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The broad banding of pay structures to compress a large number of salary grades into fewer, wider "bands" was first introduced in organizations in the late 1980s and early 1990s (*World at Work*, 2002). The introduction of flatter, broad-banded pay structures seemed to provide a better fit in newly created, flatter organizational structures with more broadly designed jobs.

Broad banding continues to be a strategy of interest to managers seeking to improve organizational performance. During the 1990s, the number of companies implementing broad banding continued to increase from 10 percent of firms surveyed in 1993 to 23 percent in 1999 (*HR Focus*, 2000).

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A broad-banded pay structure that provided greater opportunity for employees to move laterally and acquire additional skills through extensive crosstraining was thought to be consistent with the development of a new culture in which employees would take the responsibility to develop broader skills through continuous improvement programs. The new culture also would include greater emphasis on performance improvement through paying the person rather than the job.

Managers contemplating the broad-banding strategy planned to improve organizational effectiveness by achieving several goals. They wanted to place greater emphasis upon career management to develop a workforce with broader skills (a) to improve productivity by operating with fewer employees; (b) to promote career development among employees through extensive crosstraining; and (c) to reduce the amount of time devoted to administration of activities such as job evaluation (in which jobs are ranked in order of importance to the organization). They also wanted fewer administrative problems with the traditional system based upon employee promotions in hierarchical salary structures with pay increases implemented from merit increase guide charts tied to employee positions in more restricted, narrower pay grades (*World at Work*, 2002).

Have broad-banded pay structures achieved these goals over the long run? The evidence appears to be mixed. For example, although increased focus upon career management is often cited by proponents of broad banding as an important reason for implementation, broad banding often fails to improve the career management process in organizations. Additionally, the impact of broad banding upon cost reduction has been questionable. In a 1998 American Compensation Association/Hewitt Associates broad banding study, 34 percent of the respondents did not track the impact on costs and 69 percent had not installed mechanisms for tracking the effectiveness of broad banding. Confusion regarding broad banding was also demonstrated because in the survey, only 67 percent of executives and 56 percent of managers understood the concept as practiced in their organizations (Berger & Berger, 2000).

What Is Broad Banding?

Broad banding involves the collapsing of several salary grades into a few broad "bands" with significantly larger pay ranges (Milkovich & Newman, 2002). Each band may have a minimum and maximum pay rate but usually does not have a traditional midpoint. It may not be feasible to use a traditional pay range midpoint for control and analysis because the pay range is so broad and encompasses such a wide level of skills.

Broad banding is usually implemented in two steps. Initially, three to eight wide "bands" are created to replace the normally large number of existing pay grades. Bands are established at major breaks or differences in work or skill/competency requirements. For example, bands may be created for hourly, clerical, managerial, and executive-level positions in the organization. Managers must determine how much to pay employees in the same band who perform different work in different functions of the firm. In some cases, managers have to establish different pay rates for different job families within a band in order to differentiate pay based upon market rates. For example, the pay rates may differ within the managerial band for jobs in production, finance, or marketing. Second, the market pay rates are analyzed to create an overall pay range for each band (Milkovich & Newman, 2002).

An important question for managers contemplating broad banding in their organizations is whether it will result in a new, innovative pay structure or one that is merely a "downsized" version of the old system with too many pay levels and the same administrative problems.

In a 1994 survey by the American Compensation Association/Hewitt Associates that examined why organizations had implemented broad banding, 71 percent of the participants reported supporting a flatter organization and nurturing a new organizational culture, 57 percent mentioned the promotion of a widely skilled work force and facilitation of career development, and 55 percent reported minimizing administrative effort and reducing job evaluations (Peters, 1994). Clearly, managers in organizations that have implemented broad banding believe they will have greater flexibility in directing the workforce if they can move people more readily in all directions within the organization without the constraints of narrowly defined jobs and restrictive pay grades/ranges.

While a number of authors have asserted that broad banding has advantages for employers and employees (Abosch, 1995; Haslett, 1995; Parus, 1998; Ellis & McCutcheon, 1999), others have questioned it (Berger & Berger, 2000; Milkovich & Neuman, 2002; *Ioma* . . . , 1999). Additionally, since broad banding is often implemented in conjunction with downsizing and restructuring strategies in organizations and the results of these strategies have been mixed (Cappelli, 2000), what can managers expect from broad banding?

Broad Banding and the Pay System Effectiveness Criteria

Broad banding raises important questions for managers who have flattened their organizational structures or plan to do so. Should they implement broad banding to provide a better fit with the newly flattened organizational structure with broader jobs requiring greater skill variety? To help managers consider this question, the authors will analyze broad banding by examining its impact upon the criteria normally used to examine the effectiveness of pay systems in organizations. The criteria include internal equity, external competitiveness, employee motivation, ease-of-administration, legality, and budgetary issues.

Internal Equity

Internal equity is normally of less concern in broad-banded pay systems than in those with a more traditional focus. With only a few pay bands and more broadly defined jobs, one would expect less differentiation in pay between employees and a lower probability that they would perceive internal inequities in pay.

If the pay rates for employees in the same job function are the same and based upon the market, employee internal equity perceptions may be relatively positive. Also, perceptions of internal inequity by employees who perceive themselves to be superior performers with higher pay may be offset by the improved marketability they acquire from crosstraining and broader skill development obtained under the broad-banded system.

The concerns about the impact of broad banding on employee perceptions of internal equity are serious because of the increased decisionmaking autonomy of managers under a system with more emphasis on flexibility and less on control. To gain a perspective on the issue of internal equity, it is helpful to analyze pay administration from an historical perspective. An initial reason for implementing ranges and grades in the early twentieth century was to reduce foremen administrative inconsistency and favoritism that was perceived to have a negative impact on employee relations. What if the new broad-banded system permits managers to function arbitrarily like supervisors under the old "drive system" of the early 1900s (Milkovich & Newman, 2002)? What impact would this have on internal equity for job worth and employee salaries?

If an employee is influenced by the equity theory and raises questions about the pay of other employees, how can a manager explain a difference in pay between jobs grouped in the same band? If the job evaluations are significantly different, employees expect the jobs to be in different bands or grades with different salary ranges. When job evaluations are not significantly different, employees expect jobs to have the same salary range. To what extent are jobs significantly different under broad banding to require placement in another band? If job evaluation is de-emphasized in the broad-banded system or is no longer used, how would this be determined?

Internal equity in pay between employees may be more difficult to achieve under broad banding because merit increase guide charts that base an employee's pay increase on the position of the employee's salary in a pay grade and the level of performance appraisal received are difficult to develop if grade or band midpoints are not used. The significantly wider pay ranges under many broad-banded systems make use of the midpoint impractical. The band salary range is likely to be much greater than the amount of time it would take an employee to become proficient in the job, possibly resulting in higher than necessary pay levels.

Internal equity in pay between departments and organizations in a firm has been monitored historically in part by compa-ratio analysis. The compa-ratio is calculated by dividing the average rates actually paid in a band or grade by the salary range midpoint for that band or grade. A compa-ratio greater than 1.00 means that, on average, the rates paid exceed the midpoint, which is usually pegged to the average or median pay for the skill level in the market. Compa-ratios may be computed for individual employees, departments, or an organization as a whole. A compa-ratio above 1.00 could mean that a large number of employees in the band or range have high seniority, high performance, low turnover, or low rates of promotion (Milkovich & Newman, 2002). Compa-ratio analysis is difficult to implement without pay grade midpoints for reference points. This midpoint exclusion may result in inconsistent allocation of compensation between employees or, across the organization, escalation in compensation costs and potential legal problems.

External Competitiveness

Pay tends to be market driven in broad-banded pay systems with more emphasis upon internal equity in traditional pay systems (Gilbert & Abosch, 1996). One would expect less emphasis on internal equity in the broad-banded pay system because more jobs are in the same pay grade, and they are likely to be paid the same or have very similar salary levels. When organizations have restructured to increase responsiveness to markets by encouraging employee creativity and risk taking in broadened jobs with increased skill levels and productivity, managers need to emphasize external competitiveness to ensure that salaries are competitive so that the extensive investments in employee training and development are not lost to other employers.

Unfortunately, external competitiveness is more difficult to assess under a broad-banded pay structure. Whereas many organizations using more traditional pay structures peg the midpoints of their salary ranges to the market median or average salary for a job, this arrangement is not feasible in broad-banded structures without viable midpoints. Additionally, if jobs are wider in scope under a broad-banded system, it is likely to be more difficult to obtain labor market data for comparison. The use of benchmark jobs (common in industry and used for comparing salaries) may be more difficult because other organizations are unlikely to have broad-banded jobs in a similar manner, and jobs may be significantly different from one organization to another.

In a broad-banded pay system in which jobs have been combined and employees are crosstrained to have broader skills, benchmark jobs may be more difficult to identify, making it difficult to match and price jobs in labor markets. Managers may be uncertain whether salaries are competitive if survey data are more difficult to acquire and analyze. It may be significantly more difficult for managers to decide at what point to establish their pay policy lines in relation to competitors in each labor market.

Some experts have argued that individuals should be priced in the market, not jobs (Lawler, 2000). While this idea is true for people with highly specialized skills such as National Basketball Association players, for most employees, especially those working in flattened organizations in which jobs have been broadened significantly, it is very difficult to obtain market data based upon an individual, a skill, or a competency. For example, what if one is trying to acquire market salary data for a secretary with computer programming skills, should the analyst compare salaries to secretaries or computer programmers (Tyler, 1998)? While it is also true that individuals leave organizations, not jobs, and external equity concerns should be based on attracting and retaining the required talent, it is still true that most market data are based on jobs. Therefore, employers usually must acquire salary data for jobs and then differentiate the data on the basis of skills required in their organizations. Broad banding, when accompanied by increasingly broader ranges of skills in the same job, makes acquiring relevant comparison data in the market even more difficult.

Additionally, a significant number of managers in organizations that have implemented broad banding do not appear confident that the survey data they have been given are accurate for their employees. In one study, while most of the managers reported that they understood how salary survey data were collected, only 47 percent said that they were provided data regarding how employee pay relates to the market, and only 42 percent of them felt that it accurately reflected the market for employees in their company (*Ioma* . . . , 1999).

The lack of accurate pay survey data will make it more difficult to determine salaries for employees entering the organization. This fact can have a negative impact on the ability of managers to recruit, select, and retain competent employees.

Employee Motivation

In broad-banded pay systems, employees are encouraged to pursue the development of job skills instead of focusing primarily on skills they need to achieve the next promotion (*Ioma* . . . , 1999). The career development approach in which employees acquire a wider range of skills to make them more valuable to the organization and more marketable externally provides a good fit for organizations that have downsized recently. Employees in such organizations are likely to be motivated significantly by career development programs that will make them more marketable.

If the broad-banded pay system encourages employees to develop wider skills, it would help managers implement job enlargement or enrichment programs to make the work more challenging and interesting, especially if the work system is changed to a team orientation. The broad-banded system would de-emphasize structure and control and place greater emphasis upon judgment and flexible decisionmaking for managers (Mondy & Noe, 2002).

Broad-banded pay ranges provide more opportunity for upward movement in pay with increases less constrained by salary range maximums. This flexibility should provide an opportunity for managers to grant more significant pay increases to increase motivation. Fewer cases in which a manager will have to tell an employee that the pay increase would have been higher if the employee were not at the top of the pay range should occur. In one large organization that had implemented broad banding, senior management reported that they received more thoughtful recommendations for promotions because managers did not need to promote people to get a raise simply because they were at the band ceiling (Tyler, 1998).

On the other hand, broad-banded pay systems can create motivational problems. Managers have far more flexibility in assigning people to work and determining their pay levels as well as the amount of pay increases. The increased flexibility is a positive development if the managers are competent, relatively unbiased, and not motivated to use their newfound source of power for political reasons. It takes only one or two managers operating unscrupulously with favoritism or political manipulation for employee motivation to be adversely affected. Can organizations utilize the old control strategies of job evaluation, salary range midpoints pegged to medians in the market, merit increase guide charts, etc., to prevent adverse affects on motivation and monitor internal equity in the broad-banded organization? It seems unlikely, since one of the primary reasons for broad banding is to provide more flexibility for managerial decisionmaking. Managers so empowered may be unlikely to subscribe to old constraints placed upon their newly acquired freedom to act.

The impact of fewer promotional opportunities on employee commitment cannot be underestimated. Organizations with broad banding claim it provides broader skills and marketability for employees, but while 87 percent of employees in the 1998 American Compensation Association/Hewitt Associates survey indicated broad banding allowed them to develop skills in their current jobs, only 60 percent said they could apply the skills to a different job (*Ioma* . . . , 1999).

Managers are apt to be more sensitive to the probability of higher turnover in a broad-banded pay system in which some employees may be more likely to leave because of the lack of promotional opportunity. Managers may react by granting merit pay increases even more freely than in a traditional pay system, making the leniency effect in performance appraisal even more pronounced. This effect, in turn, could escalate compensation costs significantly.

How does broad banding impact upon the administration of merit pay and, in turn, employee motivation? Merit pay remains the most common means of rendering pay increases, and any analysis of broad banding should include its impact on merit pay. In organizations with very few bands, it would be very difficult to use merit increase guide charts with pay increase parameters based upon one's performance level and position in the "band." Yet, in a broad-banded structure, differences in pay between employees in the same band may need to be justified largely on differences in performance levels. In short, broad banding is likely to bring increased pressure on managers to develop and implement effective performance appraisal systems—an elusive goal in many organizations already. Many employees are likely to conclude that jobs in the same band should be paid similarly, otherwise why are they in the same band in the first place?

Data from the American Compensation Association/Hewitt Associates study in 1998 indicate two areas of concern that developed among organizations using broad banding: the lack of continuous emphasis on career development and the failure to maintain effective communication with employees after introducing the program. Many of the organizations did not have formal career planning processes and failed to develop them in conjunction with the broad-banding efforts. The need for more effective communication is becoming more critical as firms extend broad banding deeper into the organization, e.g., in 1998, 39 percent of the organizations in the American Compensation Association/Hewitt Associates survey had implemented broad banding for hourly jobs, up from only 22 percent in 1994 (Parus, 1998). Career development and effective communication are very important in sustaining employee motivation.

Ease of Administration

Broad banding has been implemented in a number of organizations to provide a better fit between a newly created, flatter organizational structure, the requirement for employees with broader skills to function in more broadly defined jobs, and a flatter pay structure (*World at Work*, 2002). It is often implemented to reinforce organizational change efforts that have already taken place (*Ioma . . .*, 1999).

Proponents of broad banding have stated that it provides administrative flexibility for managers by enabling them to move employees laterally so they can acquire depth of experience and broader skills. This movement can help motivate employees in downsized organizations with fewer promotional opportunities. Additionally, with fewer job titles in a system with emphasis upon more broadly defined jobs, the amount of management time and effort required for other administrative activities such as job evaluation should be reduced.

While administrative advantages exist for managers under the broad-banding approach, the potential for administrative difficulties also exists. For example, traditional pay system control mechanisms may be far more difficult to apply in a broad-banded pay system. Merit increase guide charts that provide guidelines for managers to use in determining the level of merit pay increases may be difficult to use when salary ranges are so broad that midpoints are not feasible.

Reasonably accurate salary survey data to analyze external competitiveness may be difficult to acquire with fewer benchmark jobs under broad banding. Fewer promotional opportunities under flatter organizational structures with broad-banded pay systems may result in lower employee motivation and commitment, creating pressure for administrative changes.

Managers who have implemented broad banding have encountered a number of other administrative problems that have made it difficult to sustain the strategy in the long run. For example, broad-banded systems often suffer from a lack of clear guidelines regarding how to pay new hires or how to place and move individuals within the bands. Broad banding policies often do not explain why some employees should be paid higher in the band and others lower. Also, how can an employee move up in the band, especially if changing jobs within the same band is not considered a promotion?

The lack of control mechanisms inherent in many broad-banded pay systems can lead to dissolution of the system in the long run. Many organizations end up creating zones within the bands to enable managers to know where to place jobs (Milkovich, 2002). In effect, the new zones create new pay grades within the bands, thereby negating one of the main purposes of broad banding—to reduce the number of pay levels. When this occurs, what is the real difference between the old, more hierarchical pay structures with more pay grades and the so-called new broad-banded approach?

Some critics of traditional job-based pay systems have argued that they do not reward employees for lateral moves that lead to cross-functional learning or learning to do one's job better (Lawler, 2000). Should people be paid more for lateral moves if their accountabilities are no more significant to the organization? If the lateral move results in learning to do one's job better, the employee could be paid more because of improved performance, assuming the performance appraisal system differentiates performance properly.

Job size and seniority have been the largest predictors of an individual's pay (Lawler, 2000). It is unlikely that broad banding would permit greater differences in pay based upon job size because it would be more difficult to tell which jobs in a band were of significantly larger size or how much larger they were. While broad banding reduces the number of pay grades, it also blurs the distinction between jobs in terms of job dimensions. For example, what if a firm has ten manufacturing plants of significantly different sizes in terms of budget and the number of employees? With few pay grades, how could management justify the needed differences in pay between these jobs? It is unlikely that ten different grades would be available in which to slot the jobs. Additionally, if a manager wanted to differentiate an individual's pay based upon seniority in a broad-banded structure, it would be more difficult to do so with more employees grouped into fewer pay levels.

Any pay system that is difficult to understand is likely to create significant problems in administration. Researchers in the American Compensation Association/Hewitt Associates 1998 study found that many employees needed help in understanding broad banding. Yet, while 73 percent of the organizations that had implemented broad banding communicated about it during introduction, many did not continue to communicate subsequently (Parus, 1998). If employees do not understand a compensation system, they may regard it with mistrust, suspicion, and apprehension—attitudes inconsistent with higher performance.

Legal Issues

Many of the legal concerns present under traditional pay systems are also present with broad banding. However, with increased flexibility and less emphasis upon controls in broad banding, legal culpability may increase if management is not vigilant. If administrative control systems such as merit increase guide charts, benchmark jobs, and compa-ratio analysis are more difficult to apply with broad banding, pay administration could be inconsistent, and the potential for legal problems could escalate. Additionally, it could be significantly more difficult to defend pay practices with labor market data, since such data are more difficult to acquire. The flexibility granted under broad banding could turn out to be a double-edged sword and require even more monitoring than under traditional pay structures.

Budgetary Issues

To the extent that broad-banded pay structures provide a better compensation fit with flattened organizational structures and help to improve productivity, the impact upon the compensation budget may be positive. However, concerns have been expressed that broad banding may make it more difficult for organizations to control costs (Mondy & Noe, 2002; *Ioma* . . . , 1999; Tyler, 1998).

If managers are not trained regarding the management of compensation, and fewer monitoring tools are available to control costs, the significantly deeper pay ranges under broad banding in which a single range may be $40,000 to $150,000 per year may result in the unnecessary movement of too many salaries toward the top of the range (Tyler, 1998). One study of the use of broad-banding structures in the federal government found that broad-banded structures were associated with more rapid increases in compensation costs than traditional pay structures (Martocchio, 2001). The greater latitude of managers in assigning pay to employees under broad banding, with less emphasis on cost controls than under the traditional approach, could result in budgetary cost overruns.

The pressure on managers to obtain pay increases for their employees under conditions in which promotional increases are more difficult to achieve could lead to greater leniency in performance appraisals and greater pressure on pay budgets already pushed to the limit. Managers also could begin to press for more pay levels in the structure to permit them to promote people more readily. These situations could lead to a return to the more hierarchical pay structure the firm was trying to eliminate in the first place.

When Is Broad Banding Most Effective?

Studies in 1999 by Hay Associates and in 1998 by the American Compensation Association/Hewitt Associates found that broad banding is most effective when it is used to support changes in culture or structure, the organization has current market data to price jobs competitively, and managers understand it clearly (*Ioma* . . . , 1999).

Conclusion

The desire for greater management flexibility in conjunction with downsizing in many organizations may foster continued efforts to implement broad banding, but as with the implementation of any other changes in compensation, managers should proceed cautiously.

The impact of broad banding on the achievement of pay system effectiveness may be far more negative than anticipated. The desire for greater management flexibility in conjunction with downsizing in many organizations may foster continued efforts to implement broad banding, but as with the implementation of any other changes in compensation, managers should proceed cautiously. Only time will tell for certain, but recent evidence seems to indicate that the rate of implementation of broad banding may be declining, and the strategy may not continue to proliferate as widely as predicted in the early 1990s. For example, the number of firms considering broad banding declined steadily from 39 percent in 1993 to 18 percent in 1999. Also, while the number of companies using broad banding grew from 10 percent in 1993 to 21 percent in 1997, the rate of increase appears to be flattening out because only 23 percent reported using it in 1999 (*HR Focus*, 2000).

Before implementing broad banding, managers should consider how it would impact upon the important criteria for evaluating pay system effectiveness in their organizations.

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