

# Designing an Optimal Salary Structure



# A SPECTRUM OF DESIGN APPROACHES (AND CHOICES)

*In designing an optimal salary structure, organizations face an array of choices*



## Traditional Grades

Traditional grade structures consist of many levels with narrow spreads, limiting variances in pay for jobs within the same grade and emphasizing internal equity.



## Broadbands

Broadband structures call for wide ranges of pay, tying compensation to the market, and allowing organizations to reward performance by facilitating movement within bands.



## Pure Market Pricing

Pure market pricing is an approach rather than a structure. Employees are not placed in grades or bands, and managers set their compensation based on market data, employee performance and budget.

### A CONTINUUM WITHIN EACH APPROACH

Within each type of structure, there is a range of specific approaches. For example, organizations with traditional grades may have varying pay range widths, midpoint progressions, numbers of grades, and overlap. Similarly, market pricing practices are compatible with all types of structures and may therefore be adopted by organizations without moving to a completely structureless, pure market pricing approach.

There are many different approaches to administering pay, ranging from highly structured approaches to very flexible one. Three of the most prevalent -and distinct- salary structures include traditional grades, broadbands, and pure market pricing.

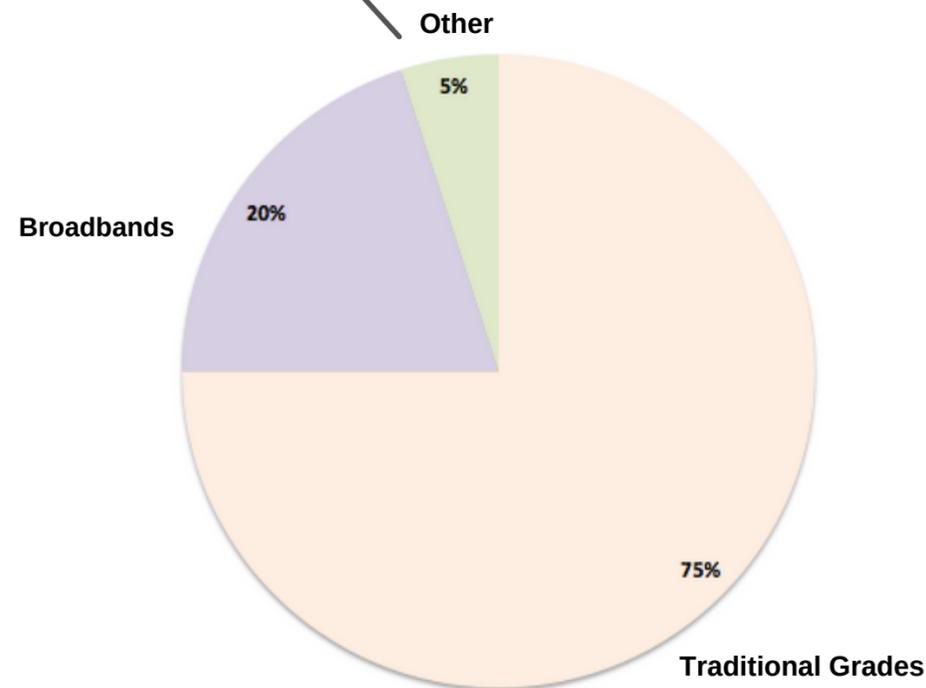
# TRADITIONAL GRADES DOMINATE

*While traditional grades remain the most prevalent approach to pay administration ...*

*... they entail more design-related decisions than less structured approaches, such as pay range width and midpoint progression.*

**Prevalence of Different Approaches to Pay Administration**

Roundtable research suggests that pure market pricing - included in the "Other" category- is used only by a minority of organizations.



Data points are approximations suggested by secondary literature

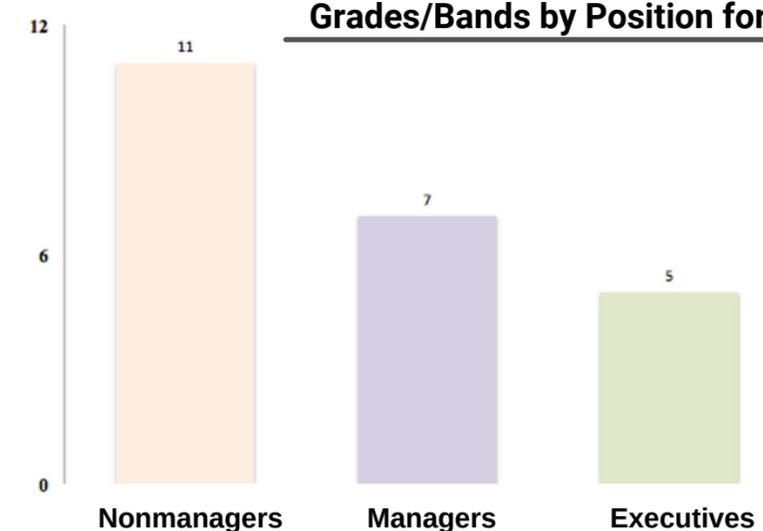
By midpoint progression, we mean the difference between the salaries paid in the midpoints of the two adjacent grades. A midpoint progression is calculated by taking the difference between the two adjacent midpoints as a percentage of the lower midpoints.

**Average Pay Range Width and Midpoint Progression by Position for All Structures**



n=37

**Average Number of Salary Grades/Bands by Position for All Structures**



n=37

Traditional grades have historically been - and still are- the most prevalent type of salary structure. However they can be complicated to design. Organizations with more structured approaches to pay administration, such as traditional grades, must make decisions regarding several key design elements, including the number of grades, pay range widths, midpoint progressions, and overlap.

# A PARADIGM SHIFT?

**Roundtable members indicate an increasing interest in more flexible pay administration approaches...**

## MANAGING TO THE MARKET

"How do companies manage their base pay? Are more organizations managing to the market, rather than a salary range?"

Compensation Professional  
Consumer Products Company

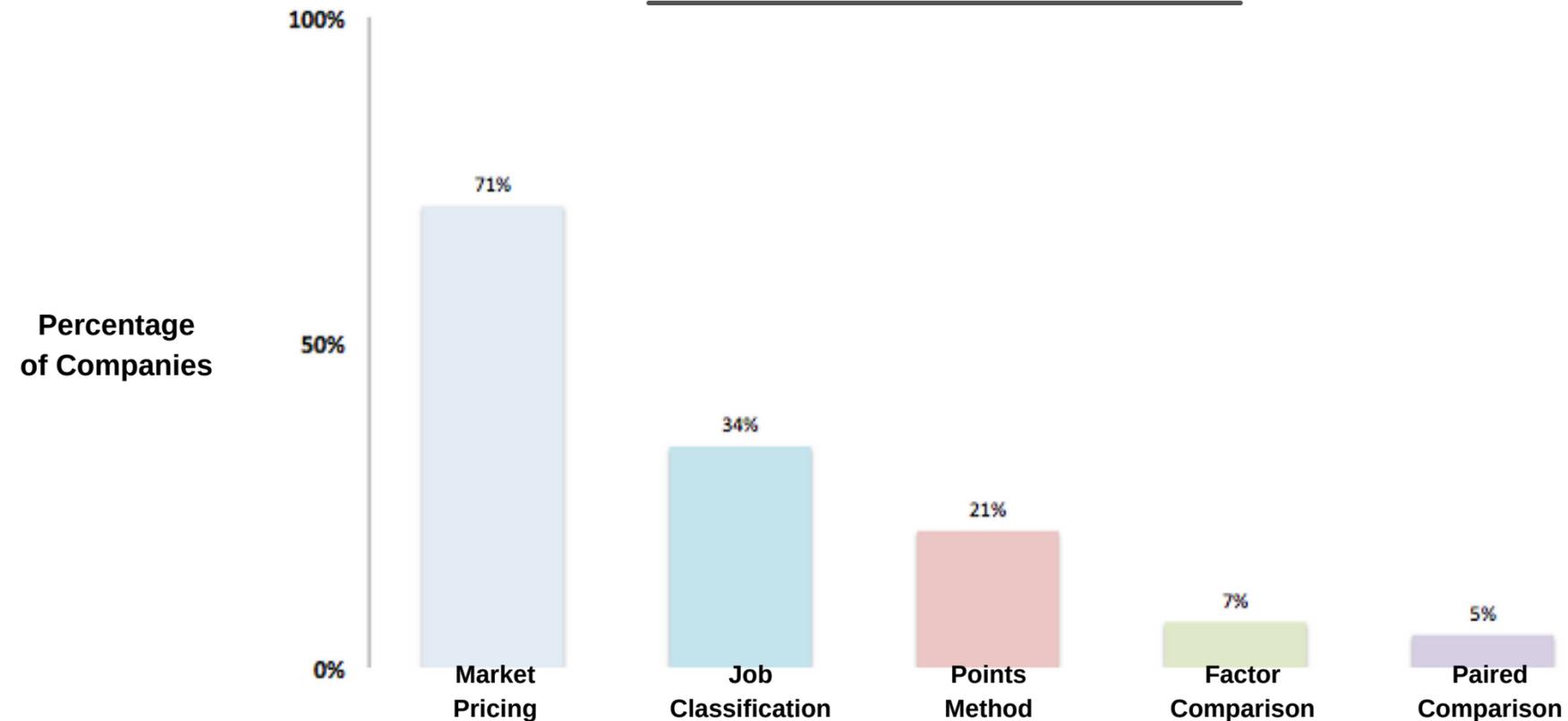
## A STRUCTURELESS STRUCTURE

"Is there a precedent for basing pay for purely on the market price without constraints of range minimums and maximums?"

Compensation Professional  
Manufacturing Company

**... which their existing use of market pricing could facilitate**

**Prevalence of Job Evaluation Methods**

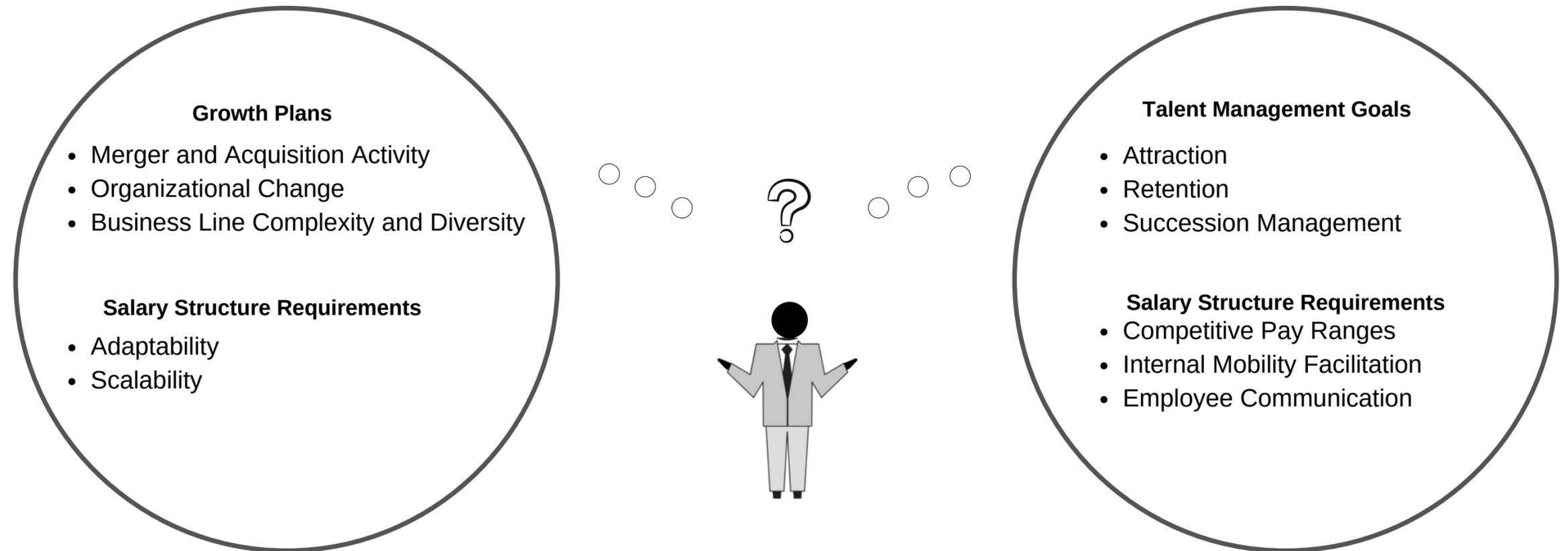


n=42

The complexities of traditional grade structures may contribute to Roundtable members' interest in exploring other, less structured approaches toward pay administration. In particular, many organizations are exploring a pure market pricing approach, which their existing use of market pricing for job evaluations (employed by more than 70% of organizations) could accommodate.

# MAKING THE RIGHT CHOICE

*Organizations must consider their growth plans and talent management goals in designing a salary structure*



Organizations should consider two key factors when designing a salary structure—growth plans and talent management goals. Growth plans include level of M&A activity, degree of organizational change, and extent of business line complexity and diversity. Talent management goals include attraction, retention, and succession management. These talent management goals, for example, may define the relative importance of certain salary structure requirements, such as adaptability and competitive pay ranges.

## Salary Structure Design Choices



Traditional Grades



Broadband with Pay Zones



Broadbands



Pure Market Pricing

# SUPPORTING GROWTH

*Organizations must consider their growth plans and talent management goals in designing a salary structure*

## Impact of Type of Growth or Operational Shift on Salary Structure Requirements

Type of Growth or Operational Shift	The Need for Adaptability— Adjusting to Changing Conditions	The Need for Scalability— Applying to Different Situations
Merger and Acquisition Activity	Salary structures must be able to integrate with acquisitions' approaches toward pay administration.	Compensation departments can more efficiently integrate salary structures following M&A when the structures are "lean" (e.g., no more grades or job descriptions than are necessary).
Organizational Change	Salary structures should be able to facilitate a shift in organizational priorities, such as an increased emphasis on career pathing and development.	Salary structures designed to ease administrative burdens (e.g., frequent requests for job evaluations) free compensation professionals to focus on more strategic issues.
Business Line Complexity and Diversity	Salary structures within growing organizations need to afford business units the flexibility to respond to market conditions in their unique geography, industry, etc.	Organizations spread across multiple geographies or lines of business need salary structures that can be easily understood and administered by compensation professionals outside of the core headquarters group.

## Selecting a Salary Structure Based on the Level of Growth or Operational Shifts



Growing and/or evolving organizations require salary structures that can adapt to changing circumstances and free compensation departments to focus on the strategic, transformational issues stemming from the change—rather than administrative, transactional issues. The level of growth or operational shifts an organization anticipates experiencing suggests what type of structure would be optimal.

# ACHIEVING TALENT MANAGEMENT GOALS

*Organizations must also consider the extent to which their design choice will pose a challenge to managing toward key talent management goals*

## Impact of Salary Structure Design on Attraction

### Traditional Grades?

Narrow ranges can mitigate runaway pay issues and help ensure internal equity, but maximums and minimums can prevent managers from paying what is necessary for attracting top talent.

### Broadbands?

Broadbands provide managers with flexibility in setting pay and providing employees with developmental opportunities and lateral moves. However, pay zones within bands could inhibit the flexibility needed for attraction.

### Pure Market Pricing?

Recruiters can clearly explain pay processes to applicants and assure them that they are paid at the market.



**Talent Management Goal: Attraction**



The nature of talent management challenges varies from one type of structure to another, and impacts an organization's ability to achieve its talent management goals. Compensation professionals need to understand how different types of salary structure designs address the challenges in meeting these goals to select the most appropriate structure.

The following three pages provide a guide to the pros, cons, and implications of each key salary structure with respect to the three core management challenges of maintaining market sensitivity, enabling career pathing, and ensuring effective communication.

