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Paying for performance in Britain: Does the type of job matter?

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Paying for performance in Britain: Does the type of job matter?

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Summary

Pay for performance (PFP) is now a common feature of the contemporary working landscape in Britain, with around two in five employees now receiving it. Very little representative evidence exists on the types of jobs in which it is most commonly applied. Using nationally representative datasets, we find: (1) an ‘occupational differentiation’ exists in PFP use: higher managerial and professional occupations have the highest rates of PFP – roughly twice that of less skilled occupations; (2) the ‘occupational differentiation’ exists across PFP types, whether based on individual, team or organisation performance; (3) the ‘occupational differentiation’ in PFP also occurs *within* workplaces. Our findings suggest PFP is more likely to be used in jobs where monitoring work effort is difficult and where specialist knowledge is important.

Introduction

Pay for performance (PFP) is now a common feature of the contemporary working landscape. Rising rapidly during the 1990s before levelling off in the early 2000s, about one-third of employees in Europe and more than two-fifths in the United States now have some element of their pay based on performance (Bryson et al 2013). Within the academic HRM literature on the determinants of HR practices including PFP, a primary focus has been on organisational factors. For instance, PFP is often viewed as a key element of ‘best practice’ to be applied uniformly throughout the organisation (Pfeffer 1998) as part of the configuration of ‘high-performance work practices’. Others have examined the competitive pressures in the product market or industrial sector as a key determinant in whether to implement certain HR practices or not (Schuler and Jackson 1987).

On other hand, the ‘HR differentiation’ or ‘workforce differentiation’ perspectives (Becker et al 2009) argue that organisations in fact often tailor their HR practices – including PFP – to specific groups of employees, such that they are not applied uniformly within organisations (Lepak and Snell 2002). Nonetheless, they do not make predictions about the basis on which differentiation occurs, or how it might vary by policy. While much research documents how the effect of PFP may vary according to different types of work (for better or worse), very little representative evidence exists on the types of jobs it is most commonly applied to. In this report, we examine the uneven diffusion of PFP across occupational groups in the British labour market. Doing so gives valuable insights into the main motivations behind managerial decisions on whether to implement it or pay a fixed wage – and the extent of concordance with academic theories on the design of employment contracts. Supporting employment contract theories, we find evidence that the *type of job* is a key differentiating factor in whether an employee receives PFP or not – specifically, it is most likely to be found where the monitoring of work effort is difficult and where specialist knowledge is important.

Why should pay for performance depend on the type of job?

In understanding why PFP should vary according to occupational groups, we draw upon sociological theories that classify types of jobs based on the type of employment relationships commonly found within them. These theories suggest three broad types of employment relationship exist (Goldthorpe 2007):

- 1 'Service relationships' are characterised by a longer-term time horizon, being salaried, clear career structures for advancement, more job security, and more autonomy over work processes.
- 2 'Labour contracts' are characterised by a shorter-term time horizon, by being hourly paid, have more limited career structures for advancement, less job security, and less control over work processes.
- 3 'Mixed forms' combine elements of both above, for example an office administrator may have considerable flexibility over when they start or finish work, but limited career structures, or a supervisor in a retail shop may be hourly paid but has opportunities for further progression within the organisation.

Table 1: The NS-SEC classification of occupations by employment relationship

Abbreviation	NS-SEC category	Monitoring difficulty	Specialist knowledge	Employment relationship	% labour force	Largest 3 SOC 2000 occupations (4-digit)
HMP	Higher managerial and administrative occupations Higher professional occupations	Difficult	High	Service	11	Marketing and sales managers; Production, works, and maintenance managers; Software professionals. Nurses; Medical radiographers; Secondary education teaching professionals; Primary and nursery education teaching professionals.
LMP	Lower managerial and professional occupations	Difficult	High	Service	29	Customer care occupations; Police officers (sergeant and below); Call centre agents/operators.
I	Intermediate occupations	Moderate	Moderate	Mixed	16	Sales and retail assistants (supervisor); Cleaners (supervisor); Heavy goods vehicle drivers (supervisor). Sales and retail assistants; Kitchen and catering assistants; Retail cashiers and check-out operators.
LST	Lower supervisory and technical occupations	Moderate	Moderate	Mixed	10	Cleaners; Heavy goods vehicle drivers; Other goods handling and storage occupations not elsewhere classified.
SR	Semi-routine occupations	Easy	Low	Labour contract	21	
SR	Routine occupations	Easy	Low	Labour contract	13	

Sources: Williams (2016); employees aged 20–65 in British Skills and Employment Survey 2012.

At the heart, choosing between these broad types of employment relationship is the *nature of job tasks*. More specifically, these theories argue that two characteristics explain these different employment

relationships: (1) the degree to which work is difficult to monitor, that is, how easy tasks are to define, their variety, and the length of time it takes to complete them; (2) 'human asset specificity', that is, the degree to which the satisfactory completion of work tasks depends upon specialist knowledge, skills and learning time, such that employees in high 'asset specificity' jobs are much more difficult to replace than jobs with very low requirements in this regard. Sociologists have found much empirical support for this classification of employment relationships and how they map onto specific occupations (job roles). This line of research culminated in the National Statistics Socio-Economic Classification (NS-SEC) of occupations (Rose and Pevalin 2003, 2005). Given the strong empirical support for this model (for example Williams 2016), we adopt it to examine variation in PFP rates. A summary of this classification of occupations is shown in Table 1.

These theories predict higher rates of PFP in higher and lower managerial and professional occupations, characterised by the 'service relationship'. This is because in these jobs, employers cannot easily monitor tasks closely on a day-to-day basis, given tasks are highly varied, diffuse and often difficult to define. Moreover, given employees in these sorts of jobs are difficult to replace, bonuses may act as a sort of 'gift exchange' encouraging extra effort and motivation in ways that benefit the organisation, but also the employee financially – a sort of 'efficiency wage'. Conversely, these theories predict lower rates of PFP in the other four occupational groups, being lowest in the semi-routine and routine occupations characterised by the 'labour contract'. This is because work effort in these jobs is much easier to monitor through direct supervision as tasks are less varied, are often repetitive, and narrowly defined. Since specialist knowledge is less important, commitment and retention are of lesser concern, so there is less economic need to offer PFP, as employees are more easily replaced.

Diffusion of PFP across job types

To examine the diffusion of PFP across occupational groups, we examine the British Skills and Employment Survey (BSES) from 2012, when the most recent survey was conducted. Examining the bottom row of Table 2 first, we find that roughly two in five employees received some form of PFP, with PFP based on individual performance (for example bonuses or merit pay) and organisational performance (for example profit-sharing or employee share ownership) being most common, with PFP based on workgroup (for example team or department) performance being least common. As we expect, PFP is most common amongst higher managerial and professional occupations, where more than half receive some kind of PFP. Next are lower managerial and professional occupations, also sharing a 'service relationship', where 44% receive PFP. PFP rates are generally lower in less skilled occupations, especially in occupations characterised by the 'labour contract', where work is easier to monitor and specialist knowledge is less important. We find the higher incidence in PFP use amongst managerial and professional occupations is apparent for all three types of PFP, and even with respect to receiving multiple PFP types (the final column).

While we argue that employers are making decisions on whether to implement PFP largely on the type of work, other factors may explain the apparent 'occupational differentiation' in PFP use in Table 2. More specifically, managerial and professional employees, for instance, are also likely to have higher levels of education and more work experience. Similarly, it could also be the case that managerial and professional employees are more likely to be employed in more competitive industries or larger workplaces – two further factors which may provide alternative explanations to the 'occupational differentiation'. To adjust (or 'control') for these 'other factors', we employ logistic multivariate regression. The results from this analysis controlling for other factors are in Table 3. The figures

represent ‘average partial effects’ relative to higher managerial and professional occupations. That is, the adjusted probability of an employee in each occupational category of receiving PFP relative to an ‘equivalent’ employee in a higher managerial and professional occupation (‘equivalent’ in terms of the other factors listed below the table). For instance, Table 3 shows that an employee in a routine occupation is about 27% less likely to receive PFP compared with an employee in a higher managerial and professional occupation, with similar levels of education and work experience, working in a similar-sized workplace, in the same industry, and so on. This lends support to our main argument that a primary consideration as to why PFP is implemented is the type of job.

Table 2: PFP by NS-SEC category (%)

NS-SEC category	Any PFP	Individual PFP	Team PFP	Organisational PFP	More than 1 PFP scheme
HMP	55	41	28	44	36
LMP	44	34	22	33	28
I	31	23	12	18	16
LST	39	24	15	26	20
SR	34	23	15	22	18
R	25	17	10	14	14
All employees	39	28	18	27	23

Source: Employees aged 20–65 in BSES 2012.

Note: Data are weighted.

Table 3: Multivariate analysis of occupational differentiation in PFP

	(1) Any PFP	(2) Individual PFP	(3) Team PFP	(4) Organisational PFP	(5) More than 1 PFP type
LMP	–0.032 (–0.77)	0.011 (0.28)	0.004 (0.11)	–0.030 (–0.78)	0.000 (0.00)
I	–0.135* (–2.56)	–0.074 (–1.45)	–0.100* (–2.32)	–0.157*** (–3.31)	–0.099* (–2.17)
LST	– 0.174*** (–3.31)	–0.134** (–2.74)	–0.107* (–2.54)	–0.167*** (–3.65)	–0.139** (–3.19)
SR	–0.156** (–3.15)	–0.104* (–2.18)	–0.067 (–1.56)	–0.155*** (–3.37)	–0.102* (–2.30)
R	– 0.266*** (–5.10)	–0.163** (–3.26)	– 0.145*** (–3.45)	–0.260*** (–5.87)	–0.179*** (–4.05)
Individual Workplace	Yes	Yes	Yes	Yes	Yes
N	2240	2240	2240	2240	2240
Pseudo-R ²	0.189	0.153	0.156	0.216	0.207

Source: Employees aged 20–65 in BSES 2012.

Notes: Data are weighted. Average partial effects reported based on logistic regression with HMP as the reference category. Individual controls: female, ethnic minority, married, any children under 16, degree-level qualification, work experience (five categories), part-time, temporary. Workplace controls: workplace size (four categories), public sector, unionised, and industry (four categories).

Statistical significance: * p < 0.05, ** p < 0.01, *** p < 0.001 (z-statistics in parentheses).

Diffusion of PFP within workplaces by job types

Finally, to be even surer employers really are choosing to implement PFP depending on the type of job, we examine a separate nationally representative dataset, the Workplace Employee Relations Survey from 2011, its latest wave. An advantage of this dataset is that it sampled around 2,000 workplaces and up to 25 employees within each one. These types of surveys are called employer–employee matched surveys since they sample multiple respondents from the same workplace, whereas household surveys such as the BSES are samples of individuals in the labour market as a whole. The sampling structure of WERS (employees nested within workplaces) means we can examine whether occupational differentiations are apparent even *within* workplaces. Table 4 replicates the analysis in Table 3 but on the WERS sample of employees. Controlling for working in a particular workplace, we find that an occupational differentiation is still apparent. This further implies employers differentiate whether to implement PFP or not to a particular employee depending on the type of job.

Table 4: Occupational differentiation in PFP within workplaces

	(1) Any PFP	(2) Individual PFP	(3) Team PFP	(4) Organisational PFP	(5) More than 1 PFP
LMP	– 0.093** (–3.02)	–0.035 (–1.45)	–0.061* (–2.48)	–0.050 (–1.94)	–0.044 (–1.62)
I	– 0.205** (–2.99)	–0.0409 (–0.90)	– 0.128*** (–3.98)	–0.147*** (–3.59)	–0.123* (–2.14)
LST	– 0.122*** (–6.82)	–0.112*** (–4.88)	– 0.120*** (–5.83)	–0.160*** (–4.57)	–0.163*** (–4.87)
SR	– 0.254*** (–4.93)	–0.088** (–2.75)	– 0.127*** (–3.68)	–0.183*** (–4.61)	–0.196*** (–3.88)
R	– 0.284*** (–5.63)	–0.079* (–2.28)	– 0.200*** (–6.06)	–0.228*** (–4.88)	–0.195*** (–4.19)
Individual Workplace FEs	Yes Yes	Yes Yes	Yes Yes	Yes Yes	Yes Yes
N employees	10570	8728	5091	5272	4116
N workplaces	957	766	436	453	344
Pseudo-R ²	0.0377	0.0257	0.0338	0.0409	0.0499

Source: Employees aged 20–65 in WERS 2011.

Notes: Data are weighted. Average partial effects reported based on logistic regression with HMP as the reference category. Individual controls: female, ethnic minority, married, any children under 16, degree-level qualification, age (five categories), part-time, temporary.

Statistical significance: * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$ (z-statistics in parentheses).

Conclusions and implications

Returning to the theories mentioned in the introduction, on whether PFP can be thought of as a ‘best practice’ to be applied uniformly through the organisation, or to specific groups – the ‘HR differentiation’ perspective – we find that British employers seem to be following the latter. Presenting new evidence from two separate nationally representative surveys, we find a clear gradient in PFP use according to the broad occupational group. More specifically, employers are more likely to implement PFP in jobs where work tasks are difficult to monitor and where specialist knowledge is important. Reinforcing this view, the gradient is also more or less apparent across PFP types, be they based on individual, team, organisational or multiple indicators of performance. Moreover, the same gradient can be found even *within* workplaces.

While our research makes use of a very broad classification of jobs (only six categories), limiting its direct relevance to any specific organisation, we hope it illustrates a broader point that the decision to implement PFP depends on the type of job. We argued that the differentiation in PFP use is based upon the extent to which work can be monitored and the degree to which specialist knowledge is required. From a practice perspective, this implies, first, that PFP is used where job tasks are difficult to define, have a great deal of variety, and the length of time it takes to complete them is long. Second, these jobs are also likely to be jobs where an employee’s value to the organisation rises with tenure and where commitment on both sides of the employment relationship is very important, so PFP can act as a way of retaining valuable talent, not just ensuring continual commitment. More generally, we recommend to follow the recommendations made by Baron and Kreps (1999), who suggest that employers design appropriate payment systems across occupational groups within organisations. For instance, they advocate performing formal job analysis to determine theoretically important factors – such as job complexity, knowledge requirements, number of employees supervised, and the types of tasks – before taking decisions on whether to implement PFP.

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