Legal Update Article

Tiered Pay Structures and Manufacturing Industry

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The current auto industry labor negotiations have sparked a lively debate about the efficacy of adopting or maintaining a tiered pay structure for a manufacturing workforce. While some may argue that these structures are a relic of the economic downturns experienced in past years, others tout the cost containment value of tiered pay.

In its simplest form, a tiered pay structure preserves existing wage progressions for current employees but adopts a different, and generally less robust, structure for new employees. The result is that an employee's wage progression is dependent on their tenure with the company. Some tiered systems contain a catch-up provision enabling lesser-tenured employees to eventually equalize their pay with greater-tenured workers by working a requisite number of years. In other cases, the company operates with permanent differing pay progressions depending on the worker's date of hire.

During times of financial stress and high unemployment, tiered pay represents a mechanism for preserving existing pay scales for longer-tenured employees while conserving resources by lowering the pay scales for new employees. The system is effective if manufacturers contemplating its use can draw on a ready pool of job applicants eager for work even at the reduced scale. The system is also effective in industries with high-demand jobs that applicants are anxious to fill even at lower initial hourly pay rates.

Some manufacturers have utilized the tiered structure as a stopgap measure to ride out economic downturns. Particularly in unionized settings, the structure can become entrenched in the organization because the system is embodied in a collective bargaining agreement between the unionized manufacturer and the labor organization representing its employees. Once established in any setting, the tiered structure tends to be self-perpetuating. Therefore, the value of institutionalizing and maintaining tiered pay warrants careful consideration.

Proponents of the system tout its effectiveness in expanding a workforce while, at the same time, containing labor costs. Manufacturers utilizing the system can hire more workers at a lower cost or conserve resources by paying lower wages to lesser-tenured employees. By preserving a wage progression, albeit at lower wage rates, the manufacturer still incentivizes workers to achieve greater tenure and thereby earn a higher wage. Moreover, as higher-tenured employees retire, the formerly lower-tier wages gradually become the norm.

Opponents of the tiered wage structure argue that the structure intrinsically creates a gulf between the greater- and lesser-tenured employees. They assert that lesser-tenured employees on production lines may find themselves performing identical work to greater-tenured cohorts but at a significantly lower rate of pay. Critics of the structure contend that it adversely affects morale among the lesser-tenured employees who may feel devalued in the work they are performing. In manufacturing settings, low morale can negatively impact production, thereby, as the argument goes, offsetting the savings achieved in labor costs.

Manufacturers in unionized settings who wish to implement a tiered wage structure must be mindful that the system cannot be implemented during the term of a collective bargaining agreement without the union's consent. Once the agreement expires, the manufacturer may propose adoption of the tiered structure, and the successful implementation of the system is dependent on the vagaries of the collective bargaining process. While some unions may embrace the concept, others will chafe at the proposal and implementation may be possible only if the parties reach a bona fide impasse in negotiations. For this reason, a manufacturer contemplating utilization of a tiered wage structure should be prepared to mount a convincing business justification for implementation.

Manufacturers contemplating use of the tiered structure should carefully weigh the pros and cons of the structure before implementation. Merit pay or hybrid pay systems can be viable alternatives. Ultimately, the advantages and disadvantages of tiered pay depend on the nature and composition of the manufacturer's workforce, the company's financial status and structure, and the company's workplace culture. In short, one size does not fit all.

Jackson Lewis attorneys are available to assist manufacturers in evaluating the efficacy of implementing or maintaining tier wage structures and in navigating the intricacies of these programs.

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