum ↑
Compare to low or 25th percentile for "entry" level in job family	Compare to desired policy position for "entry" level in job family	Compare to desired policy position for "intermediate" level in job family	Compare to high or 90th percentile for "intermediate" level in job family

Salary Survey Comparisons for Jobs in Specialist Bank
(Example)

RE-EXAMINING REWARD SYSTEM VALUES

Banding requires a re-examination of reward system values, approaches and processes, For most organizations, that means challenging a support system that has been in place a long time, and very likely looks like all the others. So, why change to banding? It is acknowledged that banding is not the answer for every firm. Many employers have sound, strategic reasons for maintaining a traditional compensation system, including the fact that their organization, hierarchy and career development system remain stable and unchallenged. But a growing number of organizations in the midst of transformational change are searching for an alternative pay structure to fit to an alternative organization structure. For them, neither status quo or incremental change is the answer. An all-new direction must be considered. For organizations that choose banding, the results can be worth the risk.

One positive outcome of banding is improved employee communication and teamwork. Fewer distinctions in level, title and status allow for a more egalitarian workplace. Also, placing every employee on the same structure, instead of differentiating according to exempt and non-exempt overtime pay eligibility, which is now the common practice, eliminates stratification based on employment class. In fact, employees quickly notice that they occupy the same pay structure as the president.

Fewer levels and structures also contribute to a simpler, less bureaucratic and fairer system. Less time is spent by both management and human resources documenting, analyzing and evaluating jobs, since there are significantly fewer leveling decisions to make. Both managers and employees spend less time making equity comparisons, as fewer levels of distinction result in fewer differences. Though banding decisions are not automatic, there are one-half to two-thirds fewer of them to make. Using multiple pay lines does add an element of complexity, but all decisions are quantitatively derived from salary survey data, thus avoiding the consensus-building delays required when decisions are qualitative and judgmental.

Another positive result of banding is the change in employee career focus. Once the structural barriers are removed, workers can consider lateral skill development moves. If career development pay is available, such moves actually can be rewarded, fostering people with both a breadth and depth of organizational knowledge and experience.

Perhaps the most significant advantage of banding is the inherent organizational flexibility created with fewer vertical break-points. Organization restructuring and downsizing result in numerous changes in job holder responsibilities. Such changes often generate actual or perceived challenges to pay grade levels. But the last thing an organization needs to bother with during a period of turbulent change is job re-evaluation. As job security is quickly vanishing and employment security is the only reasonable goal, management needs the flexibility to reassign people without the burden of job evaluation studies and the negative motivational impact of employee demotions. Banding provides more room to facilitate job changes at the same level, or band.

Yet, the advantages of banding must be weighed against some obvious disadvantages. For one thing, banding severely restricts the number of potential promotional opportunities, especially within the individual contributor job families. Although lateral career development pay and dual-career opportunities will help to fill the void, employees still will make "better-off, worse- off" comparisons to peers outside the organization.

More than one market pay line can cause confusion, and the perception of a lower (valued) class, leading to another disadvantage. It can be unclear to employees and managers who are not aware of labor market pay variations why it is financially prudent for the organization to establish two or more salary ranges for each non-executive band. Although salary survey data verify the need, few managers and almost no employees have access to or know how to analyze this information. To overcome these and other challenges to banding, effective employee and management communication and training are critical. Pay is second only to job security on the list of emotional topics. When well explained, though, people can understand how banding can benefit both them and their organizations.