

Part 5 Compensation of Human Resources

Chapter 8 Establishing Pay Plans



Chapter 8 Outline

- I Determining Pay Rates
- II Establishing Pay Rates
- III Pricing Managerial and Professional Jobs
- IV Compensation Trends
- V Comparable Worth

Learning Objectives

- List the basic factors in determining pay rates
- Explain in detail how to establish pay rates
- Describe how to price managerial and professional jobs
- Discuss current trends in compensation
- Establish a pay plan

I Determining Pay Rates

Determining Pay Rates

Employee compensation refers to all forms of pay or rewards going to employees and arising from their employment. It consists of 2 parts:

- ◆ Direct financial payments
- ◆ Indirect financial payments



Can you name examples of direct and indirect payments?

Employee Compensation

Direct or Indirect compensation is given based on:

◆ Increments of time

- Hourly
- Salaried



◆ Performance

- Piecework
- Commission



Factors Influencing Pay

- Legal considerations
- Company policy
- Competitive strategy
- Equity



Corporate Policies and Competitive Strategy

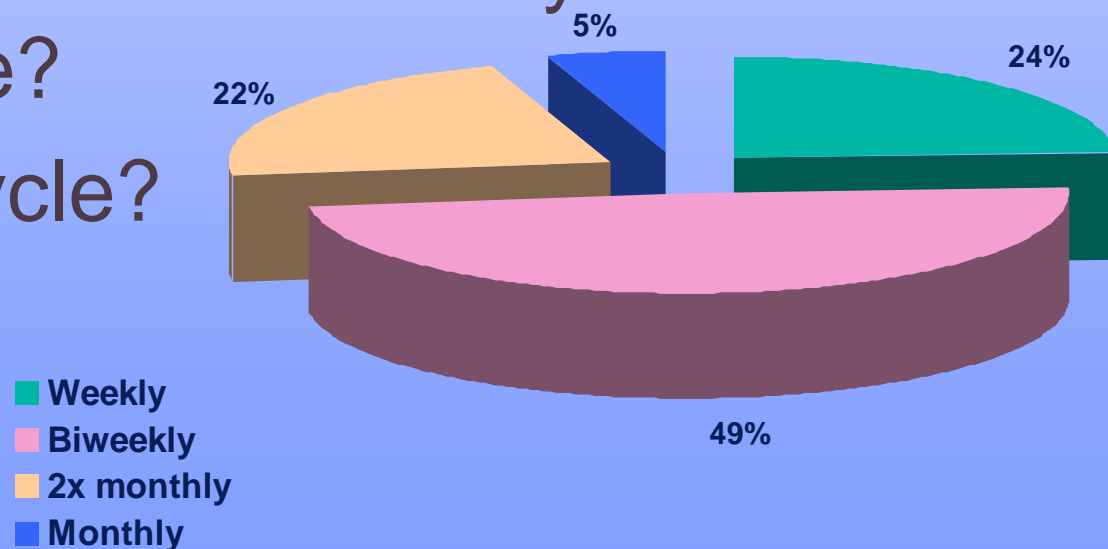
To remain competitive, compensation plans must reward strategy that furthers the firm's strategy aims by asking:

1. What are our key competitive success factors?
2. What actions implement this competitive strategy?
3. What compensation program reinforces those behaviors?
4. What requirement should each pay element meet?
5. How well do the current reward programs match these requirements?

Important Policy Issues

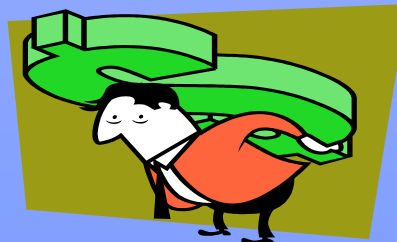
In writing the pay plan, ask the following:

1. Will we be a pay leader or a follower?
2. Will we emphasize seniority or performance?
3. What pay cycle?



Important Policy Issues

4. How do we fix salary compression?
5. How should we compensate based on geography or overseas employees?
6. Is the pay rate equitable with rates in other organizations outside the firm?





Salary Inequities

- How satisfied are you with your pay?
- What criteria were used for your recent pay increase?”
- What factors do you believe are used when your pay is determined?

Ssssssshhhh!!
Keep this raise
quiet please!



II Establishing Pay Rates

Step 1. The Salary Survey

Step 2. Job Evaluation

Step 3. Group Similar Jobs into Pay Grades

Step 4. Price Each Pay Grade—Wage Curves

Step 5. Fine-Tune Pay Rates

Establishing Pay Plans

The 5 step process:

The salary
survey

Job
evaluation

Pay grade
grouping

Price pay grade-
wage curves

Fine tune
pay rates

Step 1. The Salary Survey

The **salary survey** is a survey aimed at determining prevailing wage rates which include:

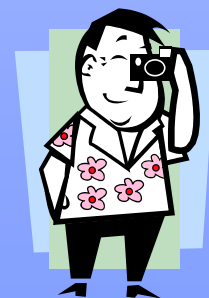
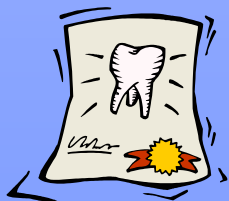
- ◆ Formal
- ◆ Informal






Uses of Salary Surveys

- Benchmark jobs
- Employers price 20% or more of their positions currently in the job market
- Surveys collect data on benefits



Commercial, Professional and Government Salary Surveys

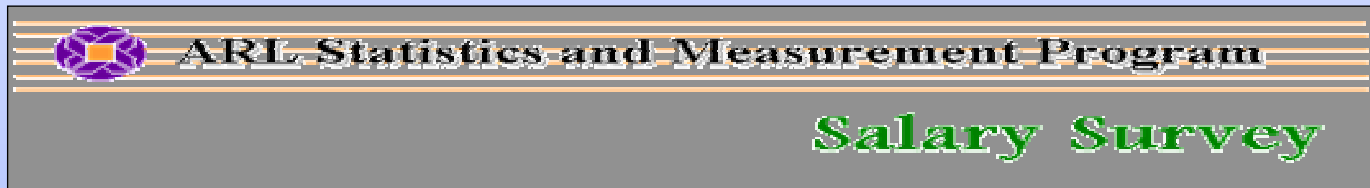
- BLS gives:
 - ◆ Area wage surveys 
 - ◆ Industry wage surveys
 - ◆ PATC surveys



- Private consultants Hay Associates, Heidrick and Struggles, and Hewitt Associates publish data covering compensation for top and middle management



Doing an Internet Based Salary Survey



YAHOO!

ExecuNet

salary.com™

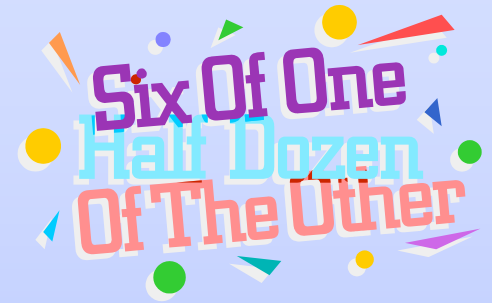
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Step 2. Job Evaluation



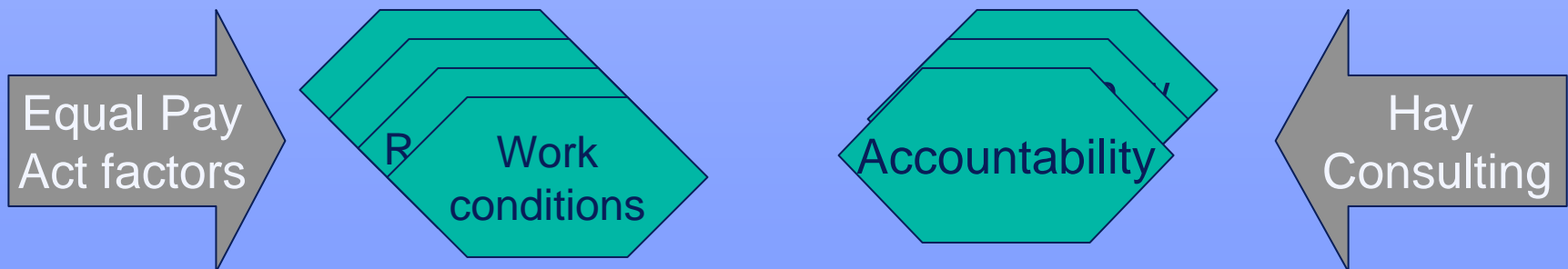
- Job evaluation is the formal and systematic comparison of jobs in order to determine the worth of one job relative to another
 - ◆ The comparison results in a wage or salary hierarchy
- Compensable factors are fundamental elements of a job

$$a^2 + b^2 = c^2$$

Compensable Factors

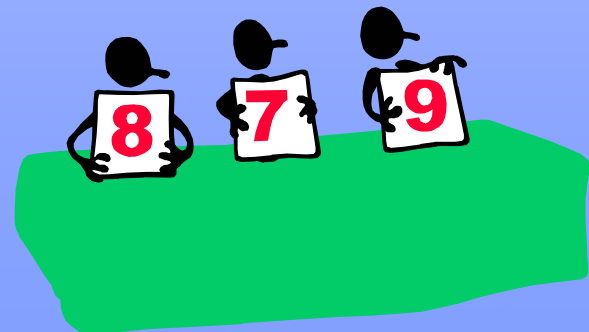


- Two approaches in comparing jobs – Intuitive or via compensable factors
- Intuitive based on decision that one job *is* more important than another
- Compensability determined arbitrarily but some metrics include:



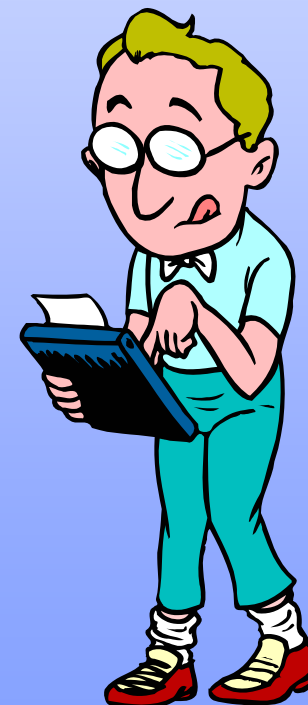
Preparing for the Job Evaluation

- Its mostly a judgmental process which requires cooperation among managers
- Identify the need for the program
- Get cooperation
- Choose an evaluation committee who will do the evaluation



Job Evaluation Committees

- Performs 3 main functions:
 - ◆ Identifies 10-15 key benchmarks
 - ◆ Selects some compensable factors
 - ◆ Evaluate the worth of each job via one of the methods on the following slides



Job Evaluation

Method 1: Ranking

- Obtain job information
- Select raters and jobs
- Select compensable factors
- Rank jobs
- Combine ratings

Try not to rely on guesstimates

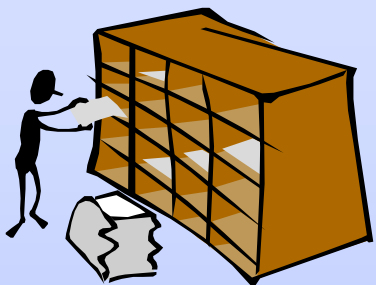


Best for small organizations

Method 2: Job Classification



- Rates categories of jobs into groups
- Groups called classes if jobs are similar
- Called grades if groups contain different jobs of similar difficulty
- Example:
 - ◆ General Schedule grading used by the U.S. government – GS-10 might grade both a dog catcher and the President!



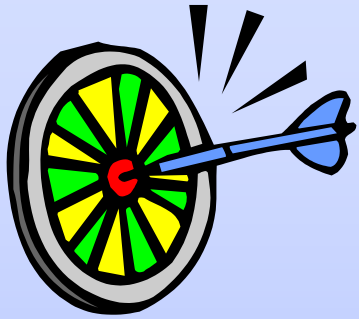
Ways to Categorize Jobs

- Write-up class or grade descriptions
- Draw up a set of guidelines
- Choose compensable factors and develop class or grade definitions

Example of GS
grade definition



GRADE	NATURE OF ASSIGNMENT	LEVEL OF RESPONSIBILITY
GS-7	Performs specialized duties in a defined functional or program area involving a wide variety of problems or situations; develops information, identifies interrelationships, and takes actions consistent with objectives of the function or program served.	Work is assigned in terms of objectives, priorities, and deadlines; the employee works independently in resolving most conflicts; completed work is evaluated for conformance to policy, guidelines, such as regulations, precedent cases, and policy statements require considerable interpretation and adaptation.



Method 3: Point

- The point method is more quantitative
- Identifies compensable factors
- The degree to which each of these factors is present
- Assume five degrees of “responsibility”
- Most widely used method

Method 4: Factor Comparison

- **Factor comparison** is a widely used method to rank jobs by a variety of skills and difficulties, then adding these to obtain a numerical rating for each job
- With this method you rank each job several times—once for each of several compensable factors





Computerized Job Evaluations



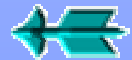
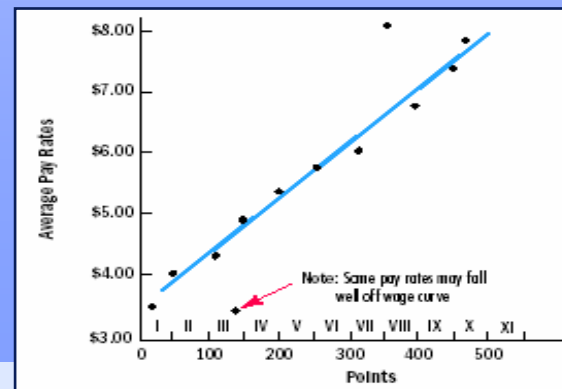
- Other methods can be time consuming
- CAJE or computer automated job evaluation streamlines things
- Simplifies job analysis
- Increases objectivity
- Manages data
- Uses structured questionnaire and statistical models

Step 3. Group Similar Jobs Into Pay Grades

- A pay grade is composed of equally difficult jobs
- Committee will assign pay rates to each job based on one of the job methods
- Ranking method grades fall in to a point range
- Point method grades fall within two-three ranks
- Factor comparison grades pay rate range
- Classification method puts into classes or grades

Step 4. Price Each Pay Grade -Wage Curves

- Developing a wage curve involves the following:
 - ◆ Find the average pay for each pay grade
 - ◆ Plot the pay rates for each pay grade
 - ◆ Fit the line called a wage line through the points just plotted
 - ◆ Price the jobs



Wage curve



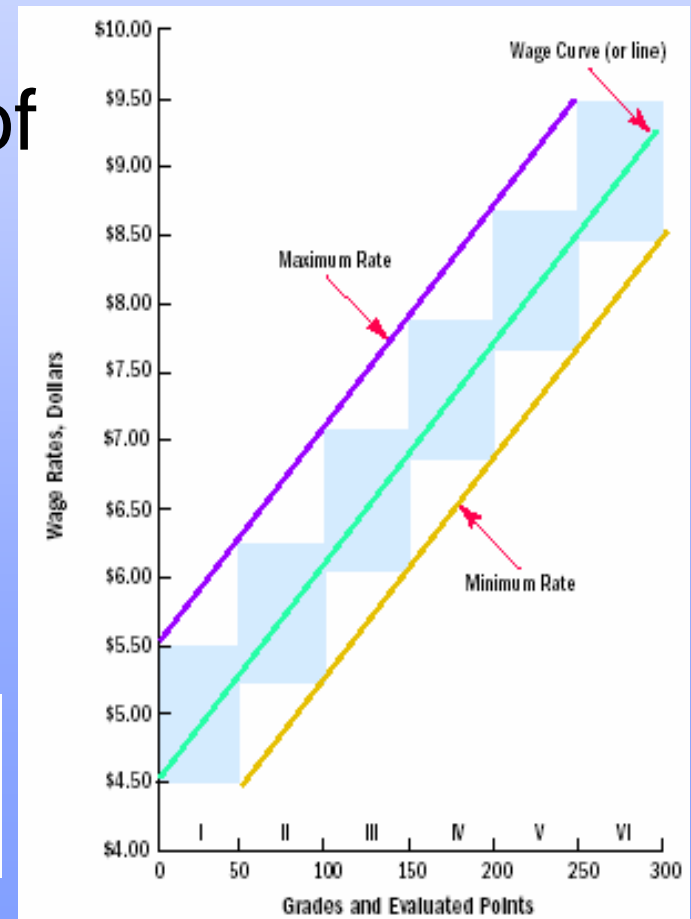
Step 5. Fine Tune Pay Rates

Pay ranges are a series of steps or levels in a pay grade, usually based on years of service

Sample pay grade schedule

Grade	Annual Rates for Steps (in dollars)									
	1	2	3	4	5	6	7	8	9	10
GS-8	32,859	33,954	35,049	36,145	37,140	38,335	39,430	40,525	41,620	42,715
GS-9	36,295	37,504	38,714	39,923	41,133	42,342	43,551	44,761	45,970	47,180
GS-10	39,969	41,302	42,635	43,967	45,300	46,633	47,966	42,298	50,631	51,964

Source: info



Correcting Out-of-Line Rates

Correct pay for grade



Too low – raise pay

Too high – lower by

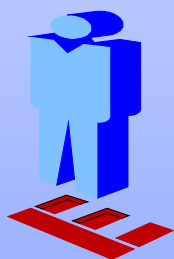
Freezing wages,
transferring or
promoting




Developing a Workable Pay Plan

Several steps to a workable pay plan:

- ◆ Conduct a wage survey by using



- Do a web based job evaluation
- Develop a pay policy that covers 
- Classify employees correctly

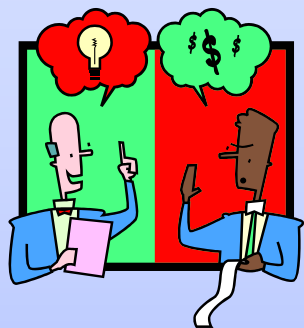


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III Pricing Managerial and Professional Jobs

3.1 Compensating Managers

3.2 Compensating Professional Employees



Pricing Managerial and Professional Jobs

- Goal is to attract and keep
- Harder to quantify evaluation
- Paid on basis of ability
- More complex and stress incentives over evaluation

3.1 Compensating Managers

Top executives compensated by:

- Base pay + guaranteed bonus
- Short term incentives
- Long term incentives
- Perks



Can you name some incentives and perks?

What Really Determines Executive Pay?

- Company size and performance
- Industry CEO average pay is \$3.6 million
- May emphasize 25% performance incentive
- Board sets CEO pay
- Shareholders may affect pay as SEC requires disclosure of all CEO pay
- Complexity of the job



3.2 Compensating

Professionals



- Job emphasizes creativity and problem solving
- Job evaluation is useful
- Some disciplines result in 4-6 grades with a broad salary range

IV Compensation Trends

4.1 Skill-Based Pay

4.2 Broadbanding

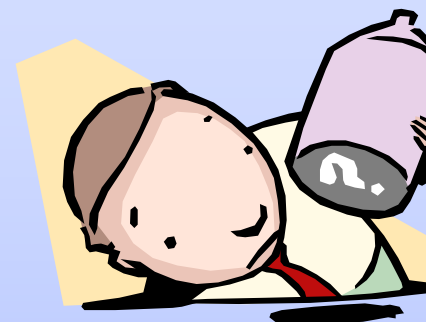
4.3 Compensation Plans in Practice

Compensation Trends



- Skill-based pay and broadbanding
- Skill-based programs pay for range, depth, and type of skills:
 - ◆ Define specific skills
 - ◆ Training system
 - ◆ Competency testing
 - ◆ Flexible work assignments
- Broadbanding combines salary grades into a few with wide salary ranges

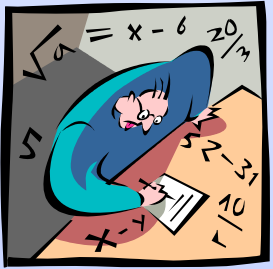
4.1 Why Pay Employees by Skill Levels?



What do you think?

- ◆ What about team organizations?
- ◆ To what extent do companies have different expectations for employees relative to multiple skill sets?
- ◆ What about overlapping jobs?
- ◆ Numbers of professionals in the company?

Skill-based Pay versus Evaluation-based Pay

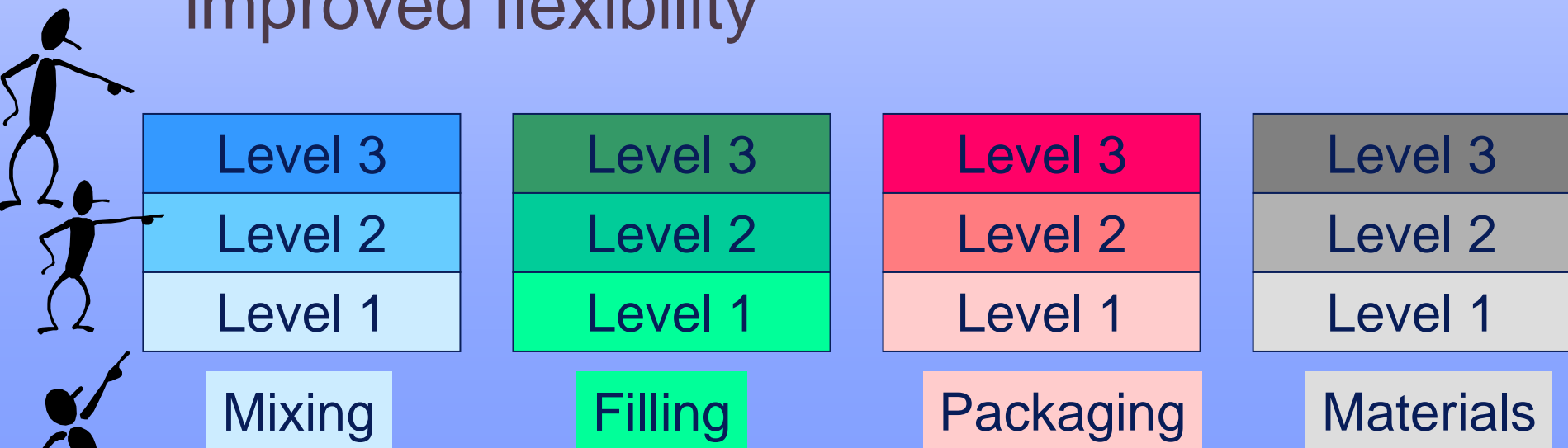


- Competence testing
- Effect of job change
- Seniority and other factors
- Advancement opportunities
- SBP may increase productivity and lower labor costs over JBP



High Performance Insight

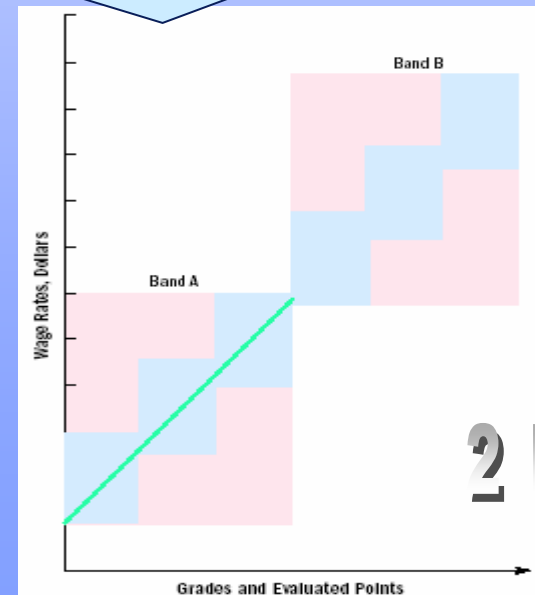
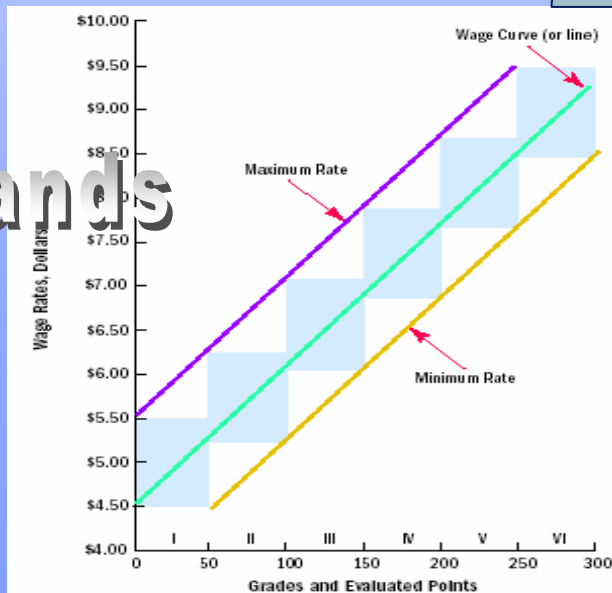
- General Mills implemented a skills-based plan
- Plan viewed as a success as it improved flexibility



4.2 Broadbanding

Broadbanding - Consolidating salary grades and ranges

6 bands

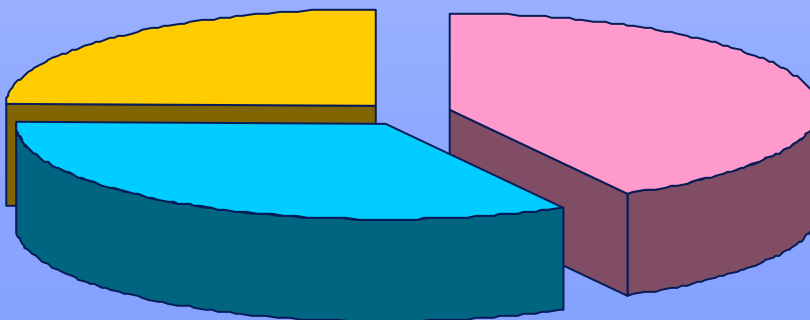


2 bands



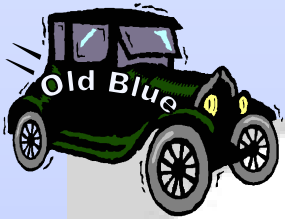
4.3 Compensation Plans in Practice

- Most employees don't understand it so how effective can they be in motivating people?
- Must make it known!



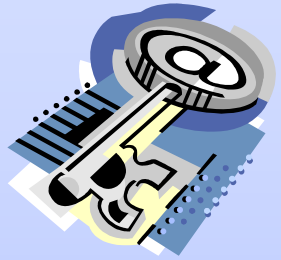
- Have articulated strategy
- Employees understand it
- Encourage desired effect

Strategic HR – IBM Study



- Prior to Gerstner, IBM used an antiquated point-based reward system
- Made 4 major changes to renew IBM's evaluation process:
 - ◆ The marketplace rules
 - ◆ Fewer jobs, evaluated differently, in broadbands
 - ◆ Managers manage
 - ◆ Big stakes for stakeholders





Compensation Plans for Dot-com Companies

- Don't use traditional pay plans
- Hiring and keeping good employees without a flexible compensation plan
- Most successful firms hire people then find jobs
- Link hiring pay to competitive practice for that position, based on real-time external research

Dot.Com Research Insight

In addition to competitive compensation and benefits, employees have:

- ◆ *Cultural expectations*
- ◆ *Rewards expectations*
- ◆ *Career opportunity expectations*



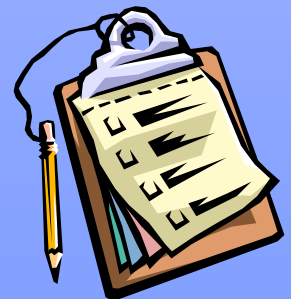
Chapter 8 Summary

- Two pay bases – time increments and production volume
- Establishing pay rates involves five steps – Can you name them?
- Job evaluation determines the relative worth of a job
- Five-step ranking method of job evaluation is simple to use – Can you name these steps?



Chapter 8 Summary

- Classification or grading groups similar jobs into classes
- Point method identifies compensable factors and the degree to which each of these is present in a job
- Factor comparison method decides which jobs have the most compensable factors



Chapter 8 Summary

- Most managers group similar jobs into wage or pay grades for pay purposes
- Compensation plan for executive, managerial, and professional personnel can be complex
- Trends in compensation include skill-based pay, broadbanding, and adjustments for comparable worth





End of Chapter Question 1



- 1. What are the pros and cons of broadbanding, and would you recommend your current employer (or some other firm you're familiar with) use it? Why or why not?



End of Chapter Question 2



- 2. Working individually or in groups, develop a compensation policy for the teller position at a local bank. Assume that there are four tellers: two were hired in May and the other two were hired in December. The compensation policy should address the following: appraisals, raises, holidays, vacation pay, overtime pay, method of pay, garnishments, and time cards.