

TRENDLINES

The Employers' Association monthly whitepaper on essential Business/Human Resources practices

The Employers' Association (TEA) delivers reports for businesses that contain relevant and up-to-date information based on our work with hundreds of employers each month. TEA is known to produce essential benchmark survey reports every year and we also compile data and observations that provide organizations practical perspectives on important business trends.

Developing an Effective Compensation Philosophy

What you should know

The way people interact with peers, the way they are treated by management, their overall satisfaction with the job and their thoughts, feelings or perceptions about the organization are critical when trying to attract or retain employees. Employee Engagement Surveys (our own and other nationally recognized surveys) consistently point out that culture, the opportunity to contribute to an organization's growth (and the ability to grow individually), a Corporate awareness of community, Diversity, Equity and Inclusion and a strong work/life balance are all more important to most workers than compensation BUT ONLY IF individuals are paid fairly (within their appropriate market), pay practices are internally equitable and consistent and each employee is appropriately recognized for what they contribute. Compensation Administration is not only a formal structure that determines how individuals are paid but also must reflect an intentional Corporate Philosophy that can be easily communicated, readily understood and consistently applied. At the heart of every effective Compensation Administration Program is a Compensation Philosophy that must be intentionally developed, transparently communicated and consistently applied.

What we know

Having developed and implemented more than 700 Compensation Administration programs throughout the country, The Employers' Association has found that:

1. ***Internal equity is much more important than external competitiveness when it comes to creating and maintaining a satisfied workforce and consistency is more important than equality.*** Some of the best organizations pay employees slightly below market averages BUT they underpay ALL employees (including their management team) in a similar manner. Dissatisfaction (causing high turnover, negative employee relations and difficulty in hiring new employees) almost always results when one group of employees is paid differently in relation to market than another. When employees know (and trust) that you will be fair and equitable (not necessarily equal) in the way they are paid they will become a big part of the organization's ongoing success. When employees doubt management credibility, or see the inconsistent application of policies or practices, they become more a part of the problem than the solution.
2. ***Strong merit pay systems tend to attract and retain high performers (and over-achievers) while tenure-based systems tend to attract risk-averse employees and retain mediocre employees.*** When definitive goals and objectives can be established **AND FULLY COMMUNICATED** to employees, linking additional pay and/or bonus to the accomplishment of those goals, employees willing and able to go the extra mile will

step forward. Paying for accomplishments is an effective way to attract and retain the best while paying for “presence” tends to attract and retain employees that may be “good” but will never be “great.”

3. ***Pay is only a part of the equation when it comes to compensation administration.*** Benefits, working conditions, flexibility, autonomy and the freedom to learn from mistakes are far more critical in creating an environment that will attract quality employees and retain a highly competent workforce. While the emerging workforce may SEEK a better work/life balance, anything that an employer can do to implement a better quality of life will benefit ALL employees and help to retain a diverse mix of ideas, talents and perspectives that will contribute to overall success.
4. ***There is a “new normal” of increased entry level pay rates due to the “war for talent” and the impact of federal and state unemployment benefits.*** The official minimum wage rate has not increased but from a practical perspective applicants and employees expect higher starting pay in entry level positions than they received prior to COVID-19. Employers are having to react/respond with previously unconsidered rates of pay to pull employees from the ranks of the unemployed AND offer benefits, flexibility and work/life balance in order to retain them.
5. ***Organizations that adjust ALL RANGES within their compensation structure with an “across the board” cost of living factor*** have found they are having difficulty attracting entry level employees and retaining highly qualified leaders while potentially overpaying their mid-level employees.
6. ***NEVER expect discretionary “gifts” to change or modify behavior.*** Link bonus / incentive programs to performance (individual and corporate), letting employees know what they must do to earn a bonus (and what could lessen their bonus), rather than giving spot cash rewards that are not linked to profits, performance or expectations. Like most change, incentive bonus pay should be the result of DELIBERATE and INTENTIONAL CONSIDERATION starting with what you hope to accomplish then working backwards to how best to bring that goal to fruition. An effective bonus program should be able to change behavior, motivate performance and reward individual (or group) contributions to the bottom line. Gifts are nice but do not meet these criteria so, while appreciated for a short time they do not typically translate to increased productivity, better quality, improved performance, a safer work environment, better customer satisfaction or higher profitability.
7. ***Compensation Administration IS NOT a static science.*** Pay ranges should be updated regularly to reflect changing market conditions AND should be tempered by an organization’s ability to pay. In order to effectively administer compensation organizations must realize that pay ranges are market driven but that pay adjustments should reward individual employee performance.
8. ***An organization can develop any system it might wish to use or benchmark against competitive practices but unless those decisions are condensed to writing, communicated to employees and applied consistently they will not effectively attract or retain a qualified workforce.***

What it means

TOTAL COMPENSATION is a combination of pay, benefits, time off and Organizational Culture. An outside “third party” can be helpful in developing a plan and a structure that will ensure external competitiveness and internal equity. An organization must take the time to consider HOW it wants to “match up” to the competition and what areas are most critical in attracting and retaining employees. Companies that seek technologically savvy workers may need to offer more pay, more time off, opportunities for growth and more flexibility to workers. Organizations needing a highly experienced workforce may need to offer more benefits and stability. All employees want to be recognized for what they do but different generations, backgrounds and levels of experience do not typically seek the same kinds of rewards.

Considering HOW you want to compare to the market and WHAT you are willing to provide to employees IN EXCHANGE FOR what you expect them to provide to the organization and HOW WELL they perform are the basic components of a strong Compensation Philosophy – a statement that should be developed intentionally and communicated without reservation. This philosophy should be consistently applied so that employees know what is expected of them AND what they will receive in return for their accomplishments. Developing a strong Compensation Administration Program that recognizes this will allow organizations to attract, retain and reward exceptional employees. Be intentional in your compensation practices – profitable and productive business models are not accidental – while considering TOTAL COMPENSATION rather than ONLY hourly or annual pay. Employers that treat everyone identically (rather than differently based on what they contribute and how well they perform) will find they have created a safe haven for mediocre workers. Exceptionally talented employees seek recognition and appropriate rewards for their individual contributions. Marginal employees provide as little as management will allow and are happy to accept as much as they are provided. An organization must look to balance what it can afford with what it is willing to provide while maintaining an acceptable margin in order to remain sustainable. Developing and communicating a Compensation Philosophy will help to solidify this position while ensuring that employees are treated fairly and equitably while establishing mutual respect.

What you can do

Organizations should develop and communicate a Corporate Compensation Philosophy (considering total compensation and appropriate pay/benefits/recognition requirements of its desired workforce) that can be shared with employees. Publishing a set of standards and expectations helps to “cement” employees in place by defining how their organization pays in relation to “market,” what employees must do in order to be recognized and receive a greater reward and what opportunities might exist within their organization to allow growth. We see more organizations “growing their own” talent as qualified workers are already working so skilled and knowledgeable employees must be developed rather than hired – and in order to retain talent employers must provide competitive pay, benefits, an exceptional culture and opportunities for advancement. In order to attract and retain the best people you must honestly say what you intend to do about total compensation and do what you said you were going to do. A strong Compensation Philosophy should allow an organization to:

1. Attract a qualified, diverse workforce through a competitive compensation program.
2. Retain and motivate the workforce by recognizing and rewarding individual and group achievement, contribution, and excellence.
3. Provide a non-discriminatory merit-based compensation program; and
4. Reward individuals for activities performed that are far beyond the scope of their assigned responsibilities, that do not interfere with the performance of their regular duties, that require significant investments of both time and intellectual capital.

A strong Compensation Philosophy should ensure that the organization utilizes local resources to establish and maintain competitive pay levels within relevant markets (considering available resources), that provides both external competitiveness and internal equity that is consistent with job content, responsibilities, and requirements. Consistent with the above, salaries for administrative and support staff should consistently mirror relevant markets, exceeding competitive rates for job proficiency when performance is substantially above established standards and expectations and lagging relevant markets when performance is below established standards and expectations. Employees should have a right to know how you perceive their performance, their strengths, and areas needing improvement.

When developing a Compensation Philosophy an organization should state (and be willing to consistently apply) its intent to consider not only pay but also benefits and working conditions (Total Compensation) when establishing fair and appropriate compensation levels for its staff. Fringe benefits (Healthcare and other insurance coverage, time-off with and without pay, workplace flexibility, Holiday Pay, Educational Reimbursement Program, internal training and growth opportunities, etc.) should be considered as a part of a Total Compensation Plan when benchmarking against other similar employers within the region.

Be consistent – as soon as an employer says one thing but does something else floodgates of suspicion and mistrust will be opened that are often difficult to close. Good employees NEED to respect their employer, feel they are valued and know they are rewarded fairly. Anything less is NOT a good foundation for effective Compensation Administration – rather it is the foundation for becoming a great training ground for other employers who are more than happy to leverage your trained and talented employees for their greater good. TEA can help as you seek to develop and implement a strong Compensation Philosophy to help guide your Compensation Administration practices. Give us a call at 616.262.8891 to learn more.

