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July 1999

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Back to the Future: A Century of Compensation

Abstract

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Four lessons for the future are drawn. These include: End the search for the one "right" compensation strategy; Understand what in the context matters; Continue pragmatic experimentation, and Support continuous learning about compensation. Readers are invited to delve into the history of compensation to discover what they take away for the future.

Keywords

compensation, practice, pay, benefit, employee, profit, incentives, stock, pension

Comments

Suggested Citation

Milkovich, G. T. & Stevens, J. (1999). *Back to the future: A century of compensation* (CAHRS Working Paper #99-08). Ithaca, NY: Cornell University, School of Industrial and Labor Relations, Center for Advanced Human Resource Studies.

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WORKING PAPER SERIES

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Working Paper 99 - 08



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Working Paper 99-08

<http://www.ilr.cornell.edu/cahrs>

This paper has not undergone formal review or approval of the faculty of the ILR School. It is intended to make results of Center research available to others interested in preliminary form to encourage discussion and suggestions.

ABSTRACT

What were the hot compensation issues and practices over the past century? Does history offer any lessons that may inform our compensation decisions in the future? To answer these questions, we reviewed newspapers and business publications from the past 100 years. To highlight changes in compensation systems during that time, we selected four topics to examine in detail in this paper: compensation's role in the changing nature of the deal; the evolution of pay-for-performance; the emergence of benefits; and the bellwethers of compensation systems.

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BACK TO THE FUTURE: A CENTURY OF COMPENSATION

What were the hot compensation issues in 1900, and how have they changed since then? Does history offer any lessons that we can use as we go forward? With the approaching millennium, we decided to review changing compensation systems over the past 100 years. We reviewed the past 100 years of news articles published by the New York Times and by magazines listed in the Periodical Index. Some interesting titles surfaced during our review, including these.

- “Entrenched Greed Underlies Executive Compensation”
- “Profit Share and Stock Ownership Unite Employee and Company Interests”
- “Industry Widening Use of Incentives”
- “GM Bonus Plans Spark Teamwork”
- “Stock Options Have Outlived Their Purpose”

Fortune magazine used the “Entrenched Greed” headline in a 1939 report on President Roosevelt’s call for caps on executive salaries and public reporting of the compensation of the top people in publicly held companies, attesting to the long history of skepticism over executive compensation. The second headline lauding profit sharing and employee stock ownership referred to Procter and Gamble in the late 1890s. Colonel Procter believed that profit sharing, pensions, a week’s vacation with pay after two years of experience, and employment security increased “efficiency and loyalty.” Why weren’t more “... industrial captains imbued with the spirit of William Cooper Procter?” the article’s author wonders.

While the “New Pay” of the 1990s features teamwork and success sharing. General Motors was there 40 years ago. The New York Times reported that GM’s bonus plan encouraged greater teamwork and that performance-based incentives were becoming increasingly widespread in companies. And possibly prefiguring a trend beyond 2000, the 1975 bear market caused a consultant to advise clients that “stock options have outlived their purpose.”

We also looked at the contents of compensation books published over the past 100 years. The similarities, shown in Table 1, are striking. So are the differences. Alternate approaches to establishing base pay, designing and administering incentives and rewards, and setting objectives are common topics throughout the century. Some topics drop out --- “The Sweat System”, and “Industrial Cooperation Rejects Profit Sharing” (Schloss, 1892); “Day Work and Week Work”, and “Mutual Benefit Associations” (Bloomfield, 1923). Some are added: Pay for special groups (sales, office workers, executives) appears in the 1920s (Bloomfield, 1923); Belcher’s first edition (1955) discusses job evaluation, market surveys, fringe benefits, and cost

controls. Milkovich and Newman (1999) add strategic approaches, total compensation, flexible benefits, international issues, and government regulations.

To get a sense of the changes over the past 100 years and look for lessons to inform our decisions as we look ahead, we focus on four topics: (1) the changing "deal", (2) pay for performance, (3) benefits and services, and (4) bellwethers. Admittedly, this becomes something of a Rorschach test: What we "see" may not be what others "see." Consequently, we hope our effort will make others curious enough to take a look at the history for themselves.

TABLE 1
The Changing Deal 100 Years

| | Early 1900 - 1925 | 1925-50 | 1950-75 | 1990s |
|-----------------------------|--|--|--|---|
| Compensation Policies | Individual contracts | Internal labor markets | Internal equity | Strategic Performance Market based |
| Performance | Piece rates Contract rates | Profit sharing | Merit Increases COLAs | Performance-Based |
| Competitiveness | Market based | Internal equity/ Market adjustments | Internal equity/ Market adjustments | Market based/ Flexible structures |
| Total compensation Focus | Cash Incentives Welfare services | Cash based Benefits Government regulations | Equity Flexible benefits | Total Returns Cash, Variable Choice |
| Security | Contracting | Stability and Commitment | Predictability Commitment | Employability/ Agility |

THE CHANGING DEAL

The new employment relationship that emerged in the 1980s and 1990s, the "New Deal", is characterized by changes. From long-term security with a single employer to "employability" among several; from permanent employees to core and contractors; from merit or seniority-based pay to performance-based pay; from one-size-fits all benefits to flexible packages that permit choice. This new deal was spawned by the new economy, with global competitive pressures that reward flexibility, strategic alliances, mergers, restructuring, technologically led productivity improvements, and the demand for people willing to learn and adapt. But is it really that new? Table 2 depicts employment relationships at each quarter century. Today's deal shares elements with life in the first part of this century.

TABLE 2:

Table of Contents for Compensation Text Books: 1900-1999 (page 1 of 2)

| <p><u>Methods of Industrial Remuneration</u> By David Schloss</p> | <p><u>Financial Incentives for Employees and Executives</u> by Daniel Bloomfield 1923 (US)</p> | <p>Compensation Administration by David W. Belcher 1955/1974</p> |
|---|---|--|
| <ol style="list-style-type: none"> 1. Different Kinds of Wages 2. Time-Wage 3. Task-Wage 4. Piece-Wage 5. Objections Entertained to Piece-Work 6. Progressive Wages 7. Collective Task-Wage 8. Collective Piece-Wage 9. Contract Work 10. Cooperative Work 11. Piece-Wage Foremanship 12. Sub-Contract 13. Objections Entertained to Sub-Contract: "The Sweating System" 14. The Interference of Public Authorities In Regard to Sub-Contract 15. Cooperation & Trade Unionism 16. The Two Kinds of Cooperation 17. What is Meant by Profit-Sharing 18. Product Sharing 19. The Theory of Profit-Sharing 20. Profit-Sharing in Practice 21. Critical Examination of Profit-Sharing 22. The Theory of Industrial Cooperation 23. The Practice of Industrial Cooperation 24. Industrial Cooperation Rejects Profit-Sharing 25. Critical Examination of Theory of Industrial Cooperation 26. The True Import of the Cooperative Movement 27. Practical Cooperation 28. Yale and Towne Gainsharing System 29. Morgan Crucible Co Benefit Scheme 30. Institutions of Benefit of Employees 31. List of British Profit-Sharing firm Profit-sharing scheme in force with Mr. Bushill | <ul style="list-style-type: none"> • General Consideration • Types of Wage Systems • Piece Work • Day Work and Week Work • Principles of Bonus Plans • Bonuses for Increased Production • Bonuses for Improved Quality • Bonuses for Economy • Bonuses for Steady Attendance • Bonuses for Length of Service • Thrift Plans • Profit Sharing • Stock Participation Plans • Mutual Benefit Associations • Pension Plans • Incentives in Retail Stores • Compensation of Salesmen • Compensation of Office Workers • Incentives for Foremen and Executives | <ul style="list-style-type: none"> • The Employment Exchange Model • Compensation Theory- Economic • Behavioral Science Compensation Theory and Research • Job-Related Contributions • Collection of Job Information and Determining Compensable Factors • Job Evaluation- Non-Quantitative Methods • Job Evaluation- Quantitative Methods • Performance Contributions • Personal Contributions • Economic Job Rewards- Wage Level • Economic Job Rewards- Wage Structure • Economic Performance Rewards- Rate Rates • Economic Performance Rewards- Incentive Plans • Economic Membership Rewards • Non-Financial Rewards • Comparison Standards • Compensation Policy • Wage and Salary Surveys • Wage Criteria • Sales Compensation • Compensation of Managers and Professionals • Control and Integration of the Compensation System |

Compensation

By Milkovich and Newman

1999

1. The Pay Model
2. Strategic Perspectives
3. Defining Internal Consistency
4. Job Analysis (Jobs vs. People, Collecting Information, Job Descriptions)
5. Evaluating Work: Job Evaluation (Job-Based Structures, Methods: Ranking, Classification, Point-Factor)
6. Person-Based Structures (Skills, Competencies)
7. Defining External Competitiveness (Competitive Pay Policy, Consequences)
8. Designing Pay Levels and Structures (Surveys, Relevant Markets, Design Ranges and Bands)
9. Pay for Performance: The Evidence
10. Pay for Performance Plans (Individual and Group and Long-Term Incentive Plans)
11. Performance Appraisals
12. The Benefits Determination Process
13. Benefits Options (Legally Required Benefits, Retirement and Savings Plans, Life Insurance, Medical)
14. Compensation of Special Groups
15. Union Role in Wage and Salary Administration
16. International Pay Systems
17. Government's Role in Compensation
18. Budgets and Administration

1900-1925: Incentives, Contracts, Few Safety Nets, Foreman-In-Charge

The economy in the early 1900s was remarkably volatile. Wild swings in the business cycle, a flood of immigrants, declining real wages and high turnover (300 percent in certain lower-skilled jobs) marked these when employment-at-will meant exactly that. And it was the will of proprietors that mattered. Owner-operated enterprises employed a larger share of the workforce than today. Supervisors were accountable for hiring, firing, and setting wages, as well as productivity and labor costs. Unfortunately, they too often exercised favoritism in fulfilling these responsibilities; taking bribes from those hoping to secure work or receive a promotion was not unusual. Not only was finding and holding a job uncertain, but the amount of take-home pay was also uncertain since it was frequently based on a piece rate. In some cases, even the base wage was not guaranteed. There was a true downside risk for employees. Incentives based on Taylor's "scientific management" were seen as "best practices". Over 60 percent of manufacturers responding to a 1920 National Industrial Conference Board survey reported using piece rates. Eighty percent of all workers were employed in plants where piece rates were used. Little was offered outside of cash compensation. Only a handful of companies

offered pensions, profit sharing, and guaranteed wages to skilled workers. There was little government regulation, and consequently few safety nets such as medical insurance, unemployment compensation, overtime pay, social security, and the like. Employees' economic security in a very real sense was closely aligned with the uncertainties of the marketplace and corporate performance. In the HR jargon of the 1990s, employees in the early 1900s owned their careers, managed the risks of performance based pay, and faced supervisors who acted as owners.

1925-1950: Regulated Bureaucracies

Jolts caused by external forces, much like earthquakes, disclose flaws in structures and trigger changes. Economic depressions and two world wars contributed to significant changes in compensation systems and the employment deals in the second quarter-century. This tumultuous period also witnessed labor unrest, violent union organizing campaigns, and long strikes. Unemployment reached over 30 percent in 1939; company payrolls dropped by 60-80 percent. People who struggled to live on one day's wage per month considered themselves fortunate to have work. In response to the very real prospect of social upheaval, the government intervened with a range of social legislation and public works programs. Unions gained strength and became more intensively engaged in compensation decision making. As part of Roosevelt's New Deal, laws passed to regulate compensation include the Social Security Act (1935), Securities and Exchange (1934), Wagner Act (1935), and the Fair Labor Standards Act (1938). The War Stabilization Board of World War II and its reincarnation during the Korean War in the 1950's had a profound effect on compensation practices. Its controlled wage increases, encouraged the adoption of fringe benefits, expanded the use of job evaluation to rationalize pay and promotion decisions. Formalized procedures, government regulations, and negotiation with labor unions supplanted the supervisor's control over compensation decisions. By the late 1940s, compensation had moved from the individual contract, incentive market - oriented system of the early 1900s to a system embedded in regulated bureaucracies. They were characterized as "internal labor markets" in which "webs of rules and procedures," collectively bargained terms and conditions, and government laws and agencies regulated employment compensation. Medical care, pensions, vacations, and greater job security all became an integral part of total compensation and rewards. The use of performance based incentives also declined during this period, although they never totally went away. The internal labor market meant, at least for employees in large firms, that they would have jobs for life as long as their performance was satisfactory. In contrast to the more uncertain first part of the century, pay increases became more predictable, since they were highly correlated with the

consumer price index and negotiated through pattern bargaining between large trade unions and large corporations. Pay increases for managerial and other non-unionized employees were often based on union settlements.

1950s-1975: Predictability, Internal Equity, Continuing Regulation

The Korean and Vietnam Wars, business cycles, and social legislation were major influences on compensation systems during 1950-1975. Wage and price controls (or “guidelines”) regulated compensation decision making; the 1963 Equal Pay Amendment to the Fair Labor Standards Act and Title 7 of the Civil Rights Act of 1964 focused attention on equal pay for equal work and internal equity. Compensation decisions became increasingly systematic and predictable. Merit increase grids, seniority-based increases, COLA clauses, career progressions and ladders, and internal equity all supported increasingly detailed job analysis and job evaluation. The use of individual incentive plans declined, and benefits increased from 12 percent of total compensation in 1950 to 28 percent in 1975. A 19xx *Harvard Business Review* article projected that benefits would top 50 percent by 1984. The future seemed safely predictable.

1975 ->: Everything Old?

The beginning and end of the century have much in common: Individualized variable pay based on performance, intense competition for highly mobile skilled workers, and a greater emphasis on the external market. Yet, these similarities are only a veneer. Competition in the 1990's is global as well as regional. Compensation decisions and the returns from the employment relationship are more regulated. Employment laws, tax laws, social welfare laws, interest rates, international exchange rates all now play a role in compensation management. Compensation remains a critical part of the employment relationship, but if the rhetoric we found in our review is representative of reality, then compensation decision making is much more strategic now than at the beginning of the century. Rather than a foreman managing a confusing and conflicting array of pay rates, today's compensation decisions are intended to be aligned with the business strategy and signal valued employee behaviors. However, strategic compensation may enjoy more articles than adopters.

Admittedly, there are dangers in characterizing any period with a single label. So while it may be convenient to label eras of compensation, as we have, such labels also mislead. During the first part of the century, a reasonable handful of companies such as Procter and Gamble, National Cash Register, and Ford did not follow the foreman-in-charge, piece rate approach. Rather, they adopted compensation systems that bear many similarities to practice today. So while at some level of abstraction, the compensation systems of an era can be generalized

under one label, a closer look reveals important differences in pay systems tailored to the specific context and time.

PAY FOR PERFORMANCE

The second issue that caught our attention during our review of the past 100 years was performance-based pay. While paying people based on performance has been a salient topic in books, newspapers and magazines throughout this century, specifics varied. Individual piece rates used early in the century were replaced by mid-century with team- or company-wide plans and merit pay. Now, at the end of the century, performance-based pay plans are diverse and complex, and depend on the strategic circumstances of each organization. It would have been very uncommon for a person in 1900 or even 1950 to have a total compensation package that included awards based on individual contribution, profit sharing bonuses, stock options, plus choices among various benefits and services. Such a package is increasingly common today. In the 1990s the Conference Board, Towers Perrin and others reported that about 35 percent of member companies used individual incentives (i.e., performance bonuses rather than piece rates), 15 percent used gainsharing, 35 percent corporate performance bonuses, and 25 percent spot awards. The need for continuous productivity improvement, remaining competitive, improving customer satisfaction, and controlling labor costs were the reasons given for the use of performance-based pay.

Unfortunately, it is difficult to locate historical data that was collected systematically enough to permit comparisons of the different types of plans and the proportion of employees covered in different periods. Consequently, it is difficult to undertake a detailed analysis of changes over time. Case histories of individual firms such as Lincoln Electric, Ford, and others do offer some insights (Jacoby, 1993). While surveys of company practices have been available since the 1920s, historical performance measures have not been collected, making it difficult to understand any effects these plans might have had on corporate performance or employee behaviors. Absent evidence, the articles offer personal accounts, experience and belief attesting to the effectiveness of these systems. Beliefs (and doubts) about the effectiveness of various pay-for-performance methods are as strongly held today as they were 100 years ago.

By the early 1900s, scientific management had transformed incentive plans. The standards and rates under earlier plans were haphazard and prone to manipulation by both supervisors and employees. Taylor engineered differential piece rates by designing the work into discrete tasks and determining minimum times to complete them. In making his case for

piece rates, Taylor argued that profit sharing and group performance programs were “too remote from the workers.” Line-of-sight terminology came later, but the concept is not new.

Group based gainsharing plans gained ground during the 1930s and 1940s. Their most famous advocate, Joseph Scanlon, developed his plan while working for the Steelworkers. Five steelworkers and three management representatives worked out the details of the original plan, which continues to emphasize joint labor-management cooperation to solve production problems and improve productivity. Successful installations occurred in 1945 at the Adamson Company and in 1947 at the LaPointe Machine Tool Company. These plans spread to other manufacturers, replacing the individualized piece rate, which was increasingly described in the press as an unfair speedup. By 1950, *Fortune* magazine described the Scanlon plan as “Enterprise for Everyman.” In that same year, Ford Motor distributed its manual on how to start and administer a Scanlon plan to other companies, and President Truman encouraged companies to use them. In 1953, 50 percent of U.S. workers were paid by some type of group-based incentive plan.

During the 1960s and 1970s, the use of all forms of pay for performance plans declined. U.S. Bureau of Labor Statistics surveys in 1968-1970 period show that only about 20 percent of manufacturing workers were paid under incentive plans (compared to 50 percent in 1953); other industries show much smaller percentages. Belcher's textbook reports that incentive plans were being replaced by standard hour plans with seniority and cost of living based increases. Similarly, managers' and professionals' pay was based on merit rates, experience, and increase budgets. Usually, only a small handful of executives enjoyed a significant portion of their compensation linked to productivity improvement and business performance. While there is no systematic study of the factors contributing to the rise and decline of pay-for-performance, it may be that the economic uncertainties inherent in variable pay, combined with volatile business cycles, inflation, and the mismanagement of performance measures contributed to its decline. The insight allegedly offered by a union negotiator of that period, “You tell me the amount of pay increase we get, and I will tell you if I like the plan!” captured the point.

Cautions about the use of incentives echo down the century. Belcher's 1955 textbook reports that employees believe that incentives cause speedups, use questionable performance measures, result in rate cutting, cause you to work yourself out of a job, shift risks to employees, and foster a lack of trust and cooperation. Back in 1898, Schloss's textbook discussed objections to Incentives and the “Sweating System.” Kohn revisited such concerns in his 1993 book “Punished by Rewards”. Responses to such criticisms continue to take the form of lists of principles that, if properly followed, insure the effectiveness of pay-for-performance systems. It

is disquieting to compare the “basic principles for effective pay for performance plans” written in 1923 and with those proffered 75 years later. As Table 3 shows, the words may differ, but not the meaning.

By the 1980s and 1990s, contemporary high performance work systems included a variety of approaches that attempt to foster a high performance - high commitment organization culture. The notion of embedding performance-based pay as part of cultural values is not unique. Scientific management in the early 1900s treated piece rates as part of the organization culture, the Scanlon gainsharing plan was part of a labor-management partnership, and employee stock ownership programs are part of a culture of ownership. Yet today the notion persists that gainsharing, profit sharing, stock options, teams and cooperation are somehow “nontraditional” approaches.

Table 3

Basic Principles of Incentive Plans (From Financial Incentives for Employee and Executives, by Daniel Bloomfield, 1923)

1. An incentive plan should have as its fundamental purpose the increasing of the value of employees' services both to themselves and their employer
 2. Such a plan should serve to promote confidence and understanding between the employer and employees.
 3. To that end, the benefits to employees should be substantial and in addition to the current rate of wages.
 4. The plan should not represent paternalism or philanthropy on the employer's part.
 5. The participants in the plan should be informed as to the factors affecting the payment and amount of the incentive
 6. They should, preferably, be represented in the administration of the plan.
 7. The plan should be designed to meet the needs of each enterprise and accomplish the worthy objects of the employer.
 8. The success of any plan is particularly dependent upon the effectiveness of its management. Any plan not matter how admirable may be its features, will fail unless it is properly managed.
-

EMPLOYEE BENEFITS

Most of the benefits with which we are familiar today -- paid vacations and holidays, health and hospitalization insurance, retirement savings plans ---were initially introduced by a small number of companies around the turn of the century. Procter & Gamble introduced an early profit-sharing plan during a period of labor unrest. "Welfare benefits" whose aim was to improve health and working life of employees were financed unilaterally by a small number of

individual companies. Washrooms, lunchrooms, company nurses, dentists, doctors, financial assistance for home purchases, subsidized housing, language and citizenship courses will be familiar to today's readers with international responsibilities in developing nations. Pensions, guaranteed income plans, life insurance and savings plans were all introduced in varying degrees in the early 1900's. 1929 statistics show that only 5% of large firms provided profit-sharing, 15% had health and accident insurance and 2% had a group pension plan. Most of these programs required continuous employment for a period of time (5 to 10 years) prior to participation. Although advertised as a means to reduce turnover, the stringent eligibility rules excluded young and unskilled employees with the highest turnover rates. Nevertheless, some company leaders believed that these "welfare" programs would reduce labor disturbances.

During the Great Depression, many of the existing programs were discontinued or became insolvent. At the same time, economic and social legislation passed to offset the dislocations caused by the Depression caused other companies to start or reinstate welfare benefits. A major cause of a resurgent interest in benefits was the dramatic increase in union activity and membership. By 1940, one in three U. S. manufacturing employees belonged to a union. Unions agitated for guaranteed wage plans and the use of seniority in determining wages, promotion and layoffs. Unions also played a role in convincing the War Labor Board to permit increases in "indirect" compensation, which it termed "fringe" benefits, at the same time that wages were frozen. Fringe benefits were said to "increase worker morale and loyalty and mitigate the effects of the wage freeze". The number of firms providing these benefits doubled from 1940 to 1946. The final factor that solidified benefits' role in total compensation was a 1949 Supreme Court decision compelling employers to collectively bargain benefits.

So benefits that started the century as a unique compensation strategy offered by a select group of "welfare" capitalists to help insure a stable work force, through the pressure of economic instability, social unrest and war, became "fringe" compensation. Sometime in the mid 1980s, faced with escalating costs (15 to 20 percent annually), the term "fringe" was dropped. Benefits are now considered part of a total compensation package. However, most organizations continue to manage them separately from other forms of compensation.

TRW introduced the first flexible benefits program in 1974. Their program included 3 medical plans, 8 life insurance plans, dependent life insurance and supplemental accidental death/dismemberment benefits. TRW's rationale for implementing the program in spite of unfavorable tax legislation was that flexible benefits were beneficial for employee relations and eliminated the prevailing pattern bargaining approach. The Revenue Act of 1978 permitted choice between taxable and non-taxable forms of compensation for the first time. Following this

and other tax law changes, the adoption of flexible benefit plans increased, with the greatest increases occurring between 1983 and 1984, when the number of plans went up by 127 percent. The variety of plans increased as well, from simply salary reduction plans to more complex, highly flexible varieties.

“BELLWETHERS” VS. “WITH THE FLOCK”

The final theme of our review is on the constancy of change, and differential approaches to change. Table 4, Going Back to the Future, is a chronology of selected compensation events covering the last 100 years. Like the bellwether sheep whose movement is followed by the flock, some companies seem to anticipate or even create change, take risks, and move. Others quickly follow. Compensation bellwethers are noted in Table 2. Colonel Procter was a bellwether when he included profit sharing, guaranteed work, pensions, disability and medical care, and paid vacations in P&G's compensation system. By 1920 over 40 leading firms had adopted similar systems. Henry Ford was a 1913 bellwether who boosted daily pay for production workers from \$2.34 to \$5.00 and cut the workday from nine to eight hours. Bill Gates led the way with an emphasis on stock options for all Microsoft employees whose value today significantly exceeds the value of base, bonus, and benefits combined.

TABLE 4
Timeline of Selected Compensation Events

- **1889- Gainsharing introduced:** The term gainsharing first appears in an article by Towne, who measured the work unit's costs and productivity and then shared future gains. Gilman's book on Profit Sharing published.
- **1891- Bureau of Labor Statistics surveys:** One of the first significant BLS surveys, resulting from a Senate request to investigate the effects of tariff legislation on wages and prices. The BLS developed wage rate history back to 1860 and a more limited history to 1840.
- **1892- First textbook in Compensation:** Schloss's Methods of Industrial remuneration published- One of first textbooks on compensation. Discusses incentive pay for individuals and groups and profit sharing.
- **1895- Taylor's Incentive System introduced:** Frederick Taylor presents his paper on differential piece rate incentives. Based on engineering principles, his program advocates setting precise standards for establishing the rate of work and clearly linking the amount of rewards to levels of performance.
- **1898- Welfare capitalists introduce profit sharing and employee services.** Procter and Gamble lead 40 other companies to offer profit-sharing plans and other welfare programs.

- **1902- NCR creates Labor Department:** NCR established its Labor Department, which was responsible for employment, payroll, and welfare programs.
- **1904 - Stock bonus:** Dupont establishes stock bonus plans to recognize high performing managers. Up to \$10,000 per year is awarded.
- **1911- Group Life Insurance:** First group life insurance plan for employees offered by the Pantasote Leather Company.
- **1914- Expanding welfare programs:** The National Civic Federation listed over 2,500 companies as being engaged in some form of welfare work.
- **1916- Deferred Profit-sharing:** Harris Trust & Savings Bank offers the first deferred profit-sharing plan
- **1916- First National Conference of Personnel Managers**
- **1916-1920 WWI-** Labor shortages, declining productivity and social unrest. Personnel departments in companies to handle these labor problems. Personnel departments reduced the power of the foremen-in-charge.
 - Increased wage standardization. Advent of job evaluation and wage structures.
 - The War Labor Board enforced two principles 1) Workers should be able to join unions without interference and 2) There should be industry-wide standards for wages and working conditions (8-hr day, paid overtime, living wage)
- **1920's: Pay for Skill Appears-** H.H. Franklin Company rewarded employees by paying them an additional 4% for every new process they learned.
- **1920's- Stock ownership increases:** As the value of stocks increase, employee stock ownership also increases. By 1928, 1 million employees own \$1 billion worth of their company's stock.
- **1929- First Million-Dollar CEO:** E. Grace of Bethlehem Steel becomes first CEO to earn a million dollars. He earned \$12,000 in salary and a \$1.6 million bonus.
- **1929- Blue Cross:** Prepaid medical costs initiated at Baylor University Hospital
- **1929-1935- Depression:** Unemployment rate hits x%. Payrolls reduced by 60-80%.
- **1931- Davis Bacon Act:** Requires public construction project contractors pay "prevailing wage"
- **1932 - Managers as Agents:** Berle and Means argue that managers' compensation package should encourage managers to act like owners.
- **1933- National Industrial Recovery Act:** The right to collectively bargain, standardized work hours and minimum wage.
- **1935: Wagner Act:** Requires employers to bargain over wages, hours, and conditions of work if a majority of employees desire union representation.

- **1935- Social Security Act:** Shift to more substantial welfare state
- **1938- First Hay Point Plan:** At the Pennsylvania Company, a commercial bank with 1,100 employees
- **1942- Wage Stabilization Act:** During WWII, pay levels are frozen to control inflation and boost production of war materials. Increased use of job evaluation to promote internal equity.
- **1943- The term “fringe benefits” used:** The War Labor Board coins the term "fringe benefits" to refer to indirect benefits such as medical insurance, pensions and profit-sharing. These are permitted during the wage freeze. As a result, these benefits increase dramatically to mitigate the effects of the wage freeze
- **1945- Scanlon Plan:** First reported installation of Scanlon gain-sharing plan at Adamson Co. of a plan developed by J. Scanlon in 1938.
- **1945- Union membership:** Peaks in the U.S. at 35.5%
- **1949- Benefits must be bargained:** Supreme Court upholds lower court decision in Inland Steel vs. USWA, stating that employers must bargain employee benefits
- **1950- Stock options:** Use of options receives favorable tax treatment
- **1950- Executive Surveys:** Arch Patton and American Management Association begin conducting executive compensation surveys
- **1952- Employee-wide Stock Options:** Pfizer introduces broad-based stock-option program
- **1955- American Compensation Association founded.** Its membership in 1999 is 25,000
- **1958- Expatriate Pay:** AMA conducts study on compensation practices of managers and executives on international assignments
- **Early 1960s- Wage Guidelines:** Council of Economic Advisors tie wage and benefit increases to productivity increases.
- **1963- Equal Pay Act:** Requires equal pay for equal work regardless of gender
- **1964- Title VII Civil Rights Act:** Prohibits employment discrimination on the basis of race, gender, national origin, religion
- **1969- Stock options lose favor:** Options fall out of favor for the next decade due to tax changes, inflation and a bear market
- **1973- HMO Act:** Spurs growth of Health Maintenance Organizations

- **1974- Flexible benefits:** After 4 ½ years of research, TRW implements the country's first flexible or cafeteria-style benefits program, offering 3 health insurance programs, 8 life insurance options and accidental death and dismemberment insurance.
 - **1974- ERISA passed:** Regulates private pensions and imposes financial and accounting controls. Does not require companies to offer pensions, but if offered, they must comply with ERISA.
 - **1978- Tax law favors flexible benefits:** Revenue Act of 1978 permits choice between taxable and non-taxable forms of compensation which lessens tax burden for companies offering flexible benefits. Creates the 401K defined contribution retirement savings plan.
 - **1980's- High Performance/High Commitment Work Practices:** Greater focus on performance and results, group incentives, team-based pay.
 - **1980's- Comparable worth:** Legislation proposed creating standard for gender-based pay comparisons based on internal measures of worth, ignoring market effects. Not passed.
 - **1980's- Delayering and Broadbanding:** As part of its "Work-Out", General Electric reduces organization levels and institutes career broad bands and pay zones.
 - **1980's- Broad based options become significant portion of total compensation:** Microsoft and other software firms radically change the mix of compensation for all employees to emphasize stock options compared to base and bonus.
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Other compensation bellwethers listed in Table 2. A gainsharing plan based on performance of teams rather than individual piece rate is offered by Townes in 1889. Pay for skills was introduced at H. H. Franklin in the 1920's. Pfizer introduced broad-based options in 1952. By 1984, General Electric was de-layering and creating broad career bands and pay zones.

What explains why some organizations are bellwethers, others are followers, and still others are not? The brief historical picture we present suggests that external factors create pressures for change: shortage/surpluses of critical talent, social unrest, concerns for justice and fairness, technological innovations, global competitive pressure, changing tax and employment laws. But why do some organizations move first? Why did Col. Procter, Henry Ford, TRW, Bill Gates and others create significant changes in compensation systems? We leave this question up to the reader. Identifying the catalysts of change and the characteristics of those who move first is not easy. It is clear that being a bellwether is not without risk. Competitive advantage in human resource strategies can be achieved via other non-compensation initiatives. Being different entails considerable risks, especially since compensation is the bedrock of most people's economic well being.

We do know that in product/service markets, first movers have well-recognized advantages that can offset the risks involved --higher margins, capturing market share, brand name recognition, and creating barriers to entry. But it is not clear that such advantages accrue to innovators in total compensation. Detailed analysis explains Ford's decision to double wages in terms of workforce stability (reducing 400 percent turnover), union avoidance, and the like. Similar efficiency gains arguments apply to other innovators. Yet, why was it Henry Ford who moved first? Why didn't his competitors? And what, if any, benefits accrue into the future for being a first mover? It is reasonable to suppose that Ford's first mover advantage disappeared as some of his competitors adapted. And what happens to those who opt not to follow but rather, evolve an existing compensation strategy?

If we cannot say why some are bellwethers, can we say why some are followers? Based on some theoretical work we recently completed, we believe that two primary forces cause organizations to adopt innovative practices: (1) institutional pressures or external forces outlined above, and (2) expected efficiency gains. The expected efficiency gains from innovation is a function of the organization's strategic objectives, which are in turn affected by labor market conditions, the nature of the work, cost factors, and employee preferences.

A third issue is why, once these innovations are adopted, does the variability in their design seem to increase over time? Consider the earlier discussion of TRW's flexible benefits. The logic underlying flexible benefits seems compelling, yet surveys show that about two-thirds of organizations with over 1,000 employees still have not adopted them. Those plans that have been adopted vary considerably in the amount of choice they offer employees. Similar patterns emerge with pay-for-performance and other compensation practices. First, bellwethers move; then some of the flock follows, and others do not.

So while our theoretical view is that institutional forces and expected economic gains create pressure for organizations to adopt changes in compensation systems, experience suggests that government regulations, particularly tax laws, as well as benchmarking fads and fashions prevail.

BACK TO THE FUTURE: LESSONS LEARNED

Since the days of our 1900s owner/operator who bore sole responsibility for people's pay, managing compensation has grown in importance. Laws regulate it, entire units within organizations are devoted to it, countless surveys disseminate information about it, the Federal Reserve Board monitors it, and a global professional society with 25,000 members is devoted to it. Almost no one is indifferent to it. Paralleling the growth in importance is a growth in

sophistication and complexity. The ACA publishes a dictionary of compensation terms, even my textbook devotes 20+ pages to definitions. So many terms, they numb the mind. But in light of such a rich and continuing history, what lesson can we learn from our review that will inform our decisions as we go forward?

*** *End the search for the one “right” compensation strategy for organizations.***

There will always be compensation systems as different from one another as General Electric, Microsoft, Toyota, and Citigroup are from each other. All four organizations compete globally, but all have different compensation systems. The systems these companies have today are different from what they had before and what they will have in the future. Rather than search for the “right” new pay approach, the changing deals of the past century tell us that there is no such thing. Compensation systems will continue to differ, depending on the markets in which organizations compete, the regulations under which they operate, and their technological innovations and strategic priorities.

So if change is a constant, we can best adjust to it by improving our understanding of the circumstances or context in which it occurs. Which leads to the second lesson.

*** *Understand what matters.*** Improving our understanding of what in the context matters improves our understanding of changes required in compensation systems. Culling our brief history, we can extract several factors: (1) expected economic gains, and (2) institutional pressures. Expected gains are a function of the shortages/surpluses of talent, the strategic intentions of the business, and competitors’ practices. Major institutional pressures result from tax and employment legislation, the objectives and power of unions, the nations’ social contract, and the like. Managing total compensation includes tracking and, where possible, influencing the shape of these factors via actively engaging in their formation.

*** *Support pragmatic experimentation.*** Another lesson we take away from our review is that changes in compensation systems evolve largely through trial and error. The past 100 years is a history of practical, applied experimentation, mostly independent of formal theoretical considerations. Though implicit, often unstated models and beliefs held by the managers probably guide their experimentation, formally articulated theories have not appeared to guide these innovations. In light of the pragmatic, applied nature of compensation decision making, some may question the usefulness of theory and research in managing compensation. However, we believe that absent the knowledge of theory and research, the trial and error approach risks being random, ad hoc, and inefficient. Improving our understanding of the factors that matter helps provide an understanding of why some changes are more likely to be useful and why others may be less so. Consequently, we believe that improved theoretical

understanding will help address what changes and experimentation will be useful. At the minimum, the lesson is that experimentation in compensation practices is characteristic of a bellwether. We believe that research can help inform bellwethers. This leads to our fourth and final lesson.

* ***Continuous learning about compensation.*** Based on our brief review of the past century of compensation systems, we are struck by the limited interaction between two activities essential for building understanding. These are **research**: the disciplined pursuit of systematic knowledge, and **practice**: people working together through trial and error to build practical knowledge based on their experience. Compensation research and practice typically occurs in disconnected, specialized organizations (businesses, universities, consultancies), and there is little in the 100 years that we reviewed that could be called a trend toward greater interaction for building knowledge and capacity. There are some exceptions, of course: Scanlon worked at MIT and in the field; several university-based research centers, corporations, and the ACA are experimenting with various forms of alliances to build knowledge through research and joint ventures. Perhaps such knowledge and capability activities are not sufficiently “newsworthy”, hence they have been excluded from newspapers and business magazines. We are hopeful that such alliances will continue so that when the history of the twenty-first century is written, they will be included.

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