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Skill-Based Pay: Fad or Classic?

Frank L. Giancola, HR Researcher and Writer

Abstract

Paying employees based on their skills and abilities rather than their current job is an idea that has been around for more than 25 years. Despite strong support from leading experts, it has not achieved the level of use that many expected. Although it continues to be recommended, usage has actually declined in recent years. This article examines the skill-based pay concept using an innovative tool that applies eight criteria to determine if an idea is a management classic or passing fad. It identifies the reasons why the pay practice has endured, despite bearing the markings of a fad.

Keywords

skill-based pay, pay practices, competencies, management fads

Compensation management has had its share of potential “silver bullets” designed to provide a deceptively simple remedy to an intractable problem or a looming crisis. Despite strong buildups, many do not deliver the promised results for a variety of reasons, including execution complexities, limited applications and economic pressures. Gainsharing plans and broad-banded salary structures are examples of concepts that have not lived up to their billing.

Today, an important concept is skill-based pay (SBP), which calls for pay to be based on the skills and competencies of individuals rather than their current job. SBP, however, is different from other “silver bullets” since it has remained at the top of the agenda of compensation professionals for more than 20 years, primarily because of the sponsorship of prominent experts. Despite its tenure and visibility, interest has slowed in recent years and job-based practices still dominate the profession, according to Mercer Human Resources emerging practices surveys of more than 1,000 firms in 2002 and 2009, as shown in Table 1. Its failure to grow is one probable reason why some experts have wondered if it is classic idea or fad that cannot stand the test of time.¹

To sort out these quandaries, researchers have developed eight criteria for separating management fads from true classics based on studies of the life cycle of new management ideas over a 17-year period in approximately 1,700 publications. They found that although fads introduce useful ideas, they do so at a cost and do not always deliver promised results.² This article applies those criteria to the concept of SBP to assess its value and to demonstrate how HR practitioners can evaluate new management ideas.

Definition and History

SBP is an alternative to traditional job-based pay. It sets pay rates based on how many skills and competencies employees have, or jobs they potentially can do, not on the job they hold. An employee’s skills are valued based on external market skill surveys that replace internal job evaluation plans and external job surveys.

The skill-based term is frequently used to refer to plans for hourly and lower level salaried employees, whereas competency-based pay is used for professional and managerial employees. The concept is recognizable by the phrase, “pay the person, not the job,” and is sometimes referred to as people-based pay.

In the 1970s and 1980s, SBP was made popular by experiments to improve the quality of work life for hourly employees.³ Skill-based plans were used successfully with production workers in greenfield manufacturing plants that also featured employee participation programs. Semiskilled workers were cross-trained to perform each other’s tasks and paid a common rate, improving workforce flexibility, staffing levels and employee satisfaction. Experts saw hope for extending the idea to other organizations and workers, including professionals and managers.⁴

At about the same time, job evaluation systems and job descriptions came under sharp criticism by a noted expert and SBP advocate, Edward Lawler, who believed that the

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Table 1. Percentage of Firms Using Skill- and Competency-Based Pay Plans

	2002	2009
Skill-based pay	19%	12%
Competency-based pay	17%	13%

Sources. Mercer Human Resource Consulting. 2002/2003 U.S. compensation planning survey executive summary, 1-6. Mercer Human Resource Consulting. 2009/2010 U.S. compensation planning survey executive summary, 1-6.

Table 2. Fad Characteristics

- Simple
- Prescriptive
- Falsely encouraging
- Easy to cut and paste
- One size fits all
- In tune with the Zeitgeist
- Novel, not radical
- Legitimized by gurus

Source. Miller, D., & Hartwick, J. (2002). Spotting management fads. *Harvard Business Review*, 80(10), 6-27.

old systems perpetuated an obsolete, bureaucratic style of management.⁵

In the 1990s, SBP received a boost from a popular futurist who claimed that the job had outlived its usefulness as a way of organizing work and was a “social artifact.”⁶ The rise of the knowledge worker, contingent employment and project-based work were cited as reasons for its demise.^{6,7}

Interest in applying SBP to knowledge workers—competency pay—was also increasing at this time.⁸ This development was influenced by studies identifying the behavioral characteristics of successful managers and the application of a new management tool—organizational competencies—to strategic human resource management. Thought leaders counseled that competencies are the “DNA of the corporation”⁹ and the “most powerful way to prevail in global competition.”¹⁰

Despite criticisms of job-based pay, optimistic forecasts and heavy promotion of SBP, the job has not been seriously challenged as the focal point for pay decisions. In recent years, articles have offered remedies for a movement that is “struggling at best,” according to compensation experts.¹¹ Significant issues include underestimating training needs, execution issues relating to skill certification, burdensome paperwork, defining competencies and a lack of systems to value skills externally.¹²⁻¹⁵

In the paragraphs below, SBP is examined against the eight criteria of fad identification, as shown in Table 2, in contrast with the hallmarks of classic management ideas.

Simple

Fads are easy to understand, communicate and usually are framed with labels, acronyms, buzzwords and lists.² SBP is a simple concept that is easy to understand—base pay should be based on the skills, knowledge and competencies of the employee, not on the job he or she holds.

Since the early 1990s, a label has been used to communicate the concept, “pay the person, not the job,” which expresses the opposite thought of the cardinal rule of traditional job analysis—consider the work, not the abilities of the job holder, to determine a pay rate. The acronym—SBP for skill-based pay—is associated with the concept of paying the person.

Buzzwords that were used in the 1980s to explain it include skill set, process, lean staffing, employee involvement, quality of work life and self-managing teams. In later years, the following were used—total quality management, core competency, role, knowledge workers, flatter and delayed organizations, contingent workers and web based. A list of action steps is typically provided.^{1,16}

Prescriptive

Fads are characterized by being too prescriptive. They indicate specific actions to solve problems or improve companies. Although the basic ideas might be sound, the need to be simple but prescriptive makes their recommended actions easy to misinterpret or to apply inappropriately.²

The SBP movement is guilty of being overly prescriptive. Instead of conveying their bottom-line message that a highly skilled workforce is key to competitiveness, and then leaving it to organizational leaders to decide on the appropriate actions to improve skills, SBP advocates went further and told them how to do this in ways that were likely to cause confusion and a lukewarm reception in the field. Surveys of HR practitioners have not been conducted to learn why most have decided against SBP, but some of the probable reasons are outlined below.

Advocates advised that employees must be paid to improve their skills through base pay increases.¹³ This was probably news to the many managers who for years had been asking employees to attend training programs, paid for by the company, without increasing their pay. Most employees jump at the opportunity to improve their job skills, because of what it means for their careers and marketability. Recent surveys show that skill acquisition and career development rank among the top three rewards for retaining and engaging employees.¹⁷

The need to be simple posed a major problem. The SBP model omitted as a pay determinant the importance of an employee’s work to achieving company objectives; only skills were to be counted. Managers knew work still had great significance in pay matters, and with this gap in logic,

SBP would lack broad acceptance by employees. Experts argued for the continuing importance of work in the pay equation.¹⁸⁻²⁰

Simplicity also contributed to another stumbling block when the skill-based model was applied to professionals and managers. Instead of offering a more appropriate basis than skills, such as broad abilities, which might complicate the concept, SBP advocates suggested pay-for-skill applications that were unconvincing, such as paying HR managers for learning accounting and production managers for mastering typing skills.⁴ Controversy also arose in 1998 among experts as to what constitutes appropriate competencies for professional and managerial employees, a complexity that remained unresolved as of 2007, according to one expert.^{14,21-23}

Today, another complication has emerged that receives insufficient attention. According to Mercer's 2009 survey of 1,100 companies, 42% are using competencies in performance management systems compared with 13% for base pay systems.²⁴ SBP advocates seldom explain why this is the case, or if one application is more effective than the other or how the two should be integrated at one firm.²⁵

Also, by emphasizing pay issues and using the slogan "pay the person, not the job," the SBP concept sounded like a compensation program, when it is just as much a training and development program. This probably contributed to major execution problems in this area.^{12,20,26}

In sum, advocates did not address a number of important practical issues adequately from the start, and when full treatment was given in their later works, the new idea seemed to present as many issues and complexities as job-based plans.

Falsely Encouraging

Fads promise outcomes that rarely occur. They are better at raising hopes than delivering results and provide no criteria for success.²

The SBP movement is premised on several claims that are unproven, may never occur, and would be recognized as such by HR professionals. These claims include the following:

- Skill-based systems will produce substantially different pay levels than job-based systems for the same work.
- Employees will not improve their skills, knowledge and competencies unless offered pay increases for doing so.
- SBP systems will free employees from the restraints imposed by job-based systems, such as job descriptions, so they will contribute more to the organization.

In addition, advocates have not always explored potential weaknesses of the concept that discourage its use. When a longitudinal study of 97 skill-based plans found positive outcomes for the 61% of the plans that survived, researchers did not investigate the reasons why 39% did not survive—information that might assist in the decision to adopt or discontinue a SBP plan.²⁷

In 1985, researchers found that about half of the corporations that were inclined to use the concept again would do so only under the right circumstances, but they did not investigate those circumstances.²⁸ Researchers have also noted that the presumed reasons why companies use skill-based plans—for example, to improve flexibility and productivity—seem supported in case studies but are largely untested empirically.²⁷

One Size Fits All

Fads claim universal relevance, and adherents propose practices applicable to almost any industry, organization and culture.² SBP advocates took a concept that had been successful in a very limited setting—semiskilled hourly employees working in greenfield manufacturing plants with a process technology—and tended to see the possibilities of future applications, even though new applications had not been tried.

Practitioners were told to avoid seams in pay policies between groups of employees, suggesting that SBP could be applied to all employees. Articles were written in the 1980s and 1990s to report the idea catching on, its advantages in additional work situations and a future that was "quite bright."^{4,29,30}

In 1985, research was specifically done to investigate the idea that SBP plans are used only in certain narrowly defined settings, for example, only in manufacturing settings.²⁸ In 1994, an SBP proponent suggested that organizations might one day be designed around people and their skills, rather than jobs, which would seemingly provide unlimited opportunities to apply the approach.³¹

In 2000, when the idea began to struggle, adherents began to moderate their enthusiasm and stated that no single type of pay practice should govern pay practices for an entire organization.¹³ In 2008, another stated that certain types of organizations, especially capital-intensive manufacturers, were better suited than others to SBP.³² One expert noted that the concept works best for skilled trades and production employees.³³ Competency-based plans are most commonly used with managers, supervisors, professionals and technicians.³⁴

Easy to Cut and Paste

Fad management ideas must be simple and easy to apply. Fad features can be grafted onto existing procedures and

localized to departments. Outside these pockets, it is business as usual, and the organizational status quo remains unchallenged.²

To date, SBP has been a “cut-and-paste” phenomenon. Reports of a major firm that has applied it on an organization-wide basis could not be located. Participation reports typically state that plans exist “somewhere in the organization”²⁹ and typically are applied to a small percentage of employees.³² A recent study of 20 companies that have adopted a competency pay system found that only 25% were using the plan with all employees and 50% were using it with core or all professional employees.³⁵

At the outset, SBP was promoted as a replacement for job-based pay systems. Today, we are told that it can take many forms from base pay to bonuses.³² Firms can now take credit for offering SBP if, for example, its IT professionals receive cash bonuses for obtaining skill certifications from software manufacturers.

In Tune With the Zeitgeist

Fads resonate with the pressing business problems of the day. Because they focus on the concerns of the moment, they tend to apply to a few specific issues rather than addressing the fundamental weaknesses or soundness of overall business practices.²

SBP has benefited from being in tune with the times for two decades. In the 1970s and 1980s, SBP was associated with work innovations in U.S. factories that gave workers more control over their jobs to improve the work experience, productivity and product quality in globally competitive markets. Concurrently, criticisms of job evaluation programs, which are complex and labor intensive, may also have struck a chord.

In the 1990s, it was linked with the rise of the knowledge-based organization, the demise of the job, flatter organizations, rapidly changing job demands and the new employment deal. Today, when execution issues are foremost, the web is the remedy.

Has SBP addressed a fundamental weakness in business practices by suggesting that pay should be based more on the person, not on the job? It is possible, but without more evidence, one cannot state with certainty that a real problem exists and SBP is the answer. Its slow, piecemeal adoption is one indication that business has not wholeheartedly bought the proposition.

Novel, Not Radical

Fads grab attention by their apparent novelty. But their freshness is often superficial, and they do not challenge basic management values. They simply repackaged or extend existing ideas that have been embraced.²

Adherents admit that their idea is not completely new and have cited instances where skill-based practices, such as career ladders and hourly generalists, were used prior to the initiation of the original SBP plans. They have recommended expanded use of those practices.^{4,13}

A review of classic compensation works published before SBP gained notoriety reveals that it can claim few fresh concepts. In 1972, the idea for determining base salary on an individual’s skills was clearly expressed by Charles L. Hughes in the *Handbook of Wage and Salary Administration*.³⁶ Hughes also used the same justifications for adopting the concept, and, surprisingly, the language that is used today—rapidly changing organizations, project work, unstable jobs, shifting from jobs to roles, rigidity of job descriptions, disappearance of the job and outdated functional organizations.^{13,37}

In 1968 and 1974, the concept of paying the person, not the job, was expressed in two books by well-known compensation experts.^{38,39} In 1975, the idea of analyzing jobs according to measures of human performance was considered by psychologists,⁴⁰ and in 1983, two methods of job analysis based on personal attributes were in use.⁴¹

In sum, the SBP movement was founded on known pay practices and existing concepts.

Legitimized By Gurus and Disciples

Many fads gain credibility through the status and the prestige of their followers rather than by empirical evidence.² Over the years, SBP has received support, in varying degrees, from some of the most prestigious names in the field of employee compensation, including Edward Lawler, Patricia Zingheim, Jay Schuster and Gerald Ledford. Despite its troubles, it is still hailed by some as the next great thing in pay and benefits and the compensation system of the future.^{42,43}

Researchers have noted, “Unfortunately, there are very few empirical studies on the determinants of SBP success. As a result, issues that are basic to both theory and practice on SBP have gone unexamined.”⁴⁴ In 2005, researchers observed, “The body of research evidence regarding its [SBP’s] effectiveness across contexts lags far behind its use in practice.”²⁷

Signs of a Classic

Following are the signs of a classic management concept and an evaluation of whether SBP exhibits those signs:

- Classics demand real organizational changes at significant costs and have lasting effects.² A SBP plan can demand real organizational change, at a significant cost and have lasting effects for

organizations that have not grasped the importance of a highly skilled workforce to their survival.³¹

- Classics typically arise not from the writing of academics or consultants but emerge out of responses to economic, social and competitive challenges.² It is not clear where SBP plans were first used. They first came to prominence in the 1960s in Norway through the work of an academic, Einar Thorsrud, and were used with semiautonomous teams of hourly employees who were expected to learn all the tasks necessary to operate a plant.⁴⁵

In their earliest applications at Volvo, the effort was supported by the company out of a business need to make industrial work more attractive to a more educated workforce and to increase competitiveness by improving productivity.⁴⁶ Since at least the 1980s, the concept has been promoted in the United States by academics and consultants.

- Classics are “complex, multifaceted, and applied in different ways in different businesses.”² SBP plans are complex and all phases of establishing one have proven to be difficult tasks. They are multifaceted and must be integrated with other reward systems, human resource programs and business strategies. Finally, they can be applied in different ways in different businesses.
- Classics do not come with “simple primers” and do not have “simple rules” or “guaranteed outcomes.”² SBP initially did not come with a primer. If it did, HR professionals would have recognized its complexity. It does come with a simple rule, “Pay the person, not the job,” which makes it sound like a pay plan, when it actually was much more. Frequently mentioned outcomes include a workforce motivated to learn new skills, retention of people with high levels of knowledge, increased workforce flexibility, lean staffing and a reduction in management.

Conclusion

There is no perfect test to distinguish fads from classics and their features can overlap. Sometimes fads can start major organizational change, although they are short-lived. Classics can receive the support of gurus. However, if a management practice exhibits most of the fad features and looks too simple, it usually is a fad.²

SBP has many features of a fad, but it also has important features of a classic, as noted. It could be classified purely as a classic, except that its underlying assumptions

have not been proven, and no evidence has been provided that the changes it promises cannot be achieved through other methods. Advocates have acted as though the assumptions are facts and have used techniques to promote the approach that characterizes a fad.

Simplicity was emphasized, a slogan was adopted, and buzzwords were employed. The concept was presented as an idea whose time has come, although the justifications for adoption have not changed in 30 years, and the pay practices and concepts are old. It has been featured as a pay program rather than a full-blown HR program, with heavy involvement of training and development, which in part has contributed to underestimating the formidable tasks that have hindered adoption. When first promoted in professional journals, reasons to discourage its use in any organization were hard to find.

Its record of adoption has been spotty for practical and conceptual reasons. Because it comprises several distinct pay practices, it can be implemented piecemeal, to advantage, without a firm changing its reward philosophy. Some, and possibly all, forms of its pay practices were in place at major companies before the attention turned to SBP. Adoption may also have been slowed for conceptual reasons by HR professionals who believe that the job is an accurate reflection of the skills of the jobholder, and employees will acquire new skills without pay incentives to ensure their marketability in the job market.

Interest in the concept is not growing, skill/competency identification and certification issues appear unresolved and a system for externally valuing skills has not been developed. If one were to hazard a guess, the advocates of SBP will have to be satisfied with the attention they have drawn to the importance of employee skill and competency development and to an underutilized pay practice. HR practitioners should continue to apply the concept as appropriate and monitor efforts to resolve execution issues that would support its broad acceptance and continued relevance.

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