Proposal for Implementing Performance-Based and Competency-Based Pay Systems

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Executive Summary

Mountain West Community Credit Union is expanding its digital banking services while continuing to operate a regional branch network. Its compensation system needs to support that growth while helping the organization retain experienced employees, develop specialized talent, and reward performance without creating incentives that conflict with member needs or compliance requirements. This proposal recommends keeping market- and job-based salary ranges as the foundation of compensation and adding performance-based and competency-based pay where each fits the work. Performance-based pay would reward measurable outcomes employees or teams can reasonably influence. Competency-based pay would provide salary progression for employees who develop and demonstrate capabilities that Mountain West needs. Using both approaches allows the credit union to recognize what employees accomplish and the skills and knowledge they bring to the organization.

Introduction

Mountain West Community Credit Union is a hypothetical regional financial institution based in Utah with operations in surrounding Mountain West states. The credit union plans to expand digital banking while maintaining its branch network. Its compensation goals are to remain competitive in relevant labor markets, reduce turnover in difficult-to-fill positions,

maintain internal pay relationships, and control labor costs as the organization grows. Incentive programs must also support performance without rewarding behavior that conflicts with compliance standards or member needs.

Previous compensation planning established salary ranges based on job value and relevant labor markets. Market data can help Mountain West determine what a job should pay, but it does not address differences in employee capability or performance. Performance-based and competency-based pay can address those differences without replacing the existing salary structure.

Organizational Strategic Goals

Mountain West's strategy depends on different types of employee contribution. Expanding digital banking requires stronger technology, cybersecurity, compliance, and financial-services expertise. Maintaining the branch network depends on member service, operational accuracy, and employees who understand the credit union's products and services. Lending growth depends on production, but those results cannot come at the expense of appropriate lending practices, compliance, or member needs.

These differences should be reflected in how employees are paid. Loan production is a reasonable performance outcome for a loan officer, but it would be a poor measure of an information security analyst's contribution. Technical expertise may create considerable value for Mountain West even when that value cannot be reduced to an individual production number. The compensation system needs enough flexibility to recognize both outcomes and employee capability.

Performance-Based Pay

Performance-based pay ties a portion of compensation to predetermined performance measures. For the incentive to motivate performance, employees need to understand what is being measured, value the reward, and have reasonable control over the result. When employees have little influence over an outcome, the link between their effort and compensation weakens (Atchison et al., 2026).

Mountain West should use performance-based compensation as variable pay rather than automatically adding these rewards to base salary. Individual incentives make the most sense in positions where employees have meaningful control over measurable results. Consumer and mortgage loan officers fit this model because they directly influence lending activity. Loan volume alone, though, would be too narrow. Employees tend to focus on what is measured and rewarded, so a production-only incentive could shift attention away from member service, documentation quality, or risk (Atchison et al., 2026).

Where work is more interdependent, incentives should shift to the team level. Member service employees could participate in a smaller branch or team incentive tied to service, accuracy, and shared operational goals. Branch managers could have a larger variable component based on overall branch results. Matching the incentive level to the level at which employees can influence performance keeps the connection between work and reward clearer (Atchison et al., 2026).

Competency-Based Pay

Competency-based pay focuses on the knowledge, skills, and capabilities employees bring to their work. Atchison et al. (2026) describe competencies as employee inputs and emphasize connecting them to organizational outcomes. For Mountain West, the purpose would be to reward employees for developing capabilities the credit union needs rather than simply increasing pay based on time in the position.

Selected job families would use three competency levels: foundational, proficient, and advanced. Moving to a higher level would require evidence that the employee can perform at that level. Depending on the job, evidence could include training, relevant certifications, proficiency assessments, increasingly complex assignments, and observable work behaviors. Experience may support competency development, but time in a position alone would not qualify an employee for progression (Atchison et al., 2026).

Competency-based progression is particularly useful for compliance, information security, digital banking, and member service positions. For example, an information security analyst could advance by demonstrating deeper technical expertise and the ability to independently address more complex security issues. A member service representative could advance through broader product knowledge, cross-training, and the ability to handle more complex member needs.

Competencies with continuing strategic value could support movement within the employee's salary range. For an emerging skill that may only be valuable for a limited period, a bonus may make more sense than permanently increasing base pay (Atchison et al., 2026).

Suitable Positions and Evaluation Criteria

The same compensation approach should not be applied to every position. Mountain West should base the mix on how much control employees have over measurable outcomes and how important increasing expertise is to successful performance.

Employee Group	Compensation Approach	Primary Evaluation Criteria
Consumer and Mortgage Loan Officers	Base salary + individual performance incentive	Lending results, member service, documentation quality, compliance/risk standards
Member Service Representatives	Base salary + competency progression + team incentive	Product knowledge, cross-training, service quality, accuracy, branch/team goals
Compliance, Information Security, and Digital Banking	Base salary + competency progression; limited team/company incentive	Technical or regulatory knowledge, relevant certifications, complexity of work, demonstrated proficiency
Branch Managers	Base salary + competency progression + team performance incentive	Branch results, member service, employee development, operational performance, compliance

Establish performance measures before the performance period, and ensure they reflect outcomes employees can reasonably influence. Compliance and conduct standards should also act as a threshold for incentive eligibility. High production should not offset serious failures in compliance or member protection.

Competency decisions need the same level of structure. Each competency should include defined proficiency levels and observable evidence for advancement. Managers would document the basis for advancement rather than relying on a general assessment that an employee is "advanced." If competency levels affect pay, employees need to understand what separates one level from another and what they need to demonstrate to progress (Atchison et al., 2026).

Challenges and Risks

Poorly designed performance pay can shift attention to the rewarded number instead of the results the organization actually needs. For Mountain West, the clearest risk is lending incentives. Paying primarily for production could encourage volume while giving less weight to service, documentation, or appropriate risk management. Using multiple measures and making compliance a condition of incentive eligibility reduces that risk.

Employee control also matters. Individual incentives should not depend heavily on results driven by market conditions or other employees. Team incentives are a better fit when work is interdependent, although they create a different concern: employees who contribute less may still share in the reward. Mountain West can address this by keeping clear individual performance expectations even when the financial incentive is based partly on team results (Atchison et al., 2026).

Competency-based pay also has measurement problems. Managers may interpret competency levels differently, and employees may pursue credentials that look valuable on paper but do not improve performance. Mountain West should use defined standards, observable evidence, and manager calibration before competency decisions affect pay. The credit union

should also review competencies periodically. Continuing to pay a premium for a capability that no longer supports the business would undermine the purpose of the system.

Recommendations for Implementation and Ongoing Management

Mountain West should introduce the system in phases. First, review the work and identify the outcomes and competencies associated with successful performance in each participating job family. Managers and employees familiar with the jobs should be involved. Job descriptions, performance information, organizational materials, and workflow can provide additional evidence when identifying relevant competencies (Atchison et al., 2026).

Once those requirements are established, Mountain West can define performance measures, competency levels, evidence requirements, incentive eligibility, and how each will affect compensation. The credit union should model the financial impact before implementation and review whether each measure captures what it is intended to reward. Competency measures should assess the intended capability, and that capability should meaningfully relate to the work Mountain West needs employees to perform (Atchison et al., 2026).

Managers will need training on performance measurement, competency assessment, documentation, and employee communication. Calibration meetings can help identify inconsistent interpretations before they become pay differences.

The system should initially be piloted with a limited number of job groups. Mountain West can then review payout patterns, labor costs, employee understanding, advancement decisions, performance results, and unintended behavior before expanding the program. The

credit union should continue to review measures and competencies as its workforce and strategy change.

Justification and Conclusion

Mountain West's compensation system needs to recognize three sources of employee value: the job, the person, and performance (Atchison et al., 2026). Job-based salary ranges provide the foundation. Competency-based progression recognizes employees who develop capabilities the credit union needs, while performance-based incentives reward results employees and teams can meaningfully influence.

Combining the approaches also avoids defining valuable performance the same way for every employee. Loan officers can be rewarded for responsible business results, member service employees can build broader capabilities while contributing to branch outcomes, and specialized professionals can progress as their expertise increases. The goal is not to add more complexity to compensation, but to make clearer decisions about what Mountain West is paying for and why. Done well, the system can support growth and employee development without losing sight of member needs, compliance, or long-term labor costs.

References

Atchison, T. J., Belcher, D. W., & Thomsen, D. J. (2026). *Internet based benefits & compensation administration*. ERI Economic Research Institute.