EFFICIENCY
- Performance
- Quality
- Customers
- Stockholders
- Costs

FAIRNESS

COMPLIANCE
Chapter 3

Defining Internal Alignment
Learning Objectives
After studying Chapter 3, students should be able to:

1. Explain why internal alignment is an important pay policy issue and how to evaluate internal alignment.
2. Discuss the dimensions that comprise a pay structure and factors that influence it.
3. Discuss the pros and cons of egalitarian and hierarchical structures and how they relate to strategy.
4. Discuss the impact of internal pay structures on efficiency, equity, and compliance in the pay system.
Compensation Strategy: Internal Consistency

- Supports Work Flow
- Supports Fairness
- Directs Behavior Toward Organization Objectives
Internal alignment, often called internal equity, refers to the pay relationships between the jobs / skills / competencies within a single organization. The relationships form a pay structure that can support the workflow, is fair to employees, and directs their behavior toward organization objectives.
Internal Consistency: Engineering Job Structure at Lockheed

Entry Level

**Engineer:** Limited use of basic principles. Close supervision.

**Senior Engineer:** Full use of standard principles and concepts. Under general supervision.

**Systems Engineer:** Wide applications of principles and concepts, plus working knowledge of other related disciplines. Under very general direction.

**Lead Engineer:** Applies extensive knowledge as a generalist or specialist. Exercises wide latitude.

**Advisor Engineer:** Applies advanced principles, theories, and concepts. Assignments often self-initiated.

**Consultant Engineer:** Exhibits an exceptional degree of ingenuity, creativity, and resourcefulness. Acts independently to uncover and resolve operational problems.

Recognized Authority
Pay structure, refers to the array of pay rates for different work or skills within a single organization. The number of levels, differentials in pay between the levels, and the criteria used to determine those differences create the structure.
Internal Consistency: Engineering Pay Structure at Lockheed

<table>
<thead>
<tr>
<th>Level</th>
<th>Position</th>
<th>Salary</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entry Level</td>
<td>Engineer ($40,000)</td>
<td>Limited use of basic principles. Close supervision.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Senior Engineer ($58,500)</td>
<td>Full use of standard principles and concepts. Under general supervision.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Systems Engineer ($73,000)</td>
<td>Wide applications of principles and concepts, plus working knowledge of other related disciplines. Under very general direction.</td>
<td></td>
</tr>
<tr>
<td>Recognized Authority</td>
<td>Lead Engineer ($93,000)</td>
<td>Applies extensive knowledge as a generalist or specialist. Exercises wide latitude.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Advisor Engineer ($120,000)</td>
<td>Applies advanced principles, theories, and concepts. Assignments often self-initiated.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Consultant Engineer ($162,000)</td>
<td>Exhibits an exceptional degree of ingenuity, creativity, and resourcefulness. Acts independently to uncover and resolve operational problems.</td>
<td></td>
</tr>
</tbody>
</table>
What Shapes Internal Structures?

EXTERNAL FACTORS:
- Economic Pressures
- Government Policies, Laws, Regulations
- Stakeholders
- Cultures and Customs

ORGANIZATION FACTORS:
- Strategy
- Technology
- Human Capital
- HR Policy
- Employee Acceptance
- Cost Implications

INTERNAL STRUCTURE:
- Levels
- Differentials
- Criteria
Illustration of an Internal Labor Market

Hire → Consultant Engineer

Hire → Advisor Engineer

Lead Engineer

Hire → Systems Engineer

Senior Engineer

Hire → Engineer
Structures Vary

- An internal pay structure is defined by:
  - the number of *levels* of work
  - the pay *differentials* between the levels
  - the *criteria* used to determine those levels and differentials

- These are the factors that a manager may vary to design a structure that supports the work flow, is fair, and directs employee behaviors toward objectives
Strategic Choices Among Structure Options

- Tailored versus Loosely Coupled
- Egalitarian versus Hierarchical
Which Structure has the Greatest Impact on Performance? On Fairness?

<table>
<thead>
<tr>
<th>Structure A</th>
<th>Structure B</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Layered</strong></td>
<td><strong>De-layered</strong></td>
</tr>
<tr>
<td>Chief Engineer</td>
<td>Chief Engineer</td>
</tr>
<tr>
<td>Engineering Manager</td>
<td>Consulting Engineer</td>
</tr>
<tr>
<td>Consulting Engineer</td>
<td>Associate Engineer</td>
</tr>
<tr>
<td>Senior Lead Engineer</td>
<td></td>
</tr>
<tr>
<td>Lead Engineer</td>
<td></td>
</tr>
<tr>
<td>Senior Engineer</td>
<td></td>
</tr>
<tr>
<td>Engineer</td>
<td></td>
</tr>
<tr>
<td>Engineer Trainee</td>
<td></td>
</tr>
</tbody>
</table>
## Strategic Choice: Hierarchical vs Egalitarian

<table>
<thead>
<tr>
<th>Levels</th>
<th>Hierarchical</th>
<th>Egalitarian</th>
</tr>
</thead>
<tbody>
<tr>
<td>Differentials</td>
<td>Many</td>
<td>Fewer</td>
</tr>
<tr>
<td>Criteria</td>
<td>Large</td>
<td>Small</td>
</tr>
<tr>
<td>Supports:</td>
<td>Person or Job</td>
<td>Person or Job</td>
</tr>
<tr>
<td>Work Organization</td>
<td>Close Fit</td>
<td>Loose Fit</td>
</tr>
<tr>
<td>Fairness</td>
<td>Individual Performers</td>
<td>Teams</td>
</tr>
<tr>
<td>Behaviors</td>
<td>Performance</td>
<td>Equal Treatment</td>
</tr>
<tr>
<td></td>
<td>Opportunities for Promotion</td>
<td>Cooperation</td>
</tr>
</tbody>
</table>
Consequences of an Internally Aligned Structure

Pay structure

- Undertake training
- Increase experience
- Reduce turnover
- Facilitate career progression
- Facilitate performance
- Reduce pay-related grievances
- Reduce pay-related work stoppages
What The Research Tells Us

- Equity Theory
- Tournament Theory
- Institutional Model: Copy Others
Perceived Equity of a Pay Structure

**MY PAY**
- My qualifications
- My work performed
- My product value

**OTHERS’ PAY**
- Their qualifications
- Their work performed
- Their product value
Which Structure Fits Best?

- How the work is organized
- Fair to employees
- Directs behavior toward organization objectives
Summary

- **Internal alignment** refers to the pay relationships among jobs / skill / competencies within a single organization.
- The potential consequences of internal pay structures are vital to organizations and individuals.
- **Pay structures** – the array of pay rates for different jobs within an organization – are shaped by societal, economic, organizational, and other factors.
Employees judge a structure to be equitable by comparing each job’s pay with the qualifications required, the work performed, and the value of that work.

Acceptance by employees of the pay differentials among jobs is a key test of an equitable pay structure.

There is widespread experience and increasing research to support the belief that differences in internal pay structures, particularly employee career paths, influence people’s attitudes and work behaviors and therefore the success of organizations.
Review Questions

1. Why is internal alignment an important policy in a strategic perspective of compensation?

2. Discuss the factors that influence internal pay structures. Based upon your own experience, which ones do you think are most important? Why?

3. Look into any organization you are familiar with. Describe the flow of work. How is the job structure aligned with the organization’s business, the work flow, and the organization objectives? How do you believe it influences employee behaviors?
4. What is the *just wage* doctrine? Can you think of any present-day applications?

5. Under what organization designs are more egalitarian versus more hierarchical structures likely to be effective?