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Case studies on Geographically-Differentiated Pay

A research report for the OME

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Contents

1	EXECUTIVE SUMMARY AND KEY FINDINGS	6
1.1	CASE STUDY: KEY FINDINGS	7
1.2	BASIC PAY SETTING	7
1.3	GEOGRAPHICALLY-DIFFERENTIATED PAY	7
1.4	COSTS AND BENEFITS OF LOCAL PAY	8
1.5	LOOSENING LABOUR MARKETS	8
1.6	WHICH EMPLOYEES RECEIVE LOCAL PAY	9
1.7	DECISIONS ON LOCAL PAY DIFFERENTIATION	9
1.8	PROBLEMS WITH LOCAL PAY	9
1.9	LAYOUT OF THE REPORT	9
2	GEOGRAPHICAL PAY DIFFERENTIATION – HISTORY AND CONTEXT OF THE DEBATE	11
2.1	INTRODUCTION	11
2.2	PRIVATE SECTOR EMPLOYERS’ APPROACHES TO GEOGRAPHICAL PAY DETERMINATION	11
2.3	HOW PRIVATE SECTOR EMPLOYERS VARY PAY BY LOCATION	13
2.4	THE DEVELOPMENT OF ZONAL PAY SYSTEMS IN THE PRIVATE SECTOR	14
3	CASE STUDY ANALYSIS AND METHODOLOGY	19
3.1	CASE STUDIES – METHODOLOGY	19
3.2	DETAILS OF CASE STUDY ORGANISATIONS	20
4	ANALYSIS OF CASE STUDY FINDINGS	22
4.1	COMPANY BACKGROUND	22
4.2	PAY SETTING MECHANISMS	22
4.3	PAY STRUCTURES AND PROGRESSION	25
4.4	GEOGRAPHICALLY-DIFFERENTIATED PAY	27
4.5	LOCAL PAY ARRANGEMENTS	27
4.6	THE COST OF GEOGRAPHICALLY-DIFFERENTIATED PAY	32
4.7	WHAT PROBLEM DOES GEOGRAPHICALLY-DIFFERENTIATED PAY SOLVE?	32
4.8	WHICH EMPLOYEES RECEIVE LOCAL PAY?	35
4.9	EMPLOYERS’ REACTIONS TO LOOSENING LABOUR MARKETS	35
4.10	DECISIONS ON LOCAL PAY DIFFERENTIATION	37
4.11	TRADE UNION INVOLVEMENT	37
4.12	GUIDELINES FOR MANAGERS	37
4.13	EVALUATING LOCAL PAY DIFFERENTIATION	37
4.14	PROBLEMS WITH LOCAL PAY	38
5	CASE STUDY A – A SUPERMARKET CHAIN	40
5.1	INTRODUCTION	40
5.2	BACKGROUND	40
5.3	BASIC PAY POLICY	40
5.4	PAY DIFFERENTIATION BY LOCATION	41
5.5	DECISIONS ON PAY DIFFERENTIATION	43
5.6	ROLE OF LOCAL MANAGERS	43

5.7	EFFECTIVENESS OF PAY DIFFERENTIATION	43
5.8	PROBLEMS WITH PAY DIFFERENTIATION	44
5.9	EFFECT OF THE LOOSENING LABOUR MARKET	44
5.10	BUILDING A BUSINESS CASE FOR LOCATION OR MARKET PAYMENTS AT ORGANISATION A - CHECKLIST	45
6	CASE STUDY B – A PROFESSIONAL SERVICES FIRM	47
6.1	INTRODUCTION	47
6.2	BACKGROUND	47
6.3	PAY STRUCTURE	47
6.4	PAY DIFFERENTIATION BY LOCATION	47
6.5	DECISIONS ON PAY DIFFERENTIATION	48
6.6	EFFECTIVENESS OF PAY DIFFERENTIATION	48
6.7	PROBLEMS WITH PAY DIFFERENTIATION	48
6.8	EFFECT OF THE LOOSENING LABOUR MARKET	48
7	CASE STUDY C – A TRANSPORT INFRASTRUCTURE COMPANY	49
7.1	INTRODUCTION	49
7.2	BACKGROUND	49
7.3	BASIC PAY POLICY	49
7.4	PAY DIFFERENTIATION BY LOCATION	50
7.5	DECISIONS ON PAY DIFFERENTIATION	51
7.6	ROLE OF LOCAL MANAGERS	52
7.7	EFFECTIVENESS OF PAY DIFFERENTIATION	52
7.8	PROBLEMS WITH PAY DIFFERENTIATION	52
7.9	EFFECT OF THE LOOSENING LABOUR MARKET	52
8	CASE STUDY D – FINANCIAL SERVICES	53
8.1	INTRODUCTION	53
8.2	BACKGROUND	53
8.3	BASIC PAY POLICY	53
8.4	PAY DIFFERENTIATION BY LOCATION	54
8.5	DECISIONS ON PAY DIFFERENTIATION	55
8.6	EFFECTIVENESS OF PAY DIFFERENTIATION	55
8.7	PROBLEMS WITH PAY DIFFERENTIATION	55
8.8	EFFECT OF THE LOOSENING LABOUR MARKET	56
9	CASE STUDY E – A FINANCIAL SERVICES COMPANY	57
9.1	INTRODUCTION	57
9.2	BACKGROUND	57
9.3	BASIC PAY POLICY	57
9.4	PAY DIFFERENTIATION BY LOCATION	58
9.5	DECISIONS ON PAY DIFFERENTIATION	59
9.6	EFFECTIVENESS OF PAY DIFFERENTIATION	59
9.7	PROBLEMS WITH PAY DIFFERENTIATION	60
9.8	EFFECT OF THE LOOSENING LABOUR MARKET	60
10	CASE STUDY F – A DISTRIBUTION COMPANY	61
10.1	INTRODUCTION	61

10.2	BACKGROUND	61
10.3	BASIC PAY POLICY	62
10.4	PAY DIFFERENTIATION BY LOCATION – CURRENT	63
10.5	PAY DIFFERENTIATION BY LOCATION - HISTORY	64
10.6	DECISIONS ON PAY DIFFERENTIATION	66
10.7	EFFECTIVENESS OF PAY DIFFERENTIATION	67
10.8	PROBLEMS WITH PAY DIFFERENTIATION	67
10.9	EFFECT OF THE LOOSENING LABOUR MARKET	68
11	CASE STUDY G – A RESEARCH-BASED MANUFACTURER	69
11.1	INTRODUCTION	69
11.2	BACKGROUND	69
11.3	BASIC PAY POLICY	69
11.4	PAY DIFFERENTIATION BY LOCATION	70
11.5	DECISIONS ON PAY DIFFERENTIATION	71
11.6	EFFECTIVENESS OF PAY DIFFERENTIATION	71
11.7	PROBLEMS WITH PAY DIFFERENTIATION	72
11.8	EFFECT OF THE LOOSENING LABOUR MARKET	72
12	CASE STUDY H – A TELECOMMUNICATIONS COMPANY	73
12.1	INTRODUCTION	73
12.2	BACKGROUND	73
12.3	BASIC PAY POLICY	73
12.4	PAY DIFFERENTIATION BY LOCATION	73
12.5	DECISIONS ON PAY DIFFERENTIATION	74
12.6	EFFECTIVENESS OF PAY DIFFERENTIATION	74
12.7	PROBLEMS WITH PAY DIFFERENTIATION	74
12.8	EFFECT OF THE LOOSENING LABOUR MARKET	75
13	CASE STUDY I – A RETAILER	76
13.1	INTRODUCTION	76
13.2	BACKGROUND	76
13.3	BASIC PAY POLICY	76
13.4	PAY DIFFERENTIATION BY LOCATION	77
13.5	DECISIONS ON PAY DIFFERENTIATION	79
13.6	EFFECTIVENESS OF PAY DIFFERENTIATION	80
13.7	PROBLEMS WITH PAY DIFFERENTIATION	80
13.8	EFFECT OF THE LOOSENING LABOUR MARKET	80
14	APPENDIX A - QUESTIONS FOR OME CASE STUDIES	82
15	APPENDIX B – LITERATURE REVIEW	85

1 Executive summary and key findings

IDS was commissioned by the OME in February 2012 to carry out between five and ten case studies on how large multi-site private sector firms approach the issue of geographical pay differentiation, and to provide an overall assessment of current practice in addressing local pay across the private sector.

Nineteen large multi-site organisations in the financial services, retail, utilities, transport and communications, manufacturing, healthcare and professional services sectors were approached. They were selected as being typical of multi-site employers as a whole and because they resemble public sector organisations and cover variations in sector, location and the nature of the workforce.

Nine case studies were completed between the middle of March and the OME deadline of the end of the first week in April 2012. They include two retailers, two financial services companies, one transport infrastructure company, one distribution company, one manufacturer, a communications services provider and a professional services company. They employ between 7,000 and 294,000 staff, around 700,000 in total.

Seven interviews were conducted face to face, with the HR director and/or the Head of Reward at headquarters. The other two were based on information supplied by the Head of Reward by phone and e-mail. In all cases the draft case studies were sent back to the organisations to be checked for accuracy.

Specifically, our objectives were to:

- Provide current detailed case studies of how large multi-site employers vary pay by location
- Examine the size of geographic differentials within the case study organisations and how these are determined (i.e. the information used and the decision-making process)
- Determine whether case study employers exclude specific groups of employees e.g. senior staff, and why
- Provide an overview of current practice on local pay across the private sector

- Identify any recent developments in practice on local pay
- Look at any potential problems with local pay e.g. equal value

1.1 Case study: key findings

- Nine case studies of multi-site firms were completed. The organisations include two retailers, two financial services companies, one transport infrastructure company, one distribution company, one manufacturer, a communications services provider and a professional services company. They are of varying size, complexity and locations.
- Employees covered by the research range from distribution and retail staff who require no qualifications to those working for financial and professional services firms or firms engaged in research and development where around half the workforce have first degrees and/or postgraduate academic or vocational qualifications.
- Seven of the nine case study employers negotiate pay settlements for at least some of their staff with recognised trade unions.

1.2 Basic pay setting

- All the case study employers use market or survey data to set basic pay.
- This market data includes location, so location pay is often an integral part of the market pay medians set for roles.
- Labour turnover, absence, the cost of living and staff satisfaction with pay are also taken into account when setting basic (and local) pay.
- Pay structures for the nine employers include spot rates, negotiated pay scales, broad bands and individual salaries for managers.
- Progression is through performance and position relative to market for middle and senior managers while progression for unionised employees is generally through negotiated pay settlements.
- The case study firms set great store by controlling pay – both basic and location-based – centrally.

1.3 Geographically-differentiated pay

- Employers' objectives for their local pay systems are the same as those for their pay setting practices and policies as a whole, with competitiveness with the external labour market being key.

- Two of the nine employers said that the purpose of their London allowances is to compensate employees for higher living costs in London.
- The nine firms use three different forms of geographically-differentiated pay
 - location-specific pay bands/zones
 - traditional London allowances
 - no specific location payments but geographical differentials arising from the use of market data.
- Some companies use different forms for different occupational groups, most frequently but not always, management and non-management staff.

1.4 Costs and benefits of local pay

- None of the employers knew what it had cost them initially to install local pay, or what it cost to administer. And only a few could say what it cost each year, but that is partly because the geographical factor is frequently subsumed into basic pay and not separately identifiable. Identifiable annual costs were between £16 million and £40 million, the latter figure amounting to around 2 per cent of the pay bill.
- Most employers thought they obtained value for money from their spend on local pay, because they had no recruitment and retention problems.
- Labour turnover, recruitment and retention and staff satisfaction are the measures employers most often use to evaluate the success of their overall pay package, including local pay.
- Seven of the nine employers would install similar location pay systems if they did not have one, one would definitely not do so and one wasn't sure.

1.5 Loosening labour markets

- The majority of employers said that labour markets had loosened in 2008; none of them have experienced recruitment and retention problems since then, although only one said that it had had recruitment and retention problems prior to 2008. In response, three of the nine have removed payments for some or all hot spots outside London.
- Several said that although they could reduce or remove location payments they had little desire to do so and would only proceed cautiously, in order to maintain stability and consistency.

1.6 Which employees receive local pay

- Where local pay is subsumed into basic pay as part of the pay benchmarking process, all employees receive the geographical differential for their role. Differentials are highest for the most junior staff and lowest, approaching zero, for the most senior staff.
- All employees receive traditional London allowances in all but one of the organisations that pay them; at the other firm only non-management staff receive them.

1.7 Decisions on local pay differentiation

- Decisions are mostly made either centrally – by senior managers, central HR or the reward team - or are market driven, with little local discretion. Where there is discretion, awards are controlled firmly by budgets.
- The reason organisations give for making decisions at these levels is the need to control the pay bill.
- Only one organisation has formal guidelines for managers to make a case for additional pay at their location. The final decision would be made centrally by a senior manager.

1.8 Problems with local pay

- Although employers were contractually entitled to remove local pay they have not done so. In situations where the allowance was removed from new starters or a business activity was moved from a high-cost to a low-cost location, they continued to pay the previous location allowances to existing staff.
- Case study interviewees were worried by the potential loss of control of the pay bill that local payments could bring about, and took steps to avoid the local discretion that might cause this.
- Equal pay was not seen as a problem by most interviewees, though one pointed out that there would be equal pay implications if people working in neighbouring offices doing the same job were paid different amounts and one finance organisation mentioned that they had equal pay issues under previous geographical hotspot arrangements.

1.9 Layout of the report

The following chapter (2) summarises the history and context of the geographical pay debate. Chapter 3 provides an overview of case study analysis and methodology, chapter 4 examines the amalgamated research findings in more detail and subsequent chapters provide detailed case study findings by individual organisation.

2 Geographical pay differentiation – history and context of the debate

2.1 Introduction

This research report will examine the evolution of different approaches to geographical pay by large, multi-site private sector companies that are a fair comparator for large multi-site public sector organisations, and look at the different approaches in banking and retailing. In both private and public sector groups we are looking at organisations that operate in almost all areas of the country.

Most multi-site private sector companies have national pay structures and operate with either four location allowances (based on inner London, outer London, the South East and national) or four to five zones which are similar to the geographical structure but allow for the reallocation of sites between the zones for recruitment and retention reasons.

Here we investigate companies that have branches and sites all over the country, in much the same way that every area of the country has schools, a hospital, a police station and a local council. Smaller and medium-sized companies will not need to have national pay structures. However, this does not mean that they set pay by locality. These firms will benchmark their pay rates against other companies in their industrial sector and will look at the market rate for the job for key skills in their organisation.

2.2 Private sector employers' approaches to geographical pay determination

IDS's ongoing research over the last decade has established that almost all large companies in the private sector with a network of branches or workplaces around the country operate with national pay structures. Large, multi-site private sector companies, among them retailers, banks and telecom companies, are not dissimilar to large multi-site public sector organisations that have national structures.

Large multi-site private sector companies operate with an optimum of to four to five zones. Zonal pay systems allow for a branch or store to be moved to a higher paying zone if labour market conditions require this. Companies have told us that relegating a store to a lower paying zone is slightly trickier. At times when the labour market is slack, when they are not

experiencing any problems with recruitment or retention, it may be that only four zones – the national zone and three other zones - would be appropriate.

Outside of London and the South East there is much more similarity than difference. In practice, most of the retailers and banks that operate with zonal-type pay systems have national pay structures outside of the South East that have worked well for some time, without seeking to differentiate between Swansea, Sheffield or Sunderland.

Local labour market/cost-of-living factors have not displaced skill level, qualification and job weight in setting pay in the private sector. Even in smaller private sector companies, skills and qualifications will be key factors. There is plenty of evidence that international engineering companies in Gloucestershire and Derbyshire will use international salary data linked to skills and qualifications rather than local data for recruitment purposes. Private sector companies tend to benchmark their pay rates with competitors within their own industry and then with larger employers in their towns or cities. Thus a set of national pay benchmarks tends to influence actual rates of pay.

In the banking crisis and recession of 2008/09 a number of key mergers took place between Lloyds TSB and HBOS and between Santander and some smaller banks. Earlier, Halifax had merged with Bank of Scotland and RBS had taken over NatWest. In all these processes, senior management might have decided to leave salary structures and terms and conditions separate in the old entities, especially if some were paying less for similar grades. In fact, all went through the process of bringing harmonisation to pay structures and to terms and conditions in the merged banks.

Most finance directors of large companies would say that pay budgets have to be set and formal procedures followed for any local variation in pay to be sanctioned. It is not the case that local branch managers in large companies have the freedom to vary pay without reference to head office. In the retail sector, finance directors use pay modelling methods to calculate the budget costs of each one pence on the hourly rates across the company.

Leading HR professionals in large companies with branches throughout the country say that national pay structures and national pay determination provide simplicity, avoid the costs of

duplication, allow for better paybill control, create consistency and avoid poaching and leapfrogging.

It continues to be the case that industrial sector and industry skills are far more important than geography in the determination of pay levels. In the car industry, for example, with different companies operating in East London, Merseyside, the West Midlands, Sunderland, Oxford, Derbyshire, North Wales, and Swindon. There is a great deal of similarity in pay levels by skill grade across the companies. These car manufacturers benchmark pay among one another and against other successful manufacturing companies in the UK.

The history of call centres is of relevance to the understanding of location and pay levels. Technological change meant that employment in call centres could be moved away from London and the South East to avoid paying London and South East allowances. One of the first to move location in the 1990s was London Electricity which moved its white-collar administrative workers to a call centre in the North East (Sunderland). Few of the staff went with the move and the company was able to operate there without the cost of London allowances. As the number of call centres grew many were located in Leeds, Liverpool, Sunderland, Derby, Glasgow, Cardiff and Swansea – all paying ‘national’ rates of pay rather than London and South East rates of pay. Some went to India to low cost areas but many then re-located to the UK. IDS research on pay in call centres has found that most pay variation is based on skill levels required and industrial sector, rather than on geography.

2.3 How private sector employers vary pay by location

Previous IDS research has identified six different ways in which large private sector organisations vary pay by location. There are similarities about each of the approaches, but there are also differences. Most of the ‘hot spot’ approach was designed for tight labour markets, where companies were experiencing recruitment and retention problems, rather than the current slack labour market which has few problems.

1. National pay scales with London/South East allowances. The dominant approach is that which operates with national scales and some form of premium for London and the surrounding area, whether free standing allowances, or higher London pay scales. Examples include BT, Age Concern and Waterstone’s.
2. National pay scales with London/South East additions and ‘hot spot’ allowances. Some organisations have added flexibility to their systems through the ability to pay more in

labour market 'hot spots' outside the traditional high-cost areas. Examples include Nationwide, Sainsbury's and Marks & Spencer.

3. Geographical pay bands. A variant of the London Allowance approach is the geographical pay bands operated by some banks. These can be more complicated as in London some of the banks pay a premium made up of two elements: a free standing London allowance plus a salary differential over national rates. There can also be an element of variation around 'hot spots'. See the example of RBS on page 17.
4. Zonal pay systems. These are well established in the retail sector among the big supermarket chains and other firms with a large number of sites around the country. They typically have three to five pay zones ranging from inner London to a national zone, but they are not defined by geography. Stores or branches of national companies are placed in one of the zones and the system allows for the flexibility to re-zone a store or branch with recruitment/retention problems. In practice head offices are not ready to re-zone a store or branch unless there is substantial evidence for change.
5. Top-up location allowances. Some organisations in retail, such as Gregg's/Baker's Oven and Wilkinson's, operate with a fairly simple system of top-up allowances in locations deemed to qualify for these.
6. Complex localism. One rare approach we have deemed as complex localism. The Body Shop sets a basic rate of pay on top of which 'indexing' for each store is paid, where applicable.

2.4 The development of zonal pay systems in the private sector

In recent years there has been no particularly identifiable new trend in geographical pay differentiation in the private sector. The recession has weakened the labour market generally and reduced recruitment and retention pressures on London and the South East. There may, however, be a new upward cost pressure in London and the South East where the size of deposits for first-time buyers has risen and the price of renting a flat has shot up.

It is still the case that different approaches to geographical pay variation depend to some extent on the industrial sector. It started out with London allowances based on concentric circles out from Charing Cross. At one stage London Weighting was strictly based on cost compensation and was explicitly not about recruitment and retention. That was its original purpose under the Pay Board in the 1970s. This view was based on a view of equity. It aimed to assess how much more an employer needed to pay an employee in London to give them the same purchasing

power as an employee in the rest of the country. Subsequently, the original concept of cost compensation in the determination of locational allowances became increasingly confused with recruitment and retention issues and clarity about the different approaches is important.

When labour markets tightened and unemployment fell in the late 1980s, after deregulation in the City, new allowances were paid in the rest of the South East (Roseland). Once four or five allowances had come into existence employers started to look for methods to re-allocate certain branches from one pay band or allowance area to a higher band or allowance to respond to labour market difficulties. As a consequence, retailers developed a zonal pay system with four or five zones while some of the banks developed hybrids of London and Roseland allowances with the addition of geographical salary bands. Others developed standalone allowances for individual 'hotspots'.

In zonal pay systems there is the possibility of rezoning a store or branch to a higher paying zone if staff turnover or other labour market indicators suggest that this would make a difference and restore stability in recruitment and retention. But it should be noted that rezoning is controlled by head office, to which requests must be submitted, where checks are made that high staff turnover is the result of labour market issues rather than poor management.

Some of the latest developments are not so different from what existed a while ago. Until 1987 the retail banks paid 'territorial' allowances to staff working in branches in five concentric rings around London – 3, 6, 10, 16 and 22 miles from Charing Cross. Increases in these allowances were negotiated from August each year. In addition, staff working in a number of nominated 'large towns' received an allowance of £298 a year. Early in 1987 the banks moved to pay a new allowance down the M3 and M4 corridors. Then the Halifax moved its outer London allowance to the M25. Soon the whole of the South East was covered and the boundaries moved further out to include Cambridge, Poole and Northampton. (IDS Report Labour Market Supplement December 1998).

One key factor that influences the approach to allowances or zones is the size of the local unit. Bank branches are typically small units and there can be several in a town or a city. On the other hand, large supermarkets are now more typically on the edge of town and can employ several thousand staff on a 24 hours, seven-day basis.

Policies towards geographical pay differentiation developed that were appropriate to the size of the unit and the frequency of the units in a particular location. As a consequence, banks developed pay policies based on multiple concentric circles out from Charing Cross - appropriate for a large number of small branches - while retailers developed policies based on allowances to nominated stores, to cover larger workforces and larger workplaces. Subsequently the two systems began to converge on the zonal system.

Previous IDS research (IDS Report on the history of London Weighting, 2002) has shown that the 1990s were the years in which the finance and retail sectors developed different approaches to geographical pay systems. The finance sector had set the highest London and South East allowances and had continued to use the model of multiple concentric circles out from Charing Cross. Over the 1990s this continued, although a minority of firms, particularly in insurance, consolidated allowances.

Changes in payment systems to broad banding and market-related pay meant that London and South East allowances were only parts of the London pay differential.

Meanwhile, developments in retail took another course. In general there are lower allowances in retail than in other parts of the private sector, being proportionate to the lower wages. Whereas other sectors tended to have allowances based on formal systems, the retail sector was less formal and favoured paying allowances to nominated stores with recruitment and retention problems. This developed over the 1990s into zonal pay systems, with three to five zones.

At the start of the 1990s, during the recession of 1990-92, there was less pressure on allowances in the retail sector and the location amounts paid grew very slowly. By the second half of the 1990s there was more use of embryonic zonal systems which a small number of firms, including Argos, Littlewoods and Woolworths, had begun to develop in the 1980s.

Essentially, this system starts from the original basis of the concentric circles out from the heart of London, but then abandons the terminology of geography (inner, outer, fringe) and used categories A to E or 1 to 5. It means that most stores in zone A are in inner London but that stores in other zones can be upgraded to zone A if their level of staff turnover suggests a higher level of pay would alleviate their problems. For example, in April 2001 Safeway, which

operated a pay system with five zones, moved its stores in Bracknell, Reading and Milton Keynes from zone 1a (mainly outer London) to zone 1 (mainly inner London).

In 1999, Tesco announced that its payment of London rates would no longer be confined to stores within the Metropolitan Police boundary. It also set up a working party to look into revising its system of location allowances. In August of that year the company introduced a new national pay structure consisting of five pay zones. The rates in zones 1 and 2 were set at the same level as the former provincial rates. Zone 3 covered provincial areas, such as Oxford and Swindon, in which recruitment and retention problems were being experienced, and areas of London, such as Romford and Woodford Green, where the company felt there was no need to pay the full London rate. Zone 4 covered the former London area of the old structure and included 'hot spots' such as Reading and Gatwick airport. Zone 5 covered mainly central London.

The slack labour market of the mid-1990s gave way to a tightening of the labour market between 1997 and 2000, with falling unemployment and rising employment. This tightening of the labour market had given an impetus to Tesco adopting a zonal model in 1999. The same labour market changes pushed Lloyds TSB to change from a more traditional system of paying London allowances to one which was zonal, with bank branches placed in one of four zones. Subsequently, some of the other leading banks moved to zonal systems. At one stage the Royal Bank of Scotland had a three-band pay model, to which two additional bands were added in 2007.

RBS geographical pay arrangements at April 2011

Zonal pay bands for clerical grades at RBS		
Pay band	Description	Examples of locations
Band 1	National rate	Cardiff, Sheffield
Band 2	Large cities	Glasgow, Birmingham, Manchester, Edinburgh, Leeds
Band 3	Financial services hot spots or towns which previously attracted a large town allowance or South East allowance	Brighton, Bristol, Oxford, Southend
Band 4	Outer London	
Band 5	Inner London	

In April 2001, HSBC introduced geographical pay bands for clerical staff. Three broad bands were established to represent the more significant differentials. The middle band (band B) covered the majority of staff and included southern England outside London and major conurbations, including areas in the North of England which were 'hot spots'. Pay band A covered national areas outside of band B and band C covered London. In pay negotiations for 2012 band A has been removed.

3 Case study analysis and methodology

3.1 Case studies – methodology

IDS approached 19 large multi-site organisations on behalf of the OME to ask if they would be prepared to be case studies. These organisations were in the following sectors: financial services, retail, utilities, transport and communications, manufacturing, healthcare and professional services. Potential organisations were selected on the basis of variations in sector, locations and the nature of the workforce. They were told that the case studies would examine the following areas:

- Overall approach to pay differentiation by location
- The process by which decisions on local pay differentiation are made
- The co-ordination and monitoring of local pay differentiation
- The cost of local pay differentiation
- Evaluation of local pay differentiation/potential problems with local pay differentiation
- The impact of loosening labour markets.

The list of those approached was discussed with the OME beforehand. Confidentiality was not offered to potential case studies in the first instance though every organisation that did take part in the research specifically asked for confidentiality, which was agreed, both when discussing participation and at the time of the interview.

Potential case studies were approached by telephone and e-mail. The five week period available to identify and contact the appropriate potential interviewees, obtain agreement to an interview, conduct and tape the interview, transcribe the notes, write the case study and send it back to the interviewee to check for factual accuracy was tight.

In the event, nine case studies were completed before the deadline. Seven of these involved face to face interviews with a company employee and two were based on information gathered from the employer by telephone and e-mail. The draft case studies were sent back to the companies to be checked for factual accuracy. In several cases the organisations removed information that they felt could identify them, which could amount to substantial cuts to the original draft.

Case study participants were sent detailed questions a few days in advance of the interviews (Appendix A). At the time of the interview they were asked for their permission to tape the interview for the convenience of the researcher, and in all cases this permission was given.

3.2 Details of case study organisations

The nine case study organisations include two retailers, two financial services companies, one transport infrastructure company, one distribution company, one manufacturer, a communications services provider and a professional services company.

Organisation A is a retailer employing 294,000 UK staff in stores varying from small convenience stores to hypermarkets and warehouse-style operations. It has 3,000 stores located throughout the UK, call centres in Scotland and Wales and distribution centres and central departments in the Home Counties. Location allowances are paid only to store staff, the pay of other employees does not vary by location. At 9.8 per cent, labour turnover is the lowest it has ever been and down from 20 per cent in 2010.

Organisation B is a professional services firm that has a large number of staff located in cities all over the UK. Overall pay ranges reflect market area, location and business performance; there are no separate location payments. Labour turnover has fallen recently.

Organisation C is a transport infrastructure company with 35,000 staff working in offices and depots throughout England, Scotland and Wales. The company pays national rates plus location allowances to employees in inner London, outer London and the South East. External market data is used to set pay for some groups, and this reflects the differential between London pay rates and those for the rest of the country. Labour turnover is 3.7 per cent for the more junior grades, lower for more senior colleagues.

Organisation D is a financial services company employing 25,000 people in 1,300 branches throughout the UK and eight call centres. The company pays national rates plus allowances for those working in inner, outer and fringe areas of London. These 'London only' allowances' replaced payments for geographical hot spots in 2010. Labour turnover is just over 10 per cent overall, up to 27 per cent in some contact centres outside London.

Organisation E is another financial services company. It has 44,000 UK staff working in retail branches throughout the UK, call centres in the Home Counties, the North of England, Wales and Scotland and a London headquarters. It has geographically-differentiated pay in the form of two pay structures for administrative and clerical branch staff by location (one national, the other London and other large conurbations). There were previously three location-based pay structures but two have been amalgamated. There are also three territorial allowances covering, respectively, London, hot spots such as Manchester and Birmingham, and other hot spots. Labour turnover is 6 per cent, and 10-12 per cent in call centres.

Organisation F is a distribution organisation with 150,000 staff working throughout the UK. It has three pay scales, national and inner and outer London. There are also two sets of recruitment and retention allowances, which together provide a range of seven separate payments. Excluding retirement, redundancies and dismissals, voluntary labour turnover is 1.3 per cent for full-time staff, 9 per cent for part-timers.

Organisation G is a research-based manufacturer with 7,000 UK employees working in London, the Home Counties and the North of England. The company pays national rates, and allowances based on external market data to those working in its London office. Labour turnover is 5 per cent and has been stable for many years.

Organisation H is a communications company with around 80,000 employees located throughout the UK. It pays legacy inner and outer London allowances to non-management staff only. Labour turnover is 8.5 per cent.

Organisation I is a retailer with 50,000 staff in branches nationwide, a head office, a call centre and in-house distribution. Since 2011 the company has only paid location allowances to those working in central and outer London. Its pay zone covering staff in larger cities and small South East towns was removed in that year. Labour turnover is 39.5 per cent.

4 ANALYSIS OF CASE STUDY FINDINGS

4.1 Company background

Case study organisations employ between 7,000 (organisation G) and 294,000 (organisation A) staff in the retail, financial services, transport, communications, distribution, manufacturing and professional services sectors. Their complexity varies; organisation A has 3,000 stores of six different sizes together with call centres, distribution centres and central departments, organisation G has a London office, a sales function, and an R&D/manufacturing site, while organisation B has professional services offices throughout the UK.

Employees covered by the research range from distribution and retail staff who require no qualifications to those working for financial and professional services firms or firms engaged in research and development where around half the workforce have first degrees and postgraduate academic or vocational qualifications.

Seven of the nine case study employers negotiate pay settlements for at least some of their staff with recognised trade unions.

4.2 Pay setting mechanisms

All the case study firms sets basic pay with reference to market or survey data, and location is often identified as an integral part of the market data. Towers Watson, Alan Jones, IDS, Hay Group and industry-specific surveys were most frequently mentioned by the case study organisations as sources of market pay data. Most companies aim to pay median rates, often using the median as the midpoint of a range, with above median earnings available to their best performers. Organisation A is an exception, choosing to pay market leading rates, more than its supermarket competitors and above the medians identified by Hay and Alan Jones. Companies also use data on pay settlement and earnings trends, such as from the Annual Survey of Hours and Earnings and IDS, especially when negotiating with trade unions who may be more interested in legacy rates than market rates.

Several case study interviewees said that they were trying to streamline their use of market data; one organisation has reduced the number of surveys used from about 20 a few years ago to two or three main sources for most roles in 2012. The reason for the streamlining is partly financial – surveys can cost £20,000 each – and partly because it has been found that fewer

roles can be benchmarked where the benchmarking of multiple roles over time has consistently produced similar market salaries.

Organisations were not entirely happy with the survey data. One commented that the regions used were too broad, but that it would be much too expensive to get the data 'cut' to its own specification. Another said 'Comparisons are a problem – how do you know the businesses you're comparing yourself with are doing the same job or require the same skill sets?'

Table 1: Case study organisations' use of market data		
Organisation	Type of business/number of employees	Use of market data
A	Supermarket retailer/294,000 UK staff	Sets basic pay rates using data from Hay Group, which compares salaries for like-for-like jobs in around 550 companies in 15 different regions and from Alan Jones, which also provides sector specific pay data by region.
B	Professional Services firm/10,000-15,000 UK staff	Uses market benchmarking survey data appropriate to the market specialism and region, where applicable.
C	Transport infrastructure company/35,000 staff	Organisation C uses Towers Watson, Hay Group and Aon Hewitt to set pay for technical staff and managers.
D	Financial Services firm/25,000 staff	Uses Towers Watson, saying that it bases pay entirely on 'market intelligence' rather than the cost of living.
E	Financial Services/44,000 UK staff	Uses Towers Watson, but also takes data from the Annual Survey of Hours and Earnings, IDS, the EEF and other sources into account when trying to determine trends.
F	Distribution company/150,000 staff	Uses Hay Group, IDSPay and industry-specific sources to set senior managerial pay.
G	Research-based manufacturer/7,000 UK staff	Uses Towers Watson and industry-specific surveys for its non-unionised workforce.
H	Telecommunications firm/80,000 staff	Benchmarks rates. But 'is there a real difference between pay rates in UK regions outside of London and the South East? Comparisons are a problem – how do you know the businesses you're comparing yourself with are doing the same job or require the same skill sets?' Cost of living studies are more relevant than specific labour markets. Use IDS and London Living Wage data.
I	Retailer/50,000	Part of a retail pay forum where pay policy decisions are discussed by high street retailers and also uses external sources such as IDS to follow market trends.

Other factors

Factors other than market data taken into account in pay setting include labour turnover, absence, the cost of living and staff satisfaction with pay

4.3 Pay structures and progression

The nine case study organisations exhibit a variety of approaches to setting basic pay. There are spot salaries for unionised staff at organisations A and G, negotiated pay scales for all but the most senior managers at organisation F, and broad bands at organisation B. While it is invariably the case that senior managers are on individual salaries, this is the case for all managers at organisation E, which has no pay scales or broad bands for managers.

Progression for middle and senior managers is through their performance and, in some cases, how their pay compares to the market median, while progression for unionised employees is generally through negotiated pay settlements. In some organisations, good performers who have reached the top of their salary ranges receive unconsolidated cash payments rather than a salary increase.

Table 2: Case study organisations' pay structures and progression arrangements		
Organisation	Type of business/number of employees	Pay structures and progression
A	Supermarket retailer/294,000 UK staff	There is a four-grade structure for weekly-paid retail staff, with starter and established rates, with pay settlements reached through collective bargaining at national level. There is also a six-grade structure for more senior store managers and a broad banded structure for central and distribution staff earning between £25,000 and £100,000, through which staff progress on merit.
B	Professional Services firm/10,000-15,000 UK staff	There are five levels of seniority in the organisation and pay is organised into a series of five broad bands.
C	Transport infrastructure company/35,000 staff	There are 'dozens' of legacy pay ranges for maintenance and operations staff while pay for other staff is set on an individual basis in line with market data. Pay increases are negotiated with the recognised trade unions.
D	Financial Services firm/25,000 staff	There are centralised pay and progression arrangements and pay settlements are reached annually through collective bargaining.
E	Financial Services/44,000 UK staff	There are three pay structures, one for call centre staff below managerial level and two for branch clerical and administrative staff, with pay increases negotiated with the recognised union. Managerial pay is entirely discretionary; there are no pay scales or broad bands. The company consults with a non-union management representative body.
F	Distribution company/150,000 staff	There are three sets of pay scales for operational, administrative and secretarial staff, and engineering staff, with pay increases negotiated through collective bargaining. Senior managers are on individual salaries.
G	Research-based manufacturer/7,000 UK staff	Negotiated pay rates for the unionised manufacturing employees; pay ranges for benchmarked roles, through which staff progress through performance and their position relative to the median. Internal equity and the budget are also taken into account.
H	Telecommunications firm/80,000 staff	Separate pay negotiations with recognised trade unions for management and non-management staff.
I	Retailer/50,000	Non-negotiated pay scales for retail staff and managers.

Bonuses

Some of the case study organisations (B, E and G) pay bonuses, which can be substantial, based on company or unit and individual performance. Bonuses are often used explicitly to reward good performers above the median.

Controlling pay

The large multi-site employers selected as case studies set great store by controlling pay – both basic and location-based - centrally. One said, ‘if you have a large number of employees you need a structure or it becomes a free for all. You don’t have a direct line of sight to what’s going on locally and there might be local inconsistencies.’

4.4 Geographically-differentiated pay

Objectives

Case study employers’ aims for their local pay systems are the same as those for their pay setting policies and practices as a whole. Competitiveness with the external labour market is key for most employers. When asked about their objectives, two employers said ‘To manage our pay in line with the market’, one said ‘to pay fairly and in line with the market’ and another said ‘to pay competitively, in line with the market. One said ‘to deal with recruitment and retention’ while another commented that ‘we don’t think of what we do as local pay so we can’t identify separate objectives. Our overall philosophy is to pay at the right level to recruit and retain staff, and to pay staff fairly in line with the market and internal relativities.’ Two employers mentioned living costs, saying that the objective of their local pay system was ‘to cover the cost of living’.

None of the organisations have recruitment or retention supplements for individuals, only very broad categories, such as ‘store staff’.

4.5 Local pay arrangements

The preceding discussion of overall pay setting arrangements showed that all the case study organisations use external data to help determine pay. Three organisations take this further and, for some groups of staff at least, have no separately identifiable local pay since differentials arising from external market data are incorporated into basic pay.

Table 3 shows the variety of geographically-differentiated payments made by the nine case studies. Arrangements fall into four categories:

- Location-specific pay bands/zones, as at organisations A, F, and I
- Traditional London allowances, as at organisations C, D and H
- No specific location payments but geographical differentials arising from the use of market data, at organisation B
- Combinations of two of the above, at organisation E and G.

Table 3: Case study organisations' local pay arrangements				
Organisation	Type of business/number of employees	Location payments	Annual cost to the organisation, where identifiable	Further details
A	Supermarket retailer/294,000 UK staff	There are five location-specific pay bands/zones for store staff, national and four others: London postcode areas £1.01 per hour for retail staff and £5,350 pa for section managers M25 outside London postcodes £0.68 per hour for retail staff and £3,800 pa for section managers Home Counties £0.45 per hour for retail staff and £1,800 pa for section managers larger towns outside the South East £0.03 per hour for retail staff and £800 pa for section managers.	£40 million, about 2% of the pay bill, paid to around one third of the overall store workforce – 79,000 employees.	Allowances last updated in 2009. Only paid to store staff. All other employees paid national rates, regardless of location
B	Professional Services firm/10,000-15,000 UK staff	Pay set according to external market data, which incorporates locational differences		
C	Transport infrastructure company/35,000 staff	There are three location allowances, set on the basis of cost compensation: 0-16 miles from Charing Cross £2,400 pa 16-40 miles from Charing Cross £1,390 pa a radius encompassing distances between 40 miles from Charing Cross and the South Coast £955 pa These allowances are paid in addition to the following differentials between London pay rates and pay rates for the rest of the UK arising from market pay data: : 21% for central London and 5% for outer	£16 million	Allowances last updated in 2009

		<p>London for more junior technical roles and secretarial and administrative staff</p> <p>10% for central London and 5% for outer London for junior manager and more senior technical roles</p> <p>5% for the most senior roles working within 40 miles of Charing Cross</p>		
D	Financial Services firm/25,000 staff	<p>There is a national rate and three London allowances, incorporated into salary ranges:</p> <p>0-6.99 miles from Charing Cross £3,500 pa</p> <p>7-21.99 miles from Charing Cross £2,000 pa</p> <p>22-36.99 miles from Charing Cross £1,000 pa.</p>	6,500 employees, around a quarter of the workforce, receive allowances.	In 2011 the current system of London allowances replaced legacy arrangements based on geographical hot spots.
E	Financial Services/44,000 UK staff	<p>There are three territorial allowances:</p> <p>Central London £4,000 pa</p> <p>Hot spots such as Manchester and Birmingham £2,000 pa</p> <p>Hot spots such as Worthing £1,000 pa.</p> <p>There are also two pay bands for branch clerical and administrative staff, national and hot spots, with a differential of about 6% between them.</p>		Allowances last increased in 2007. There used to be two pay bands for locations outside London but there is now only one.
F	Distribution company/150,000 staff	<p>There are inner (up to 4 miles from Charing Cross) and outer (within London postcodes) London and national pay scales, with a differential of approximately £91 and £66 per week respectively over the national scales. There are also a series of additional recruitment and retention supplements ranging from £5 (e.g.</p>	£25 million, paid to around 10,000 employees.	

		Bromley) to £35 (e.g. Oxford, Sevenoaks) per week.		
G	Research-based manufacturer/7,000 UK staff	Central London staff receive the better of an allowance or a fixed percentage of salary, according to grade. The percentages are the differentials between London and national rates, arising from the market data used to establish a market median for each role.		Employees in the Home Counties and the North West of England receive national rates.
H	Telecommunications firm/80,000 staff	Inner London (0–4 miles from Charing Cross) allowance of £3,600 pa and outer London (4–18 miles from Charing Cross) allowance of £1,600 pa.		Reviewed every year though not always increased.
I	Retailer/50,000	National rates plus pay scales for inner and outer London. Retail staff in larger cities and small South East towns, who previously received a 5% premium, now receive national rates. Distribution staff in Hemel Hempstead receive an 11% premium on national rates		Until 2011 the company operated a zonal pay structure with four zones. One of these was removed in 2011, leaving national rates plus allowances for central and outer London.

4.6 The cost of geographically-differentiated pay

None of the case study organisations could say what it had cost them initially to install their geographically-differentiated pay systems and none could identify the recurring administration costs of their system, though several said that it would be minimal. An organisation said that its London allowances were not costly to administer but a more complex system of geographical allowances would be: ‘You would have to have ten different systems and that would be costly.’ Just three employers told us what their local pay allowances cost them in direct payments each year, with the figures ranging from £16 million at organisation C to £40 million – around 2% of the pay bill – at organisation A. In several cases employers do not identify the cost of local pay since for them location is just one part of the pay benchmarking process used to set pay rates.

When asked if they obtain value for money from their ‘spend’ on local pay, some case study employers said that they did, because they had no recruitment and retention problems. Others said that it is just part of the overall pay package so cannot be evaluated separately. One firm said that it wasn’t sure whether it obtained value for money.

4.7 What problem does geographically-differentiated pay solve?

As discussed in section 1, geographically-differentiated pay was introduced in the past either to compensate employees for the higher cost of living, principally in London, or to help them recruit and retain staff in an era of tight labour markets, or both. Two companies – C and H – were clear that their London allowances were intended to compensate staff for the higher cost of living in London. Company H said ‘Studies show that there’s a cost premium of around 7 per cent for London. There’s a definite cost of living issue and London allowances help with that.’

But while the higher cost of living in London is undiminished, labour markets have, in general, loosened. IDS asked the case study employers about their labour turnover and whether they were experiencing recruitment and retention problems. One organisation said that it has ‘an unhealthy lack of turnover’ and another commented that ‘there have never really been any recruitment and retention problems, even before 2008’. A financial services organisation said that recruitment and retention ‘is not just about pay. We have to think of the employee proposition, their base pay and bonuses.’ This was backed up by an employer who said ‘you can’t say it is just pay. There are issues about job content too.’ Most of the case study employers regularly assess staff satisfaction with overall pay levels through employee surveys.

Table 4 shows that none of the case study organisations have experienced recruitment and retention problems in the last few years. In response, three organisations have removed payments from some or all hot spots outside London. Organisation D did this in 2011, replacing legacy arrangements based on geographical hot spots with London allowances. Organisation E merged two of its pay bands for staff outside London so that now there is a national scale and another scale for staff working in London and large conurbations, instead of a national scale and two pay bands for London and other hot spots. Organisation I, which used to operate a zonal pay structure with four zones, removed the zone covering retail staff in larger cities and small South East towns in 2011. There are now just national rates plus allowances for central and outer London. In a different approach, employers who have left the structure of their payments intact - organisations A, C and, E – have not updated the value of location payments for several years.

Table 4: Labour turnover and recruitment and retention problems in eight case study organisations				
Organisation	Type of business/number of employees	Labour turnover	Recruitment and retention problems prior to 2008?	Recruitment and retention problems since 2008?
A	Supermarket retailer/294,000 UK staff	9.8% in stores, the lowest it has ever been, down from 20% in 2010	Yes	No
C	Transport infrastructure company/35,000 staff	3.7% for the most junior grades	No	No
D	Financial Services firm/25,000 staff	Just over 10% overall, up to 27% in some contact centres outside London	No	Not generally but problems in some areas as a result of replacing local pay arrangements with a national rate
E	Financial Services/44,000 UK staff	6%, 10-12% in call centres	Had a few problems	No
F	Distribution company/150,000 staff	Voluntary resignations are running at 1.3% for full-timers, 9% for part-timers	Yes	No. There are a few hot spots but they are dealt with through redeployment
G	Research-based manufacturer/7,000 UK staff	6%, stable for many years	No	No
H	Telecommunications firm/80,000 staff	8.5% (average)	No	No
I	Retailer/50,000	39.5%	More difficult to recruit than in 2012	No, because there are many applicants for each job.

4.8 Which employees receive local pay?

Where local pay is subsumed into basic pay as part of the pay benchmarking process, all employees receive the geographical differential implicit in the benchmarking data as part of their base pay, rather than a separate allowance. Organisation G pointed out that the differential between national and London market pay rates is highest for the most junior staff and approaches zero for senior staff, and another organisation commented that differentials are lower for senior staff. At a third organisation – C - there is a 21% embedded market pay differential between national and central London pay rates for junior technical and secretarial and administrative staff while for the most senior roles working within 40 miles of Charing Cross the embedded differential is 5%.

In all but one of the case study organisations which pay the traditional flat rate London allowances, all employees received them. In the other company – H - only non-management staff were paid them. However, when it comes to zonal pay arrangements, these tend to be confined to more junior staff in shops and bank branches. Organisation A has national rates and four other location-specific pay bands/zones for retail staff and section managers while organisation E has two pay bands for branch clerical and administrative staff, one national and one for staff in London and other large conurbations. Organisation D, a bank, used to have zonal arrangements based on geographical hot spots but replaced them in 2011 with a system of London allowances incorporated into salary ranges.

4.9 Employers' reactions to loosening labour markets

Apart from the changes described above, IDS asked employers if they were planning any further changes to their local pay arrangements. Several said that they could reduce or remove location payments, but wished to proceed cautiously, in order to maintain stability and consistency. One had done so in 2009, when some locations had premium payments taken away while others gained them, resulting in a cost saving of £500,000, about 0.025 per cent of the pay bill. Other employers said that they definitely would not remove supplements. 'We don't want market pay going up and down, so we don't review it every year' another employer said. One employer commented that 'he had a problem when industry wanted to take advantage of high unemployment to reduce costs. It's a very short term approach.' A few firms commented that it would be difficult to reduce or remove location payments in the face of opposition from their recognised trade unions.

Table 5: Case study organisations' reactions to loosening labour markets		
Organisation	Type of business/number of employees	Reaction
A	Supermarket retailer/294,000 UK staff	There have been no changes to the location bands in which stores are placed nor the amounts paid to staff working in them since 2009. The fall in labour turnover and absence of recruitment and retention problems has resulted in anecdotal feedback from some stores that location rates might be reduced, since they are no longer necessary to recruit and retain staff. But HR has decided not to do this to avoid inconsistencies between neighbouring stores and also because it will soon conduct a full review of the process.
B	Professional Services firm/10,000-15,000 UK staff	Considers the changing labour market and the ability to recruit and retain staff alongside market benchmarking data.
C	Transport infrastructure company/35,000 staff	Local allowances are set on the basis of cost compensation so labour turnover would have no effect either way.
D	Financial Services firm/25,000 staff	Has already (2011) replaced local pay arrangements with national pay rates and London allowances.
E	Financial Services/44,000 UK staff	Will continue to make location payments in the interests of stability and its long-term approach to pay setting. It would only change the payments on the basis of labour market intelligence, labour turnover and an analysis of potential cost savings.
F	Distribution company/150,000 staff	The company would like to review its arrangements but says that this is subject to negotiation with the union.
G	Research-based manufacturer/7,000 UK staff	Is not aware of any loosening of its relevant labour markets, but as its location payments are based on external market data it could remove or reduce them. But it would approach such a project with caution, and says that it 'does not want market pay going up and down all the time.'
H	Telecommunications firm/80,000 staff	We could take London allowances away but it would probably cause industrial relations problems. It would be very short term approach to do this.
I	Retailer/50,000	Has already (2011) removed one of its pay zones.

4.10 Decisions on local pay differentiation

Decisions on local pay differentiation are either mostly made centrally or are market driven, with little local discretion in the case study organisations. Store managers can make representations at organisation A, but decisions are made centrally. At organisation E local managers can give feedback during the annual review process, but decisions are made elsewhere. Decisions at organisation G are made by a local manager and their manager, but this is within market pay matrices and formulas, and is firmly controlled by budgets. In the past, organisation D had legacy arrangements of local pay, which were locally negotiated. These were a 'complete disaster' since local negotiations resulted in massive cost issues and were very tough to administer. These arrangements have now been replaced by a centrally determined set of London allowances.

Central HR makes the decisions at organisations A, the reward team decides after negotiations with the unions at organisation H and senior managers decide at organisations B, C, D and E. Organisation F reaches decisions through national negotiations with national trade union officials. The reason organisations give for making decisions at these levels is the need to control the pay bill.

4.11 Trade union involvement

Where trade unions are recognised they are involved at national level in negotiating local pay additions. At organisation A the unions were involved in the initial setting of pay bands, the amounts to be paid, and the process by which changes could be made.

4.12 Guidelines for managers

Only one organisation - A - provides guidelines for managers in preparing a case for additional pay at their location and has a formal process for putting such a case forward. In some other organisations, local managers are free to raise the issue informally with HR, which may or may not then take the matter forward to more senior managers. Where pay progression is linked to performance, managers are given information and guidelines on the whole pay setting process so that they can operate the performance pay system and explain pay awards to their staff.

4.13 Evaluating local pay differentiation

Labour turnover, recruitment and retention and staff satisfaction are the measures employers most often use to evaluate the success of the overall pay package, including local pay, and on these indicators employers are satisfied with the outcomes of their policies. When asked if they

would introduce a system of local pay if they currently did not have one, all but two said yes. The exceptions were two organisations with large unionised workforces' One said 'Absolutely not!' and the other said 'probably not at this point. There's no real pressure to get people to London. People generally are more mobile, more willing to move.'

Most of the case study companies use employee opinion surveys to gauge staff satisfaction with overall pay levels. The majority of surveyed organisations said that their employees understood the system for deciding upon and the purpose of local pay, or pay determined by geographical pay data, and where they understood it, they thought it fair. An organisation which has turned down requests from locations for local pay premiums on the grounds that none of the indicators – labour turnover, the staff survey, and what its other local shops were paying – justified it, said that these employees probably didn't think the system was fair. And one organisation said that staff occasionally challenged the differentials between locations identified by market pay data.

4.14 Problems with local pay

One of the main problems identified elsewhere, though not by our case studies, is the difficulty of removing pay additions given to support recruitment and retention. The fact that our case study interviewees were so unenthusiastic about taking their local payments away, even though they were usually entitled to do so, suggests that such a step would be counterproductive; costs would be saved but the effect on employee satisfaction would be considerable. When one case study organisation relocated from a high cost to a low cost area it found that it had to continue paying the supplement if it wanted staff to move to the new office, even though it had planned to pay no supplement in the new location. And when organisation I removed its zonal pay system and reverted to London allowances, it did not reduce the pay of existing staff who were receiving them.

Another potential problem with local pay additions is that staff who do not receive them may feel hard done by. That does not seem to be the case at the surveyed organisations, perhaps because the supplements and allowances have been in place for a long time and everyone has got used to them.

The case study employers said that staff could be moving to areas where local supplements were being paid or being discouraged by the supplements from moving away from those areas

for promotion, but the interviewees were not themselves aware that this was a problem. One organisation commented that the payments weren't high enough to make people want to undertake a longer journey to work.

Comments from case study companies suggest that one of the biggest potential problems with local pay differentiation is lack of control. All the case studies ensure that their systems are under firm central control, and the one organisation – I - that used to have pay zones and more local input has recently changed the system. 'For a long time pay just went up and up and there was no motivation for store managers to tell HR if they felt that they no longer needed to pay a higher rate to recruit.' Now there are only inner and outer London allowances.

IDS asked interviewees if they had considered the equal pay implications of varying pay by location. One firm said that they hadn't thought about it, and were pleased to be prompted to do so. Another said that they were sure there were no problems because they conducted regular equal pay audits. A third, which sets all pay with reference to external market data which embeds geographical differentials, was sure that it could defend these. A fourth commented that 'we need appropriate differentiation between the rewards received by different individuals, but location isn't it.' And a fifth, which only pays London allowances, was sure that there would be equal pay implications if people working in offices relatively close to each other and doing the same job were paid different amounts.

5 Case study A – A supermarket chain

5.1 Introduction

Organisation A replaced the previous London Weighting allowance with a system of local pay in 1999. Since then stores have been placed in one of five bands covering national locations, London, inside the M25 except for London postcodes, other Home Counties locations, and larger towns outside the South East. Four levels of hourly or annual allowances are paid to customer service staff, skilled staff, section managers and line and more senior managers in stores in these locations.

Labour turnover fell from over around 20 per cent in 2010 to 9.8 per cent in the current year at this company's stores. It has made no changes to either the amount of location allowances or the stores which receive them since 2009, although it did receive some anecdotal feedback from a few store areas that location rates might be reduced given the absence of recruitment and retention problems. The company has not done this partly because it wants to avoid inconsistencies between neighbouring stores and partly because a major review is imminent.

5.2 Background

This international retailer employs 294,000 UK staff (493,000 worldwide) in six store formats, ranging from small convenience stores to hypermarkets and warehouse-style operations selling non-food items such as furniture. It has 3,000 stores located throughout the UK, call centres in Scotland and Wales, and distribution centres and central departments in the Home Counties. Location allowances are only paid to store staff; the pay of other employees does not vary by location.

Retail staff include non-skilled hourly paid employees working a range of shifts to cover a 24-hour operation, the majority of whom are part-time, working an average of 22 hours a week, skilled workers such as butchers and bakers, section and line managers, senior managers, such as personnel managers, and store managers.

5.3 Basic pay policy

Pay settlements for store staff and section managers are reached through collective bargaining at national level. There is a four-grade structure for weekly-paid staff with established rates for staff who have completed 12 months' service and starter rates which are 95 per cent of the

established rates. In addition there is a six-grade structure for more senior store managers, with pay ranges based on store turnover, through which managers progress on merit, and a broad banded structure for central and distribution staff. Four wide bands cover a range of staff from junior managers to directors, earning between £25,000 and £250,000.

Staff employed at the company's convenience stores are covered by a separate pay and grading structure. At most stores all staff below supervisory level are on the same grade which pays approximately 6 per cent less than the equivalent grade in the main stores. These staff are eligible for a four-week bonus scheme through which they can earn up to 20 per cent of basic salary. The bonus is calculated on a combination of targets based on stock loss and customer service.

Pay structure at 3 July 2011- retail staff			
Grade	Job examples	Starter £ph	Established £ph
B&C	Customer assistant	6.65	7.00
D	Fishmonger, semi-skilled baker	6.99	7.36
E	Skilled baker	7.41	7.80
F	Lead baker	7.89	8.31

Pay structure at 3 July 2011- retail section managers				
Section managers (in applicable superstores)		Appointment £pa	Development £pa	Established £pa
C1	Grocery manager	19,767	20,864	21,963
C2	Security manager	21,684	22,887	24,093

Organisation A sets basic pay rates using data from Hay Group, which compares salaries for like-for-like jobs in around 550 companies in 15 different regions, and from Alan Jones, which also provides sector-specific pay data by region. The company chooses to pay market leading rates, more than its supermarket competitors and above the medians identified by Hay and Alan Jones.

5.4 Pay differentiation by location

Organisation A sets out to manage pay in line with the market, especially where demand for labour exceeds supply. It believes that it is most important to get basic pay right, and to use location allowances as fine tuning. Location allowances are paid only to store staff, all other employees are in receipt of national rates, regardless of salary level or location. All staff apart

from directors are considered to be part of local labour markets. Allowances are paid to all staff in store as shown in the tables below; there are no discretionary allowances.

Location allowances at 3 July 2011 – retail staff and section managers			
Band		Retail staff £ph	Section managers £pa
1	National	No allowances	
2	Larger towns outside the South East, excluding new stores	0.03	800
3	Home counties	0.45	1,800
4	M25 outside of London postcodes	0.68	3,800
5	London postcode areas	1.01	5,350

The company uses five location bands for store staff. Band 1 is the national rate. Staff in stores in bands 2-5 receive hourly supplements while section managers receive annual supplements. Although there is an allowance for larger towns outside the South East it is just 3 pence per hour for non-managerial staff. The company does not pay this in the new stores it opens in the band 2 areas, and is currently considering options on whether to continue with this band. A store in a larger city outside the South East could be in band 3 or in band 4 if this is required to keep pay in line with that of other businesses in the town.

Staff working in convenience stores receive location payments worth around 6 per cent less than those paid in the bigger stores, which is in line with basic rates which are about six per cent lower than those of colleagues elsewhere.

Line managers and senior store managers receive an additional 10 per cent of salary in locations inside the M25 and an additional five per cent of salary in hot spots. In total, around one third of the overall store workforce – some 79,000 employees – receive location pay - at an approximate cost of £40 million in 2011, around 2 per cent of the pay bill. The system has been in place for many years and with regular reviews has been easy to administer. There is a detailed review planned for the near future.

5.5 Decisions on pay differentiation

Decisions on pay differentiation are made at national level, by central HR, in order to control the overall pay bill. Group and area management teams can make representations, such as requesting the removal of location allowances, discussed below, but the centre makes its own decisions, based on the following data:

- supermarket competitors' location rates
- staff satisfaction with their overall pay, identified through the annual staff survey
- the number of leavers with more/less than one year's service
- absence rates
- the store wage percentage versus sales percentage
- store manager performance grade
- for store staff and section managers, salaries for like-for-like jobs in around 550 companies across the market in 15 regions, provided by Hay Group
- for store line managers and the senior team, market data from Alan Jones.

Stores where the company believes it is underpaying are prioritised through consultation with operations directors, and the prioritised list is taken to the staff pay negotiations. The recognised union was consulted over the design of the location pay system, and up until very recently was consulted about stores changing bands. They would continue to be consulted over any proposals to vary the amounts paid.

Basic pay and allowances are reviewed each April and announced in June. Store staff meet their line manager face to face in groups to be informed about changes to the terms and conditions. Staff have also been given a leaflet explaining the changes.

5.6 Role of local managers

All decisions are made centrally, but local managers have the option to feed their views into the process. They are provided with a 'business case pack' which sets out the information required to put forward in a case for an increase in location pay. One of the functions of the checklist (see below) is to enable managers to find out if people are leaving or are dissatisfied because of their pay or for other reasons.

5.7 Effectiveness of pay differentiation

The company uses local pay to enhance its rates to help it recruit and retain staff, in the context of its policy of paying the highest rates of all major supermarkets. It believes that it obtains

value for money from its expenditure on location allowances, basing that view on the following indicators: labour turnover, staff satisfaction with their overall pay, and feedback from stores.

The only slight reservation organisation A has about its current system is that it 'would like to be slicker about turning allowances on and off'. It also has some doubts about the effectiveness of one of the five bands, since the amount paid (3 pence per hour to store staff) is low.

5.8 Problems with pay differentiation

Organisation A bases the four bands in which stores receiving additional location allowances are placed on the 15 regions used by Hay Group. It comments that Hay regions are very large, so there are no cliff edge effects on or bidding wars between neighbouring stores. On the other hand the Hay regions are not always identical to the regions that the company thinks appropriate. There has been no feedback from stores that staff mobility between stores has been affected.

5.9 Effect of the loosening labour market

Labour turnover has fallen from 20 per cent in 2010 to 9.8 per cent in 2012. There have been no recent changes to either company policy or practice in recent years, and neither the amount of location allowances nor the stores that receive them have changed since 2009. The fall in labour turnover and the absence of recruitment and retention problems has resulted in anecdotal feedback from some store areas that location rates might be reduced given that at present they are no longer necessary to recruit or retain staff. But the company's central HR department, which controls the process of deciding which stores get allowances, has decided not to do this. This is partly because it does not want any inconsistencies between neighbouring stores and partly because it will soon conduct a full review of the whole process.

5.10 Building a business case for location or market payments at organisation A - Checklist

Use this checklist to help you build up the information needed for your business case.

VACANCIES

- ☐ Review the number of vacancies in your store, and identify any trends in Departments or level of staff / managers.
- ☐ Review the average length of time to fill vacancies for your store and Departments.

LOCAL LABOUR MARKET

- ☐ Contact your local Job Centre to find out the local unemployment rate
- ☐ Establish who your local competitors for staff are.
- ☐ Find out their rates of pay and benefits (including night and Sunday premiums and location pay).
(You may be able to get this information directly from your competitors or from your local Job Centre.)
- ☐ Do their rates of pay and/or benefits vary according to length of service?

RECRUITMENT

Are you making effective use of:

- ☐ Instore advertising/recruitment POS Toolkit
- ☐ Open days
- ☐ Job Centre/Career Fairs/Job Fairs.

LABOUR TURNOVER & RETENTION

- ☐ Review your Labour Turnover Analysis reports for the last 13 periods and identify any trends with specific departments/full-time vs part-time/ student leavers/seasonal trading patterns.
- ☐ Compare your store's figures with your Group/cluster.
- ☐ From the same reports, note your annual retention figure and compare with Group/cluster averages.

REASONS FOR LEAVING / EXIT INTERVIEWS

- ☐ Review your store's Reasons for Leaving Report for the last 6/13 periods and identify the top three reasons for leaving. Are pay/benefits identified?
- ☐ Do exit Interview always take place when a member of staff leaves us?
- ☐ Track exit Interviews to show if codes 'N' or 'O' used to identify where people are leaving us for better pay and benefits.
- ☐ If these codes are used, can you identify who they are leaving us for?

STEERING WHEEL MEASURES

Review your store's most recent Viewpoint results. What are the scores for the following and how do they compare against your Group?

- ☐ % overall morale
- ☐ % satisfaction with pay
- ☐ % have had a review
- ☐ % have a PDP

Lack of training and development is often a reason people leave us. Include your store's Steering Wheel results for:

- ☐ training
- ☐ reviews

- ☐ Review how attendance has been tracking for the past 6/13 periods.
- ☐ Identify any issues within specific departments.
- ☐ Review PI reports for store and department performance against budget.

6 Case study B – A professional services firm

6.1 Introduction

Pay at organisation B is determined largely through external benchmarking against similar businesses. External pay data varies from region to region, and the company's pay rates reflect this. The difference between rates in the lowest paying areas and London could be up to 25 per cent, with the size of the difference being mostly related to the distance of the regional office from London and the South East.

6.2 Background

This professional services firm has a large number of staff located in many cities across the UK. In general, overall pay ranges reflect market area, location and business performance. Most employees have a first degree and many have a second degree or are studying towards or have acquired a professional qualification.

6.3 Pay structure

There are five levels of seniority in the organisation, director, senior manager, manager and two non-managerial levels, and pay is organised into a series of five broad bands. Market benchmarking survey data is used as part of the pay review process. This data will be appropriate to the market specialism and where applicable, region. Pay is reviewed generally once a year. Staff satisfaction with pay is scrutinised by means of staff surveys and other indicators, such as labour turnover will be considered.

Staff are eligible to participate in a discretionary bonus plan; bonus levels take into account both business performance and market practice.

6.4 Pay differentiation by location

Organisation B does not think of differentiating pay by location as a different activity from pay setting in general, so cannot identify the costs of 'geographical pay'. Instead, in most areas, location is and has been for many years a central aspect of pay benchmarking, and the objectives of geographical pay are the same as for pay in general. For similar skills and experience, people sitting next to each other may be paid different amounts, because they have different market specialisms.

When pay, including geographical pay, is set, the local cost of living is not a direct consideration although it is likely to have impacted market pay rates.

6.5 Decisions on pay differentiation

Overall decisions on pay are taken by the board, local leaders would determine how this is implemented within agreed principles. Pay decisions are communicated to staff face-to-face by local leaders and managers.

6.6 Effectiveness of pay differentiation

Organisation B continues to review its pay approach and evaluates this through staff satisfaction with their pay and the company's ability to recruit and retain staff.

6.7 Problems with pay differentiation

Organisation B has experienced no problems with its approach to geographical pay differentiation.

6.8 Effect of the loosening labour market

The changing labour market and the ability to recruit and retain staff on current pay levels will be considered alongside market benchmarking data to provide a full picture of the relevant labour market.

7 Case study C – A transport infrastructure company

7.1 Introduction

This company pays location allowances to all employees in inner London, outer London and the South East. External market data is a factor used to set pay for some groups and reflects the differential between London market pay rates and those for the rest of the country. Labour turnover has traditionally been low and has been unaffected by the economic climate. Pay for management and non-management staff is negotiated with recognised trade unions.

7.2 Background

Organisation C employs around 35,000 staff in a range of manual, clerical, administrative, technical and managerial roles at offices and depots throughout England, Scotland and Wales. Of the 35,000 employees, around 20,000 will have had no pre-entry qualifications although some will subsequently have studied for City and Guilds awards and/or received other on-the-job training. White collar workers have a range of qualifications, from GCSEs to postgraduate diplomas and professional qualifications. The company has brought together a number of other infrastructure companies over the years and there are a multitude of pay grading structures resulting from the TUPEing over of staff on different terms and conditions.

7.3 Basic pay policy

Pay for maintenance and operations staff at organisation C is determined by collective bargaining. Pay for technical staff and managers is set according to external market data and individual performance subject to pay negotiation. Although it would be helpful to tidy up and/or harmonise the dozens of existing arrangements, the company currently has other priorities. Progress has been made in recent years, with broad bands for some white collar staff.

The pay of senior managers is not covered by collective bargaining. Instead, it is set according to external market data, principally from Towers Watson, Hay Group and Aon Hewitt, although the latter is mostly used for senior executives. The company benchmarks roles against similar roles in similar organisations – FTSE 100 companies and other regulated quasi-governmental businesses. The data is used to provide a remuneration benchmark tool, which is supplied to HR Managers and business leaders to help inform individual pay determination. The tool sets out external median and upper and lower quartile data, together with similar internal data. Pay is targeted at market medians

7.4 Pay differentiation by location

Company C has two approaches to pay differentiation by location. It pays location allowances to staff to compensate them for the higher cost of living in London and the South East. The allowances were introduced many years ago and the basis on which they were originally calculated is unknown. They have subsequently been negotiated with the recognised trade unions and cost the organisation around £16 million per annum. Allowances are currently Inner London £2,400 (0-16 miles from Charing Cross); Outer London £1,390 (16-40 miles from Charing Cross); and £955 (South East), all unchanged since 2009.

Staff group	Inner London (0-16 miles Charing Cross) £pa	Outer London 16-40 miles from Charing Cross £pa	South East (M25 Corridor) £pa
Maintenance and operations	2,400	1,390	955
Junior technical roles, secretarial and administrative	2,400 in addition to salaries which include a 21% differential resulting from benchmarking using external market data	1,390 in addition to salaries which include a 5% differential resulting from benchmarking using external market data	955
Junior managers and more senior technical roles	2,400 in addition to salaries which include a 10% differential resulting from benchmarking using external market data	1,390 in addition to salaries which include a 5% differential resulting from benchmarking using external market data	933

Staff group	Inner London (0-16 miles Charing Cross) £pa	Outer London 16-40 miles from Charing Cross £pa	South East (M25 Corridor) £pa
The most senior roles	2,400 in addition to salaries which include a 5% differential resulting from benchmarking using external market data	1,390 in addition to salaries which include a 5% differential resulting from benchmarking using external market data	

There are no explicit allowances for other staff, instead, external market data used to inform pay decisions incorporates the differentials between London pay rates and those for the rest of the country as follow:

- a 5 per cent premium for the most senior roles working in central and outer London (up to 40 miles from Charing Cross);
- a 10 per cent premium for central London and 5 per cent for outer London for junior manager and more senior technical roles and
- a 21 per cent premium for central London and 5 per cent for outer London for more junior technical roles and secretarial and administrative staff.

These premia are not added by company C, they are embedded in the external market data, and may change from year to year as the external labour market changes.

7.5 Decisions on pay differentiation

Local allowances for those working in inner and outer London and the South East are decided upon as part of the negotiations with the trade unions. No other decisions on pay differentiation by locality are required since the data on which managerial and senior technical pay is based

already reflects the premium the external market is paying for work in inner and outer London. Actual pay rates in different geographical areas are based on a mix of market data, personal performance and negotiation with the recognised trade unions.

7.6 Role of local managers

Local senior managers are supplied with market pay rates for their direct reports, including lower quartile, median and upper quartile pay in London, the South East, and the rest of England, Scotland and Wales. They award pay increases based on the mix of individual performance, affordability and recognition with recognised trade unions. Local managers have no discretion over geographical pay.

7.7 Effectiveness of pay differentiation

The company is reasonably satisfied with its current arrangements for compensating staff in London and the South East for higher living costs. It has no strategy for changing allowances at the moment.

7.8 Problems with pay differentiation

In general, organisation C has had no problems with the allowances it pays for those working in London and the South East.

7.9 Effect of the loosening labour market

Labour turnover is very low at organisation C, and has not changed in recent years. Local allowances are set on the basis of cost compensation, however, so labour turnover, would have had no effect either way.

8 Case study D – Financial services

8.1 Introduction

Organisation D operates a system of London allowances based on postcode distance from Charing Cross. This current locational pay system at the financial services firm replaces legacy arrangements based on geographical hotspots. These arrangements were replaced in 2010 following takeover and integration. Any location allowance is rolled into basic salary and London allowance levels are benchmarked annually using relevant market data.

Overall staff turnover at the firm is 10.3 per cent. But the main recruitment and retention problems are all in contact centres, where turnover is 27 per cent.

8.2 Background

Organisation D currently employs some 25,000 staff. It has around 1,300 branches in the UK as well as eight contact centres. London allowances are received by all levels of employees.

8.3 Basic pay policy

The firm has centralised pay and progression arrangements and pay settlements are made annually through collective bargaining. The organisation pays market median basic rates to retail staff while variable pay is “aggressive” and based on performance – half of staff get a good bonus, the other half get nothing.

Location allowances are incorporated into basic pay rather than paid as a separate allowance, and are applied to the ‘market rate’. This means the organisation can keep its same pay approach, just with altered reference points for the London area. So, for example, if a job is benchmarked at £15,000 for the national rate, it will be benchmarked at £18,500 in central London and £17,000 in outer London. This means the system of individual pay rates with reference to a benchmarked market rate can be used everywhere, just with a different reference point.

This framework of rolling allowances into basic pay was carried over from a pre-integration legacy arrangement. There is a perceived benefit for staff, as basic pay is pensionable and used for bonus calculation, unlike a separate allowance. This means it usually works well for integration.

Salary ranges are benchmarked each year and salary reviews are carried out with input from and negotiations with unions. Pay levels are set centrally although if there are specific areas that need attention then the reward team liaise with relevant regional staff and address issues.

The current centralised pay policy – national ranges with London allowances, is particular to organisation D and other businesses merging with the company switch over to this model. Some of the pay arrangements in merged companies were complicated and expensive to maintain and monitor.

At one firm that came into the business for example, pay was very decentralised and negotiated locally, in branches. There were massive cost issues associated with these local pay negotiations and the result was often people doing similar jobs on very different rates of pay. And there were occasionally equal pay claims under the old system.

Now that pay for these sites is managed centrally the cost pressures have drastically reduced but there are other pressures. There are higher levels of turnover in areas of the business that historically received higher pay. This is the case in some of the contact centres, for example.

8.4 Pay differentiation by location

The firm has a national pay rate with extra allowances for London staff rolled into salary ranges. London allowances are based on postcode distance from Charing Cross: national – 37 miles + from Charing Cross; fringe - 22-36.99 miles from Charing Cross; outer – 7-21.99 miles; inner – 0-6.99 miles. At present, some 6,500 employees receive location supplements.

Region	Criteria (miles from Charing Cross)	Amount £pa
National	37+	N/A
Fringe	22-36.99	1,000
Outer	7-21.99	2,000
Inner	0-6.99	3,500

The organisation hasn't signed up to the London Living Wage, saying it prefers a 'purely market-based approach'. The organisation benchmarks roles on a national basis (using Towers Watson) then takes the median figure for the role and uses it as a midpoint of a range. Like most financial firms, it operates these salary ranges with reference to a 'market rate', so

individuals can be at '95% of market rate' or 105%. Organisation D bases pay entirely on 'market intelligence' rather than cost of living.

8.5 Decisions on pay differentiation

Pay decisions are now centralised whereas previously, in the legacy arrangements of acquired businesses they were carried out locally. London allowances are benchmarked using comparable data from financial services pay data. There are no other national payments, however, if there are any areas with recruitment and retention problems then local managers can make a business case to recruit at a higher level on the pay band. So in effect there is still some geographical flexibility within the national structure.

8.6 Effectiveness of pay differentiation

The current system is effective, it is easy to administer and easy to control. There is a huge difference to how things used to be under legacy arrangements, which were, at times, 'a disaster'. That said there have been some consequences of removing local pay arrangements. In some contact centres in the north of England, for example, the removal of geographically-determined pay has resulted in recruitment and retention problems as salaries in some areas are not as competitive as they once were with the local labour market.

8.7 Problems with pay differentiation

This is apparent in the problem of staff turnover at some of the contact centres outside London. High turnover levels, of up to 27 per cent, appear to be based on local competition from similar types of employers who have lower overheads. Most contact centres are in the north of England, e.g. in Sheffield, Bootle and Bradford (and Belfast). In some areas the main competition is telephone banking contact centres, which require some of the same skills from its employees but without the overhead costs of also running local branches.

Before integration, there were defined hotspot areas and cities, and pay in these locations was calculated by working back from the London rate. For example, wages in a particular city might be paid at the London rate minus 10 per cent. This was an extended and reversed version of the company's current practice, which is to take the national rate and add a premium for London.

Prior to integration, the company had started to get local pressure from union representatives concerning local pay premiums and living wages in particular regions. Integration led to the closure of a number of branches, which as a result reversed the pressure on pay as unions changed focus. Now, with much (though not all) of the integration process complete, some upward pressure is starting to build again in particular regions. Where there are problems, such as with the issue of call centres, for example, organisation D has flexibility to recruit higher up a pay scale, if market data shows there is a need. For example, if the typical salary range is 80-120 per cent of the benchmarked market rate, they may decide, for a particular site with recruitment and retention problems, not to pay anyone less than 90 per cent of the market rate. This therefore provides local flexibility in a very few exceptional circumstances to troubleshoot, rather than a general rule for localised pay. The organisation has had no equal pay claims since integration, and only a few historic ones related to the hotspot system.

8.8 Effect of the loosening labour market

Organisation D in its current state is the result of a series of mergers and acquisitions in recent years. As such, part of its focus is on reducing branches and staffing levels to avoid duplication of effort. Therefore a loosening labour market is not really a concern. One area where a loosening labour market has occurred is in contact centres outside London where there have been some recruitment and retention issues in a few, very specific instances. It is probable that these problems would have been greater had the labour market been tighter.

More generally, there have been pressures but these have concerned the integration process. The organisation has in effect removed local pay arrangements which were costly and difficult to manage, and replaced these arrangements with a national pay rate. Though there are some issues in very specific areas there is a little flexibility within the national pay structure to deal with this.

9 Case study E – A financial services company

9.1 Introduction

Organisation E pays territorial allowances to around 14,500 staff working in central London and hot spots and has a separate, higher pay scale for some 6,700 administrative and clerical branch staff in London and other urban conurbations. Allowances have not changed for 'at least five years', although a third locality-based pay scale for branch staff was amalgamated with another so that there are now only two scales – national, and London and large towns.

9.2 Background

This global financial services company has 44,000 UK employees out of a worldwide total of 300,000. It has a London headquarters, call centres in the Home Counties, the North of England, Wales and Scotland and retail branches in almost every UK town and city. At least half the workforce is educated to degree level and many staff have a postgraduate vocational qualification. Labour turnover, which has been almost static since 2008, is about 6 per cent across the organisation and 10-12 per cent in call centres.

9.3 Basic pay policy

Organisation E sets pay over the long term and aims for stability, consistency, fairness and simplicity in its pay arrangements. And although it wants to encourage ownership of pay by line managers, as a large organisation it considers it vital to control pay setting from the centre. It does not want to have to deal with the fallout from possibly idiosyncratic and inconsistent decisions at local level. Pay for clerical and administrative staff is negotiated with a recognised trade union while the company consults with a non-union management representative body for that population.

There are three pay structures, one for call centre staff below managerial level and two for branch clerical and administrative staff. Managerial pay is entirely discretionary; there are no pay scales or broad bands. Although call centres are located all over the UK, staff are paid national rates and there is no variation in pay by location. The two pay structures for branch staff are differentiated by location. One structure is for staff in London and other large conurbations, the other is for staff working everywhere else.

Organisation E aims to pay median rates. Pay structures for non-management staff consist of benchmarked medians for roles, with staff being paid between 70 per cent and 105 per cent of the median rate. Medians are set with reference to Towers Watson's regional market medians and data from the Annual Survey of Hours and Earnings (ASHE) to establish trends in pay increases and regional pay differentials. Annual increases for non-management staff in 2011 were awarded according to each individual's position relative to the median and their individual performance rating. Anyone earning more than 105 per cent of the median received an unconsolidated cash payment rather than a salary increase.

National market medians for managers are also determined on the basis of Towers Watson and ASHE data. Line managers set individuals' pay according to their performance, how their pay relates to that of their peers, and their pay relative to the market median.

All staff are also eligible for bonuses which are awarded according to individual and company performance.

9.4 Pay differentiation by location

Organisation E had some recruitment and retention problems prior to 2008 but has had few problems since. In any case, the company says, it is important to think about the overall employee proposition, which is not just about pay. It has geographically-differentiated pay in the form of separate pay structures for branch staff by location, and territorial allowances for all levels of staff. Apart from the territorial allowances, all managers except around 200 executives are paid national rates, as are call centre staff. Branch administrative and clerical staff are paid on one of two pay scales, determined by location. There were originally three pay bands, one each for national rates, hot spots, and London and large conurbations. But the bottom band was abolished in 2012. Staff on this band tended to be long-serving and female and at the top of the pay scale, so not receiving pay increases. The two bands are now London and large conurbations, and national.

Towers Watson regional data is used both to establish which of the two pay scales branches should be using, and also the differential between the two scales. These arrangements are reviewed every year but have not changed since 2008. The differential is currently around 6 per cent.

The three territorial allowances paid to staff working in particular locations, on top of the pay scale differential, are £4,000 in central London, £2,000 in hot spots such as Manchester and Birmingham and £1,000 in hot spots such as Worthing, which has a number of other financial services employers located nearby. The payments have been set at the same level since 2007. This is partly because the company wants pay increases to result solely from individual performance, not through increased territorial allowances.

9.5 Decisions on pay differentiation

Towers Watson regional market pay data and ASHE data are used to indicate appropriate territorial allowances and the two location-based pay scales for clerical and administrative staff, while changes in the Consumer Prices Index, labour turnover and staff satisfaction with pay are also taken into account. Local managers would decide whether or not to address any problems with pay in a particular location, as part of the annual pay review process. In practice there is little differentiation between individual occupations or locations outside the existing structures other than that determined by the market data received by the organisation, which is used to set role medians. And even if problems were identified, the company would only make changes as part of the annual review process, not some way through the year. Local managers are provided with guidelines on the pay setting process, but there is nothing specific on local pay and no format for making a case for it. There is no local discretion. The process would probably be that the manager would raise the issue with the local HR business partner, who would in turn raise it with central HR and the regional manager.

9.6 Effectiveness of pay differentiation

Organisation E evaluates the effectiveness of its approach to local pay differentiation by looking at management information such as labour turnover, position in the labour market, local recruitment and retentions problems and staff satisfaction with pay. It would introduce the same system again tomorrow, and comments that 'If you have 40,000 employees then you need a structure or it becomes a free for all. You don't have a direct line of sight to what's going on locally and there might be local inconsistencies.'

Employees are very aware of local pay differentiation. Line managers discuss pay and performance with each individual every year. The company's pay structures are underpinned by job evaluation and it says that if employees believe that the overall grading structure is fair then they will think their own pay is fair. 'There needs to be appropriate differentiation between

pay for individuals, but it should be on the basis of performance, not location', the company says.

9.7 Problems with pay differentiation

There are few problems with organisation E's approach to local pay. There can be potential issues, it says, where there are two branches close together but recruitment and retention difficulties in only one. The company would look at the relative territorial allowances and consider adjusting them, but there is no guarantee that any action would be taken. Younger staff, who are more mobile and more concerned with pay may be moving between branches to secure a higher location allowance, but this is not considered a problem. Conversely, there could be a problem with staff refusing promotions which result in a loss of territorial allowance, although in this case the allowance is protected on a tapering basis for three years. Where a whole office, such as a call centre, is moved, the allowance would also be protected over three years.

9.8 Effect of the loosening labour market

To date the company has not reacted to the loosening of the labour market by withdrawing location payments though it says it could do so. At the moment it intends to go on paying the allowances because it wants stability and takes a long term view. It would only do so on the basis of labour market intelligence, labour turnover and a budgetary analysis of the resulting savings. A paper would be put forward by HR to senior managers and the issue would be discussed at and decided upon at a very high level in the organisation.

10 Case study F – A distribution company

10.1 Introduction

This organisation differentiates pay on the basis of location in two ways. Firstly, the company's pay scales include inner and outer London and national rates. On top of this, there are two sets of recruitment and retention allowances for the most populous operational grades. The first set, comprised of two allowances, was introduced in 1989 and covers locations as far north as the Midlands. The second, introduced following a re-evaluation of the recruitment and retention situation in 2003/04, is comprised of five allowances, but is paid in fewer locations, concentrated mainly in West London, the South East, and the commuter towns. There has been no further re-evaluation since 2003/04, although it is an issue open to future collective bargaining.

Other recruitment and retention allowances are also in place for different grades of employee, up to middle manager level. These are based on a variety of factors, mainly to do with the various results of pay bargaining for different groups.

Pay for employees up to middle manager level is negotiated nationally with trade unions, while pay for senior managers is individualised.

Staff turnover is not currently seen as a problem, with voluntary resignation turnover running at around 1.3% for full-time and around 9% for part-time staff. Restructuring means that the company is looking to reduce headcount rather than increase it, so recruitment and retention are not currently a problem.

10.2 Background

Organisation F employs around 150,000 people in operational, logistics, delivery, white-collar and managerial roles at locations across the UK, with 129,000 of these working in the part of the business covered by the main system of recruitment and retention allowances. Of these, 91,000 are full-time and 37,400 are part-time employees. There is an established national bargaining structure, with a high level of union involvement.

Recruitment and retention allowances and inner and outer London salaries apply up to middle manager level, with pay for senior managers (£40-45k plus) determined individually and benchmarked against central London, or non-central London only.

10.3 Basic pay policy

Pay reviews for non-management grades take place annually in April, with managers' pay reviews taking place annually in July. Pay up to middle manager level is negotiated nationally with trade unions.

Operational and operational support staff are paid weekly, while clerical, secretarial and engineering staff are salaried. For operational and admin staff, there are recruitment rates, rates payable after 6 months and maximum rates in each grade. Engineers have a six point incremental scale. For each grade there are separate rates payable nationally and in inner and outer London.

Senior managers are on individual salaries. These are benchmarked against central London or the rest of the UK.

The company sets basic pay by benchmarking against a variety of sources, including Hay, IDSPay, and attendance at a distribution employers' forum.

Example pay rates effective from 1 April 2012 are as follows:

Pay structure at 1 April 2012 main operational grade			
	National £pw	Outer London £pw	Inner London £pw
Age 16	223.26	264.79	280.06
Age 17	260.47	308.92	326.73
Adult recruit (age 18)	334.89	397.19	420.08
Six months' service	353.50	419.25	443.42
Maximum (after one year's service)	372.10	441.32	466.76

Pay structure at 1 April 2012 – main administrative and secretarial grades (see separate file)			
	National £pa	Outer London £pa	Inner London £pa
Administrator			
Age 16	13,712	15,723	16,599
Age 17	15,996	18,324	19,345
Adult recruit	18,948	22,021	23,388
Six months' service	19,596	22,771	24,185
Maximum	22,853	26,130	27,589
Secretary			
Age 16	13,937	15,803	16,731
Age 17	16,261	18,437	19,518
Adult recruit	20,019	23,046	24,542
Six months' service	20,331	23,395	24,917
Maximum	23,230	26,340	27,884

Pay structure at 1 April 2012 – main engineering grade (see below)			
	National £pa	Outer London £pa	Inner London £pa
Engineering grades 1-8	24,710 to 35,840	27,949 to 39,080	29,400 to 40,532

A history of large scale re-organisation and re-structuring, coupled with established trade union pay bargaining, has led to a system complicated by large numbers of legacy payments and allowances for different groups, with one of the sets of recruitment and retention allowances covered by this study falling into this category.

10.4 Pay differentiation by location – current

There are two main aspects to pay differentiation on the basis of location at the company. The first is the inner and outer London rates mentioned above. Inner London is defined as within 4

miles of Charing Cross, while outer London covers locations that fall within a historical operational area. London weighting is worth varying amounts dependent on grade.

The second aspect is a series of 'old' and 'new' recruitment and retention supplements (see history section below for explanation of how these were established). These are paid as a non-pensionable addition to basic pay at the following levels:

Recruitment and retention allowances, main operational grades at 1 April 2011, £pw

Old payment (original locations)	Old payment (later locations)	New payment (high problem areas)	New payment (medium problem areas outside London)	New payment (medium problem areas within London)	New payment (mild problem areas outside London)	New payment (mild problem areas within London)
20	10	35	27.50	20	10	5
The 'new' payments for problem areas were introduced in April 2004. They are discussed in more detail in the table below.						

In total, recruitment and retention supplements are paid to an estimated 10,000 employees, at an annual cost of around £25 million, though this figure is slowly falling due to headcount reductions as a result of restructuring. The administration costs are minimal, amounting just to payroll costs, as the locations in which supplements are paid are not reviewed frequently. All that is necessary is for a code to be assigned to the payroll for new starters in locations receiving a supplement. This will automatically generate the addition to pay. The company would like to undertake a detailed review, subject to negotiation with the union.

10.5 Pay differentiation by location - history

Up to the late 1980s, the only locational addition to pay at the company was inner and outer London weighting. By the end of the 1980's, the company was experiencing serious recruitment and retention difficulties, with turnover running at between 40 and 60 per cent in some parts of London.

In 1989 the company and union agreed on the introduction of a system of recruitment and retention supplements, with payments ranging from £6 to £15. Outside of London, where no existing allowances were paid, the payments were highest, at £15 a week. In inner London the

rate was £6 on top of the existing £28 London weighting, and in outer London the premium was £10 on top of the existing £15 London weighting. Outside of London, payments were confined solely to the South and West of London, with the exception of a wide corridor running up the M11 from London to Cambridge. From September 1989 the scheme was extended to cover some areas in the south Midlands and East Anglia, paid at a lower rate. The supplements introduced under this scheme are the 'old' supplements.

In October 1993, separate London weighting was incorporated into basic pay, providing national, inner and outer London rates for the main operational grades. (From Jan 1995 for secretaries and engineers).

By 1996, the four levels of premium were £13.87 in inner London, £16.31 in outer London, £20 in the original areas outside London and £10 in the areas added in September 1989.

Recruitment and retention payments in inner and outer London were consolidated into basic pay from 6 October 2003, leaving two rates of recruitment and retention supplement at £20 in the original locations and £10 in the areas added later, and slightly further away from London.

Throughout 2003/04 there was a dispute over London weighting, with an agreement reached in 2004 that provided flat rate increases to London weighting, plus a guarantee that this would rise in line with annual pay settlements.

On 5 April 2004, the 'new' recruitment and retention allowances were introduced, as follows:

Recruitment and retention allowance pay area	Payment £pw	Areas covered e.g.
Red pay area	35	Oxford, Hemel Hempstead, Reading, Guildford, Redhill, Winchester, Sevenoaks
Orange pay area (outside London)	27.50	Cambridge, Stevenage, Slough, Milton Keynes
Orange pay area (within the London pay area)	10	St Albans, Watford, Harrow, Kingston
Yellow pay area (outside London)	20	Salisbury, Chichester, Portsmouth, Worthing, Ashford, Harlow & Chelmsford
Yellow pay area (within the London pay area)	5	Bromley, Sutton, Twickenham, Uxbridge

These have since sat alongside the remaining two rates (outside of London) from the 'old' 1989 scheme. In locations which received no increase in recruitment and retention supplement from April 2004, or were no longer deemed eligible, all employees, including new starters, continue to be paid the existing level of the recruitment and retention payment. The rates of recruitment and retention supplement have not been increased since this time.

10.6 Decisions on pay differentiation

Decisions on pay differentiation are made through national negotiations between the company and trade unions. There is broad acceptance of this among employees, who are accustomed to having pay and conditions negotiated nationally. Negotiations on recruitment and retention supplements happen infrequently, having taken place in 1989 and 2003/04 only.

The old recruitment and retention supplements in 1989 were paid in locations where unemployment was below 5 per cent and labour turnover above 15 per cent at the scheme launch in 1989. The re-assessment in 2003/04 was based 50 per cent on internal wastage and 10 per cent on full-time male average earnings in the broad postcode area. Some 40% of the assessment was based on other factors, including local unemployment.

Removing supplements from workplaces where they were no longer deemed necessary has proved difficult. The company has not been able to negotiate this with the union.

10.7 Effectiveness of pay differentiation

There has not been ongoing analysis of location-based pay in a period of tight labour markets, so it is difficult to say how effective the payments have been. The problems experienced in 1989 and again in 03/04 have seemed to have gone away, but this is partly due to reorganisation, with the company looking to reduce rather than increase headcount. There are still a few 'hot spots' but the company is dealing with this through redeployment of existing staff, rather than recruitment. Where there is a problem, this tends to be a retention rather than a recruitment issue. This raises questions about job content as well as just pay. Since 2008, there has been an increase in the pace of change within the business, and there are now no major recruitment and retention problems.

10.8 Problems with pay differentiation

Because geographically-determined pay is collectively bargained, the pay structure hasn't really kept up with this change, and the company is now paying the 'old' recruitment and retention allowances in areas where it does not need to be. It has not been able to negotiate the removal of these with the union, even on a marked time basis. Although in the 1990s this 'old' system may have provided value for money it is more questionable in the current economic and business climate. Given the choice, the company would not see local pay supplements as a reward priority.

There are some cliff edge effects, for example Coventry receives a supplement but Birmingham does not. However the rates of supplement are low enough that this does not lead to poaching of staff from one location to the other.

In terms of relocation, this does not tend to be from one existing location to another but from a location that is to be closed either to a new one or to an existing one that will remain open. Although recruitment and retention supplements will be a factor in negotiations, employees tend to be more focussed on other aspects of relocation. If employees are moved from an area that qualifies to one that doesn't, the supplement continues to be paid on a 'marked time' basis.

Negotiations with the union over changes to the system can be lengthy and difficult.

10.9 Effect of the loosening labour market

In the latest period, restructuring has been the focus, rather than recruitment and retention. The company has noticed that turnover is lower – possibly as a result of a slacker labour market, meaning that people are less willing to leave their jobs. The number of people voluntarily leaving the organisation has fallen from around 300 people to around 150 people a week.

11 Case study G – A research-based manufacturer

11.1 Introduction

This organisation pays national rates, and allowances based on external market data to those working in its London office. There are no territorial allowances for those working in the Home Counties, and thus no difference between pay levels there and those at its other location in the North of England. Labour turnover is low and at any time is constrained more by the availability of specialist skills than the overall state of the labour markets. Overall pay levels are set either with reference to external market data or legacy pay rates for the unionised population; pay budgets are set for the UK as a whole. There are no discretionary location payments.

11.2 Background

This is a global company employing around 7,000 people in the UK and some 60,000 worldwide. In the UK, there are three main sites; the headquarters in London, the sales function in the Home Counties and the R&D/manufacturing site in the North of England. The workforce includes scientists, sales staff, corporate employees and manufacturing staff. Between a third and a half of employees are graduates or post graduates, with some roles comparable with NHS jobs, while manufacturing staff generally have lower level or no qualifications. Voluntary labour turnover has been stable at under 5 per cent for many years, but does vary between functions.

11.3 Basic pay policy

Pay budgets are set in line with external market data and affordability; staff satisfaction with pay is measured in annual surveys. Basic pay for all staff is based around the market median and is determined separately for the unionised manufacturing employees and the rest of the workforce. There are across-the-board negotiated pay increases for the unionised manufacturing staff while non-unionised staff receive increases based on a matrix consisting of the individual's position relative to the market data and their performance – that is, their performance over the current and the two previous years. Internal equity and budget are also taken into account. The trend in pay setting at organisation G is to make it a leaner, simpler process whilst maintaining the company's ability to recruit and retain. The number of surveys used for pay benchmarking has fallen from around 20 a few years to two or three main sources for most roles. The number of roles being benchmarked is also being reduced, as detailed benchmarking of different roles consistently identifies similar market medians.

Unionised employees are on introductory and established spot rates, with pay increases negotiated regularly with the recognised trade unions and covering one or multi-year periods. The negotiations are informed by market data, principally from Alan Jones and an industry-specific salary survey, together with the state of the organisation's trading environment and how it is faring against its competitors. The company researches pay settlement trends, using data from a number of sources, including IDS and the EEF. All employees, including unionised, are eligible to receive annual performance related bonuses, based on individual and company performance. Current pay rates set a floor under negotiations for the following year.

The roles of scientists, corporate/professional and sales staff not covered by the collective agreement are grouped into job families, underpinned by a job classification system. Each job family has a number of levels, Market data is produced for every role in the job families, using Towers Watson and industry-specific surveys. Pay ranges for each role are set at between 80 per cent and 120 per cent of the market median. When it comes to the annual review, managers can give more in one area, if there are a large number of good performers who are paid less than the market, providing another area receives less (that is, managers have to balance budgets). Annual pay increase decisions are normally made by the line manager and follow an approval process. Central control of the pay budget is exerted by the need to remain within an overall budget figure, with a single figure set for pay increases for the non-unionised workforce throughout the UK. Annual increases for the unionised workforce may be a different figure, depending on the details of the negotiation.

Bonuses are benchmarked against the market; bonus ranges are dependent on grade, with each grade having a bonus range (for example 0-20 per cent) and a target (for example, 10 per cent) determined by the market. The company creates a bonus pot based on targets and company performance and individuals receive a proportion of this pot based on their personal achievements. Total bonuses cannot exceed the bonus pot so if there is a disproportionate number of high performers this will impact their average bonus and also the bonuses of lower performers.

11.4 Pay differentiation by location

Organisation G has offices in central London and the Home Counties, but only pays an allowance in central London. Pay rates at offices in both the Home Counties offices and the

North are based on national pay rates. In central London, staff receive the better of an allowance or a fixed percentage of salary, according to grade. These figures, which are the differentials between London and national rates, arise from the market data used to establish a market median for each role. The differential is greatest for the most junior staff. For the most senior staff the differential approaches zero. There are no discretionary additional location payments.

The company has not experienced general recruitment and retention problems for many years. The occasional difficulties it has filling specific roles result from an overall shortage of people with the requisite skills rather the heating up or cooling down of the labour market. It recruits in an international labour market for its top scientists, the national labour market for senior staff, and regional or local labour markets for everyone else.

11.5 Decisions on pay differentiation

Pay decisions during the annual reward round are signed off by senior management. London allowances are determined centrally. The company says 'we want managers to run their own businesses and be accountable', so line managers make most decisions about the pay of the non-unionised staff who report to them, and these are approved by their own manager. Line managers receive guidance, a matrix setting out recommended annual reviews for individuals in line with their performance and position relative to the market data, and, most importantly, a budget. They must put forward a case if they wish to exceed the budget, which may happen if they have good performers paid below the range. Their manager will then determine other direct reports to spend less so that the overall budget is not exceeded. Increases outside the annual pay review are also controlled by the line manager, their manager, and overall budgets.

If a manager has problems recruiting at the salary suggested by the market data, there may be a challenge to the data which may be reviewed, however, managers have considerable flexibility, subject to budget

11.6 Effectiveness of pay differentiation

Organisation G says that the absence of recruitment and retention problems and low labour turnover means that it will not be making changes to its approach in the short to medium term.

11.7 Problems with pay differentiation

Recruitment and retention problems, uncompetitive pay ranges, or company restructures resulting in new or changed jobs could present challenges to the existing system. But to date, none of these have disturbed the current arrangements. Employees have a one-to-one meeting with their line manager to discuss their performance rating and their annual pay award, and there is good understanding of the way in which pay is determined according to external market data. London allowances are not controversial. The company carries out equal pay audits to check that its approach to pay differentiation does not cause any issues. It is not aware of any problems with staff seeking to move from its Home Counties office to its London head office to obtain a London allowance, or being reluctant to move the other way if offered a promotion.

11.8 Effect of the loosening labour market

Organisation G is not aware of any obvious loosening of its relevant labour markets. As its London allowances are based on external market data, it says that it would be relatively easy to reduce them or even remove them if the market data and its labour turnover figures supported such a move. But it would approach such a project with caution and says that it 'does not want market pay going up and down' all the time, and does not review the allowances each year.

12 Case study H – A telecommunications company

12.1 Introduction

Organisation H is a large national organisation with many employee groups, from engineers to call centre staff, to HR, finance and general administration. The company has a national pay framework with London allowances covering inner and outer London. The current system of cost of living pay differentiation for London has been in place since the 1950s. On average, turnover at the organisation is running at 8.5 per cent and the company is not experiencing any recruitment and retention problems.

12.2 Background

Organisation H currently employs around 80,000 staff across all UK regions. London allowances are provided to around 9,000 non-management staff only, and cover inner London areas, 0-4 miles from Charing X and outer London, 4-18 miles.

12.3 Basic pay policy

The organisation has centralised all pay and progression arrangements and pay settlements are made annually via collective bargaining. London allowances are separate from pay bargaining and are not linked to pay increases. They are negotiated separately and are therefore not necessarily increased in line with pay. There are a number of factors taken into account when reviewing pay, such as company performance, economic environment, RPI, market settlements, etc.

12.4 Pay differentiation by location

The firm has a national pay rate with London allowances based on distance from Central London. Payments are £3,600 per annum for employees working between 0 and 4 miles from the centre and £1,600 to employees working within 4 to 18 miles of the centre. The organisation benchmarks the London allowances annually using various surveys for example. London Living wage, Towers Watson and other studies including IDS data. The rationale for the London allowances is, in the main, to reflect higher living costs including housing and travel.

12.5 Decisions on pay differentiation

London allowances are a contractual right at the firm and as such they are negotiated annually each year, but separately from pay negotiations. This means that increases in basic pay are not necessarily combined with increases in London allowances.

12.6 Effectiveness of pay differentiation

The system is effective and easy to administer. Payments are paid as a fixed allowance in addition to basic salary. Whilst administering pay generally is costly, once set up the cost of administering of the fixed allowance is minimal and much less than administering geographically-differentiated pay that covered all UK regions.

12.7 Problems with pay differentiation

The company only has London Allowances, and there are no real issues with these. Employees, in general, think that they are fair. They recognise that there is a cost-of-living factor associated with London. If the company decided to move more fully into geographically-determined pay then issues may arise. Given the national spread of its workforce the organisation considers that difficulties could stem from portioning up the country into different regions. It is also the view that there would be changes in equal pay legislation to consider and companies would have to be very careful about how differences are justified in one region and not another and other issues arising from a number of separate negotiations including time spent and employee morale.

With benchmarking generally the company recognises that it has to be careful. The organisation's aim is to remain an employer of choice – and therefore wants to attract a certain calibre of employee. It does therefore look at national rates to ensure they are paying competitively and if there was a specific recruitment and retention reason to look at a region then it would be investigated but to date it is not something that has arisen. The company acknowledges that it is an issue that does come up now and again but has not been taken on board as any value may be offset by other problems and additional costs.

Analysis of market data for the relevant employee groups the company wishes to attract shows that there is not a huge difference in pay rates in the UK regions outside of London and the South East.

The organisation questions the gain to be had, in terms of a return on all the investment required for geographically-determined pay, when actual differences are probably quite slight. Benchmarking comparisons are not straightforward – there is, for the firm, the question of whether businesses in a particular benchmarking sample in a particular region are doing the same job or require the same skill-sets and skill levels or are delivering the same quality of service.

12.8 Effect of the loosening labour market

Organisation H has detected no major effects associated with a loosening of the labour market other than an increase in the number of applications for vacancies. As London allowances are based on cost-of-living supplements there would be no justification for removing them in response to a loosening of the labour market as cost of living factors remain.

13 Case study I – A retailer

13.1 Introduction

Until 2011, organisation I operated a zonal pay structure for retail staff and managers comprised of four pay zones. In 2011, the company removed the second lowest pay zone, covering larger cities and small South East towns, meaning that additions to basic pay on the basis of location would henceforth be made in central and outer London only. Although labour turnover is running at 39.5 per cent, the company reports few recruitment and retention issues, with thousands of applicants per job. A jobs website introduced a few years ago, together with the general state of the labour market, have eased recruitment and retention further.

13.2 Background

Organisation I is a national retailer, with a head office, a call centre and in-house distribution. It employs around 50,000 staff in total, the bulk of whom are retail staff. The second largest group is distribution workers, followed by retail store managers, head office staff and call centre staff. This case study focuses on retail staff and retail managers, as these are the main groups where location-based pay is an issue.

Pay for head office staff and call centre staff does not vary by location, as they are based at just one place. Pay for distribution staff varies only in the case of one location – Hemel Hempstead – where an 11 per cent weighting is applied to basic pay.

13.3 Basic pay policy

Pay is reviewed annually, in October for retail staff and in February for head office, distribution and call centre staff and retail managers. The company does not recognise a trade union for pay bargaining.

Until 2011, organisation I operated a zonal pay structure comprised of four zones for both retail staff and managers, as below. Before 2007, a higher rate was paid to new starters in zone 2 than zone 1. From 2007 onwards, starter rates in the two zones have been the same, as a result of pressure from the National Minimum Wage.

Pay for retail managers was also based on the same four location-based zones until 2011, though it too varied according to store turnover, and, as with sales assistants, competency level.

From October 2011, the company removed location-based pay for retail staff and managers outside of London.

13.4 Pay differentiation by location

Until 2011, pay zones were organised as below, with higher basic pay in zones 2 to 4:

Organisation I pay structure at 1 October 2010 – retail staff				
Sales assistants	Zone 1 £ph	Zone 2 £ph	Zone 3 £ph	Zone 4 £ph
Starter	5.93	5.93	6.27	7.26
Established	6.10	6.34	6.98	7.52
Organisation I pay structure at 1 February 2010 – retail managers				
Level 1 (probationary to competent)*	Zone 1 £pa	Zone 2 £pa	Zone 3 £pa	Zone 4 £pa
5 – sales turnover less than £1.41m	17,878 to 18,883	18,769 to 19,827	20,645 to 21,809	21,682 to 22,899
4 – sales turnover £1.42-£2.41m	20,391 to 21,412	21,414 to 22,485	23,551 to 24,730	24,730 to 25,961
3 – sales turnover £2.42-£4.19m	22,941 to 24,088	24,089 to 25,296	26,495 to 27,821	27,821 to 29,209
2 – sales turnover £4.20-£8.02m	25,233 to 26,495	26,495 to 27,821	29,147 to 30,601	30,601 to 32,129
1 – sales turnover £8.03-£12.92m	27,876 to 29,619	29,271 to 31,101	32,198 to 34,209	33,809 to 35,921
1a – sales turnover £12.93-£19.49m	29,772 to 31,631	31,261 to 33,216	34,387 to 36,536	36,105 to 38,365
Super – sales turnover £19.50m+	-	35,058 to 37,263	37,479 to 40,296	39,354 to 42,845

*Pay rates for level 2 store managers (experienced to excellent) not shown

The locations corresponding to the various pay zones were as follows:

Organisation I pay zones		
Zone 1	National	e.g. Burnley, Crewe, Dundee, Eastbourne, Hull, Kirkcaldy, Lincoln, Northampton
Zone 2	Larger cities and small South East towns	e.g. Aberdeen, Belfast, Birmingham, Cardiff, Edinburgh, Glasgow, Leeds, Manchester, Sheffield, York
Zone 3	Outer London and large South East towns	e.g. Enfield, Gatwick, Kingston, Orpington, Staines, Thurrock, Uxbridge, Wandsworth
Zone 4	Central London	e.g. Bond Street, Covent Garden, Holborn, Marble Arch, Kensington, Oxford Street, Regent Street

As part of the 2011 pay review, organisation I removed pay zone 2, covering larger cities and smaller South East towns, moving to a structure based on three zones, as below, with premium rates covering outer and central London only. The pay rates applicable in pay zone 1 are now also applicable in the locations previously covered by pay zone 2, though this applied to new starters only, so no existing staff saw a reduction in pay.

Organisation I pay structure at 1 October 2011 – retail staff			
Sales assistants	Standard £ph	Outer London £ph	Central London £ph
Starter	6.08	6.43	7.45
Established	6.25	7.16	7.71
Organisation I pay structure at 1 February 2011 – retail managers			
Level 1 (probationary to competent)	Standard £pa	Outer London £pa	Central London £pa
5 – sales turnover less than £1.41 million	18,096 to 19,110	20,893 to 22,071	21,942 to 23,174
4 – sales turnover £1.42-£2.41 million	20,636 to 21,669	23,834 to 25,027	25,027 to 26,273
3 – sales turnover £2.42-£4.19 million	23,216 to 24,377	26,813 to 28,155	28,155 to 29,560
2 – sales turnover £4.20-£8.02 million	25,536 to 26,813	29,497 to 30,968	30,968 to 32,515
1 – sales turnover £8.03-£12.92 million	28,211 to 29,974	32,584 to 34,620	34,215 to 36,352
1a – sales turnover £12.93-£19.49 million	30,129 to 32,011	34,387 to 36,974	36,538 to 38,825
Super – sales turnover £19.50 million +	-	37,929 to 40,780	39,826 to 43,359

13.5 Decisions on pay differentiation

Decisions on increasing pay in particular locations used to begin with pressure from store managers. Locations would be reviewed annually, and if a store manager highlighted recruitment and retention problems, and wished to offer higher rates, they would be asked to make a business case for this, to include names of and rates paid at nearby retailers. They would also be asked to cost locally a 'basket of goods' to measure the local cost of living. The reward department would also check what competitors pay in the area concerned and the final decision would be made by senior managers.

While pressure to raise rates based on location under the old system came in the first instance from local managers, with senior managers having the final say, the decision to remove location-based pay outside of London in 2011 was made entirely by senior managers, based on market trends and cost-saving.

Organisation I is part of a retail pay forum, where pay policy decisions are discussed among various high-street retailers and also uses external resources, such as IDS publications, to follow market trends.

13.6 Effectiveness of pay differentiation

The zonal system was not monitored in a concrete way, but was more about making sure the organisation was competitive and able to attract the best candidates in a given location. The checks in place (on local cost of living, benchmarking etc) were thorough enough for the company to be able to say that it wasn't just throwing money at the problem.

The zonal system worked and managers had a process for getting stores uplifted, with robust checks from HR.

13.7 Problems with pay differentiation

Where zonal pay didn't work was that for a long time pay just went up and up and there was no motivation for store managers to tell HR if they felt they no longer needed to pay the higher rate to recruit.

Apart from that, the company did not have many problems with zonal pay. It did not have locations close to each other (in the same city) paying different rates, so poaching was not a problem. But decisions were more postcode-based than region-based, so Bolton for example would not have received a premium just because it was in the same region as Manchester, where premiums were paid. If Bolton had received a premium, this would have been the result of an individual assessment.

13.8 Effect of the loosening labour market

The recession made the company more stringent. It tried to limit pay and keep jobs rather than allowing pay to continue to go up and then having to cut jobs. That way it has retained staff, having managed them through the recession, and feels it will be in a better position for when things pick up.

Organisation I's pay zones had been in place for many years. Looking at what the company's competitors were doing, it realised it had an opportunity to re-organise. The company started

looking at particular areas in 2011 and was finding 'this could come down, this could come down' and eventually realised that allowances need only be paid in three zones.

The company kept location payments in inner and outer London because the cost of living is still higher, and also because although it might still have been able to attract candidates if it reduced London rates to the level of the minimum wage, it felt that it might not have been able to attract the calibre of candidates it would wish to employ. The fact that the company's competitors still pay higher rates in London was also a factor.

It is not yet clear how much money has been saved, and it is too soon to tell if there will be any impact on recruitment and retention.

But cost was a motivation in removing the zonal system, partially based on a feeling that the company was paying above market rates in some areas. 'Decisions like this are sometimes more about a feeling than numbers', the company says. It looks at what other organisations are doing and compares this to its own practice. No existing staff had their pay reduced as a result of the removal of location-based pay, the change just affected new starters.

14 Appendix A - Questions for OME case studies

A Background to company

1. Structure of company
2. Number of employees
3. Type of employees (occupations, qualifications)
4. Labour turnover
5. Pay setting mechanisms, pay structure and annual reviews. What are your local pay arrangements?
6. Recruitment and retention problems experienced and how they have been dealt with:
 - Prior to 2008 (i.e. what were you doing in a period of labour shortages?)
 - Since 2008 and current (i.e. are you still having R&R problems? If yes, how are you dealing with these? If no, how have you withdrawn from previous approaches and arrangements?)

B Approach to pay differentiation by location

7. What are the objectives of your local pay system?
8. Which employee groups are covered by any system of local pay? How many employees receive local pay? Has this changed since 2008? Will you be making any changes in the near future?
9. Are any employee groups (e.g. senior/professional staff) excluded and at what salary levels? If yes, why? And has this changed recently?
10. What do you consider the relevant labour markets (i.e. local, regional, national, international) for different employee groups and how is this determined? Has this changed recently?

C The process by which decisions on pay differentiation are made

11. What data and evidence is used in decision making?
12. What factors are considered to be important e.g. cost of living, external labour market, internal staff turnover?
13. How are individual occupations selected for pay differentiation?
14. How are decisions made on the degree of pay differentiation used?
15. At what level in the organisation are decisions made – e.g. local managers, regional managers, central HR?
16. Why is pay set at this level i.e. if central why not local and vice versa?

17. Are trade unions or staff representatives involved in the decision?
18. Is the pay system constantly changing, or set for the medium term. How often are decisions made or the labour market assessed?
19. What are the mechanisms for initiating a review of pay for an occupation or locality – what triggers a change, who proposes it and how is the case assessed?
20. How are changes in pay communicated to employees?
21. Are employees aware of and do they understand the system and purpose of pay differentiation?
22. Have any aspects of the decision-making process on local pay changed in recent years/since 2008?

D Co-ordination and monitoring of pay differentiation

23. What mechanisms are in place to support the implementation of local pay, e.g. guidelines for local managers?
24. If decisions are made by local managers, how are these decisions monitored and by whom?
25. Does your organisation monitor centrally what employees are paid and the extent to which discretionary allowances or extra pay are being used?
26. Have there been any changes in the way you co-ordinate and monitor pay differentiation in recent years?

E Cost of pay differentiation

27. How do you control the overall paybill while providing discretionary local pay?
28. What was the cost of installing geographically differentiated pay?
29. What have been the recurring costs - in additions to salaries - each year?
30. What were the resource and personnel costs of administering local pay and monitoring data in the past year?
31. Is it administratively demanding to run your local pay system?
32. Have you obtained value for money for your 'spend' on local pay?

F Evaluation of pay differentiation

33. Do you evaluate the success or effectiveness of the system in dealing with recruitment and retention problems, and if so, how?
34. What have been the outcomes of your local pay system?
35. Have the objectives of your local pay system been met?

36. If you currently had no system of local pay, would you introduce one now?
If yes, would you introduce the same system?

G Potential problems with pay differentiation

37. Is the extent of variation in pay between regions for the same or similar jobs considered acceptable throughout the organisation, as a general principle and also with respect to the amount of variation?
38. Do your employees think local pay is fair?
39. Are there any equal pay implications from varying pay by location, i.e. how do you align local pay differentiation with job evaluation and equal pay?
40. Are there cliff edge/boundary effects between different local labour markets, and how are these managed?
41. Have any of your staff moved between regions simply to obtain a local pay supplement?
42. Conversely, have local pay additions discouraged employees from applying for promotions or moving to other regions at the employer's request?
43. Have you had problems with bidding wars between different regions?
44. Have your local pay additions had an effect on the external labour market?
45. If there has been a significant change in your approach to these issues, what 'transition' issues arose?

H Loosening labour markets

46. Can you take local payments away? Have you already reduced or removed local supplements as a result of a loosening of the labour market, or for any other reason?
47. If so, what did you do, how much money has been saved, and what has been the reaction of those responsible for recruitment and employees?
48. If this has not already happened, how would you deal with a loosening of the labour market?
49. Who would decide whether to withdraw market supplements, and on what basis?
50. What evidence would be used to support such a decision?
51. How would you communicate the decision to staff?
52. Do you check that you are not paying above market rates in some areas, or do you not consider this to be an issue?
53. If yes, what did you do about, or what would you do should this happen?

15 Appendix B – Literature Review

Literature search for articles on geographical pay differentiation

- 1) What price geography in pay determination? A Hatchett, Personnel Management October 1988
- 2) Regional earnings differences – A South East phenomenon: IDS Pay Report 537, January 1989
- 3) Local pay bargaining in the NHS: Includes a survey of pay and labour markets developments in the NHS and local government: IDS Pay in the Public Services 1998/99
- 4) Pay differentiation practice in UK organisations: A research report by IDS for the OME, November 2002
- 5) A history of London Weighting: A report by IDS for the Greater London Authority London Weighting Advisory Panel, March 2002
- 6) Estimated regional wage relativities for England: a report for the South East Cost Adjustment Group and Association of London Government: D Blanchflower, A Oswald and B Williamson, NERA Economic Consulting 2002
- 7) Differentiated pay and incentives: Chapter 4 of the STRB report, OME, 2002
- 8) London Weighting: Report of the London Weighting Advisory Panel: GLA 2002
- 9) Regional pay: getting the balance right between national and local: IDS Pay Report 872, January 2003
- 10) Regional pay: The realities of private and public sector practice IDS April 2003
- 11) Gordon Brown launches review of regional cost-of-living data: IDS Pay Report 878, April 2003
- 12) Chancellor advocates regional pay within national frameworks: IDS Pay Report 884, July 2003
- 13) Local approaches to pay: Chapter 4 of STRB Report Volume 2, OME, 2004
- 14) London pay, recruitment and retention in higher education: A report by IDS for the London HE Pay Consortium July 2004
- 15) How zonal pay is used to address cost-of-living and labour market variations: IDS Pay Report 904, may 2004
- 16) Pay in London and the South East: IDS Pay Report 908, July 2004
- 17) Regional wages and the need for a better area cost adjustment: D Blanchflower and A Oswald, Public Money and Management, April 2005
- 18) London Weighting Payments: A report by IDS for the OME February 2005
- 19) Recent research on the levels of variation of geographical pay differentials and the implications for London Weighting payments for DDRB'S remit groups: OME 2005

- 20) NHS Partners Report on high cost area supplements and recruitment and retention premiums: OME 2005
- 21) Local pay: approaches and levels: CIPD fact sheet by Steve Palmer September 2006
- 22) Developments in occupational pay differentiation: A research report by IDS for the OME, October 2006
- 23) Regional earnings show little variation outside London and the South East: IDS Pay Report 965, November 2006
- 24) Geographical pay differentiation in multi-site private sector organisations: A research report by IDS for the OME October 2008
- 25) More than we bargained for: the social and economic costs of national wage bargaining, Alison Wolf, Centre Forum 2011
- 26) Controlling public spending: pay, staffing and conditions in the public sector: E Holmes and A Lilico, Policy Exchange 2010
- 27) Public and private sector terms, conditions and the issue of fairness E Holmes and M Oakley, Policy Exchange May 2011
- 28) Public and private sector earnings: fact and fiction: IDS Pay Report June 2010
- 29) Estimating differences in public and private sector pay: A Damant and J Jenkins, ONS July 2011
- 30) Public Sector Pensions and Pay: C Emmerson and W Jin: IFS Green Budget, IFS February 2012
- 31) Pay in the Public Services 2011: IDS February 2011
- 32) The purpose and risks of zonal pay: IDS Pay report 1074 June 2011
- 33) Regional pay at the Royal Bank of Scotland: IDS Pay Report 1078 August 2011
- 34) Pay in finance: IDS Pay Report 1079 August 2011
- 35) Autumn Statement: HM Treasury 29 November 2011
- 36) Regional pay – Can it work this time? S Bevan Work Foundation November 2011
- 37) London allowances 2011 (Includes sections on zonal pay in the banks and retailing) IDS HR Study 955, December 2011
- 38) Pay in the public services 2012: IDS February 2012
- 39) Regional variations in Pay: Chapter in Pay and conditions in retail 2012, IDS, January 2012
- 40) Ten myths about local pay determination: IDS Pay Report 1090, February 2011
- 41) Ministry of Justice pay agreements giving details of regional pay zones: IDS Pay Report 1091 February 2012