

Human Resources Management

Robert L. Mathis | John H. Jackson

Prepared by Dr. Samah Abdelfatah

MGM 243

Lecture 09



Part 4: Compensating Human Resources

Chapter
12

Total Rewards & Compensation

Lecture 9

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**Chapter
12**

Learning Outcomes

After you have read this chapter, you should be able to:

- Identify the three general components of total rewards and examples of each.
- Discuss four compensation system design issues.
- Outline the process of building a base pay system.
- Describe the two means of valuing jobs.
- Explain two ways individual pay increases are determined

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Nature of Compensation

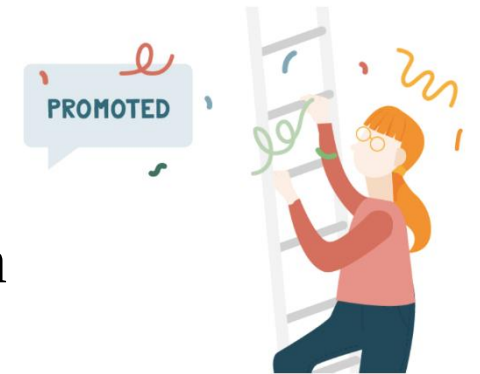
Total rewards: Monetary and non-monetary rewards provided to employees in order to attract, motivate, and retain them

Types of Rewards○ **Intrinsic**

- Intangible, psychological and social effects of compensation

○ **Extrinsic**

- Tangible, monetary and nonmonetary effects of compensation



Total Rewards Components



FIGURE 12-1

COMPENSATION

Includes *fixed (base) pay* and *variable pay (pay at risk)*.

Also includes several forms of variable pay, such as short- and long-term incentives.

The most traditional element in total rewards and a key to business success

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COMPENSATION

- **Base pay** Basic compensation that an employee receives, usually as a wage or a salary.
- **Wages** Payments directly calculated on the amount of time worked.
- **Salaries** Consistent payments made each period regardless of the number of hours worked.
- **Variable pay** Compensation linked directly to individual, team, or organizational performance (e.g. **bonuses**)
- **Benefits** Include traditional programs such as medical, dental, and retirement, as well as newer, nontraditional programs such as identity theft and pet insurance.



Compensation Philosophies

Continuum of Compensation Philosophies



- ◆ Seniority-based pay
- ◆ Across-the-board raises
- ◆ Pay scales raised annually
- ◆ Industry comparisons of compensation only
- ◆ “Santa Claus” bonuses

- ◆ No raises for length of service
- ◆ No raises for longer-service poor performers
- ◆ Market-adjusted pay structures
- ◆ Broader industry comparison
- ◆ Bonuses tied to performance results

Typical Division of HR Responsibilities: Compensation

HR Unit

- Develops and administers the compensation system
- Evaluate jobs and analyzes pay surveys
- Develops wage/salary structures and policies

Managers

- Identify job descriptions and compensation concerns
- Recommend pay rates and increases according to HR guidelines
- Evaluate employee performance for compensation purposes

COMPENSATION SYSTEM DESIGN ISSUES

Compensation Fairness and Equity

Equity	The perceived fairness between what a person does (inputs) and what the person receives (outcomes).
Procedural Justice	The perceived fairness of the process and procedures use to make decisions about employees
Distributive Justice	The perceived fairness in the distribution of outcomes.
Pay Openness	The degree of openness or secrecy that an organization allows regarding its pay system.
External Equity	The perception that the organization provides employees with compensation that comparable to the compensation of employees with similar jobs in other organizations.

EQUITY CONSIDERATIONS IN COMPENSATION



FIGURE 12-2

COMPENSATION SYSTEM DESIGN ISSUES CONT.

Market Competitiveness and Compensation

Compensation Strategies	
Above-Market	Paying for higher qualified, more productive workers.
Middle-Market	Attempting to balance of employer costs and need to attract and retain employees.
Below-Market	Paying all that the firm can afford Taking advantage of the abundant supply of potential employees in a loose labor market.

COMPENSATION SYSTEM DESIGN ISSUES CONT.

- **Competency-based pay:** Rewards individuals for the capabilities they demonstrate and acquire.
- **Individual vs. Team Rewards:** Many organizations use team incentive rewards on top of base pay.
- **Global Compensation Issues**

Possible Components of Global Employee Compensation

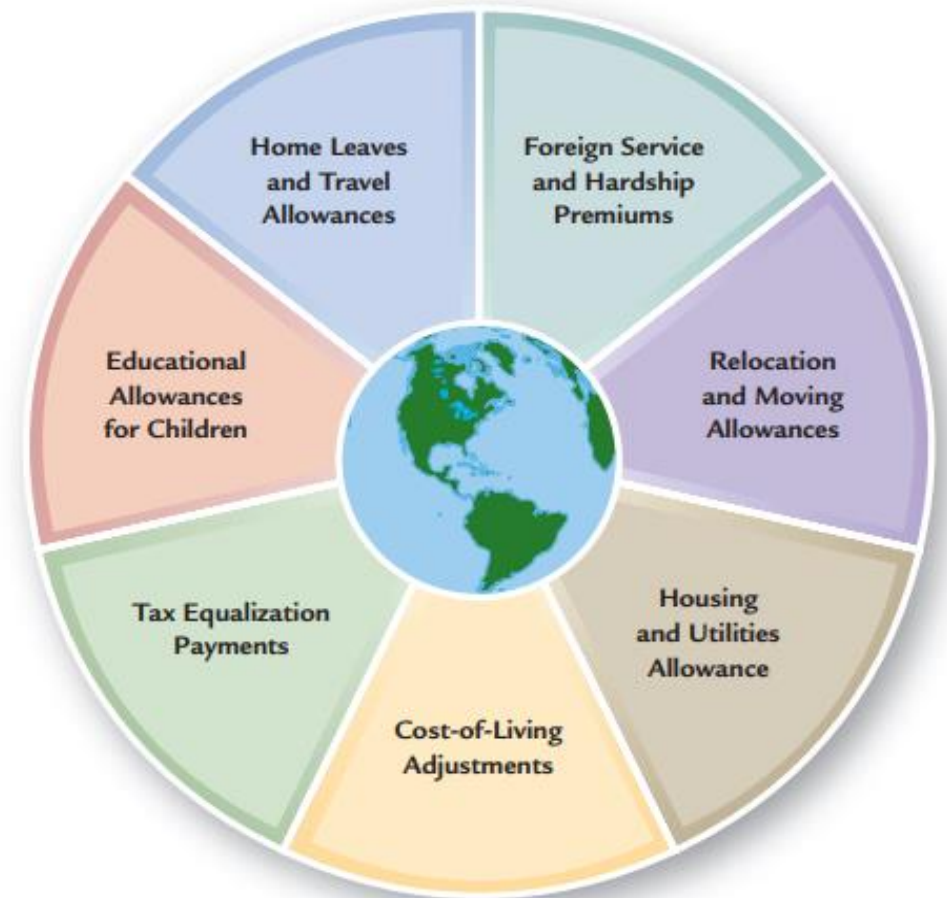


FIGURE 12-3

LEGAL CONSTRAINTS ON PAY SYSTEMS

○ Fair Labor Standards

- Establish a minimum wage.
- Discourage oppressive use of child labor.
- Encourage limits on the number of hours employees work per week, through overtime provisions (exempt and non-exempt statuses).

- **Exempt employees** to whom employers are not required to pay overtime.
- **Non-exempt employees** who must be paid overtime

COMPENSATION ADMINISTRATION PROCESS

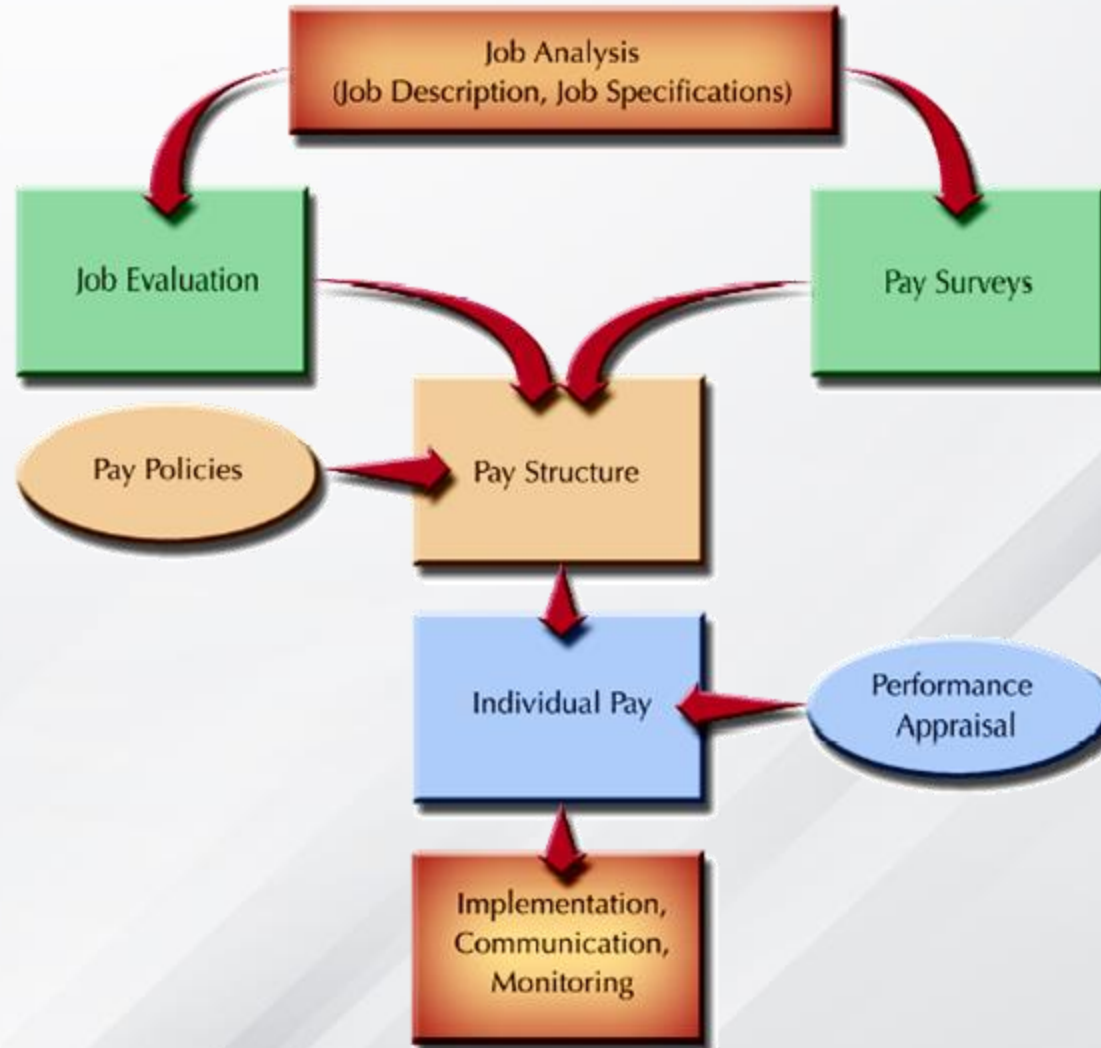


FIGURE 12-4

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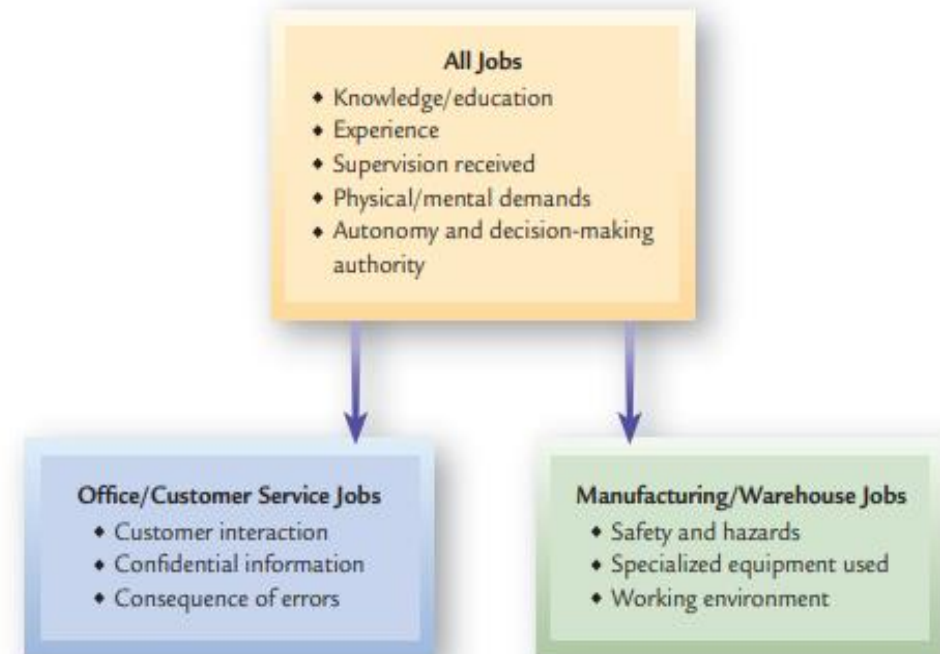
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Valuing Jobs with Job Evaluation Methods

Job evaluation: Formal, systematic means to identify the relative worth of jobs within an organization

- **Point Method :Is the most used method.**
- It breaks jobs down into various **compensable factors** and places *weights*, or *points*, on them.
- **A compensable factor** identifies a job value commonly present throughout a group of jobs. Compensable factors are derived from the job analysis and reflect the nature of different types of jobs.

Examples of Compensable Factors for Different Job Families



Valuing Jobs with Job Evaluation Methods

Other Job Evaluation Methods

The ranking method

- Is a simple system that places jobs in order, from highest to lowest, by their value to the organization.

The classification method

- Descriptions of each class of jobs are written, and then each job in the organization is put into a grade according to the class description it best matches.

The factor-comparison method

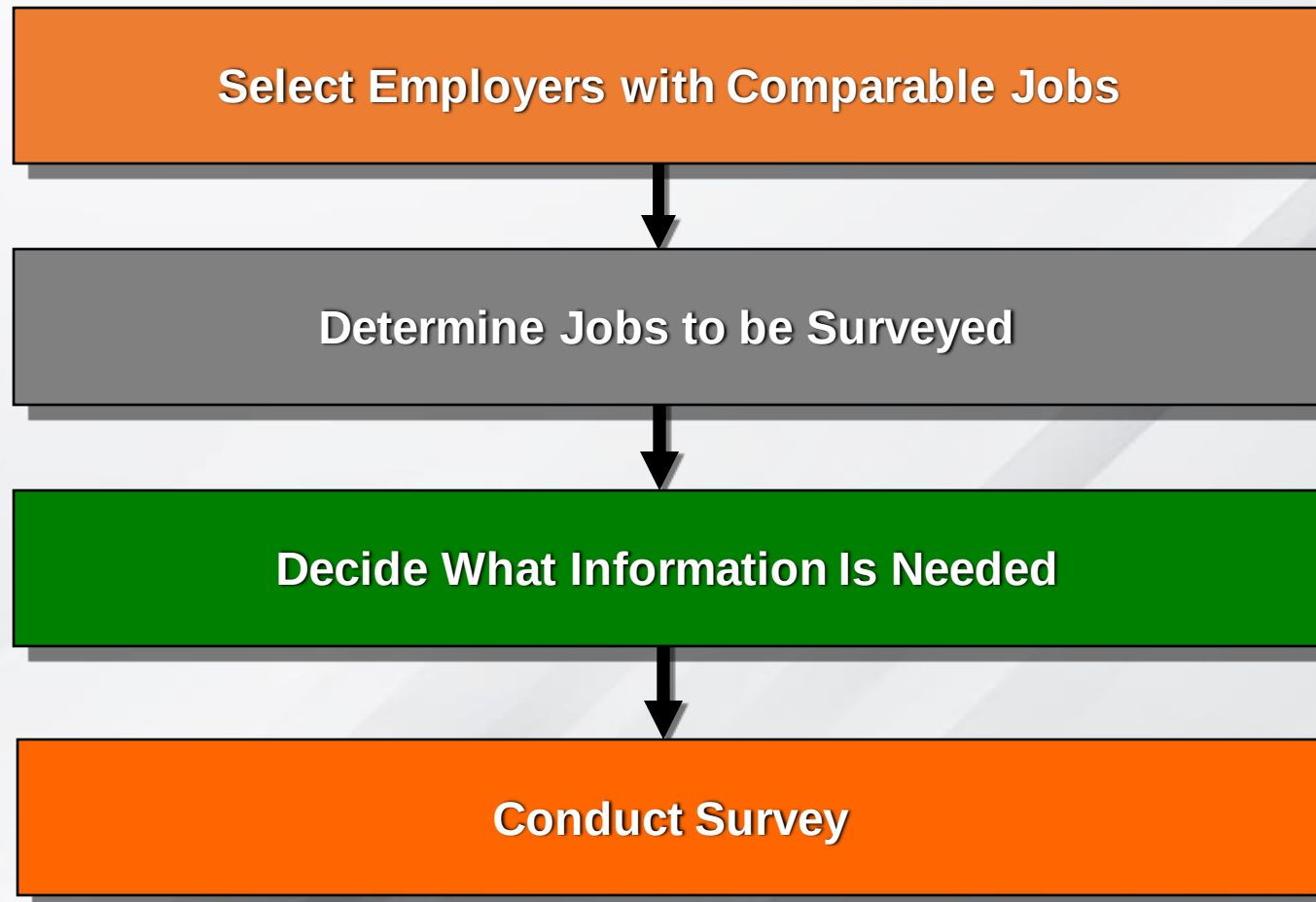
- a quantitative complex combination of the ranking and point methods. Each organization must develop its own key jobs and its own factors.

Market pricing

- Use of market pay data to identify the relative value of jobs based on what other employers pay for similar jobs

Developing Pay Surveys

- **Pay Surveys** :Collection of data on compensation rates for workers performing similar jobs in other organizations. It is important to **Benchmark jobs**.



Establishing Pay Structures

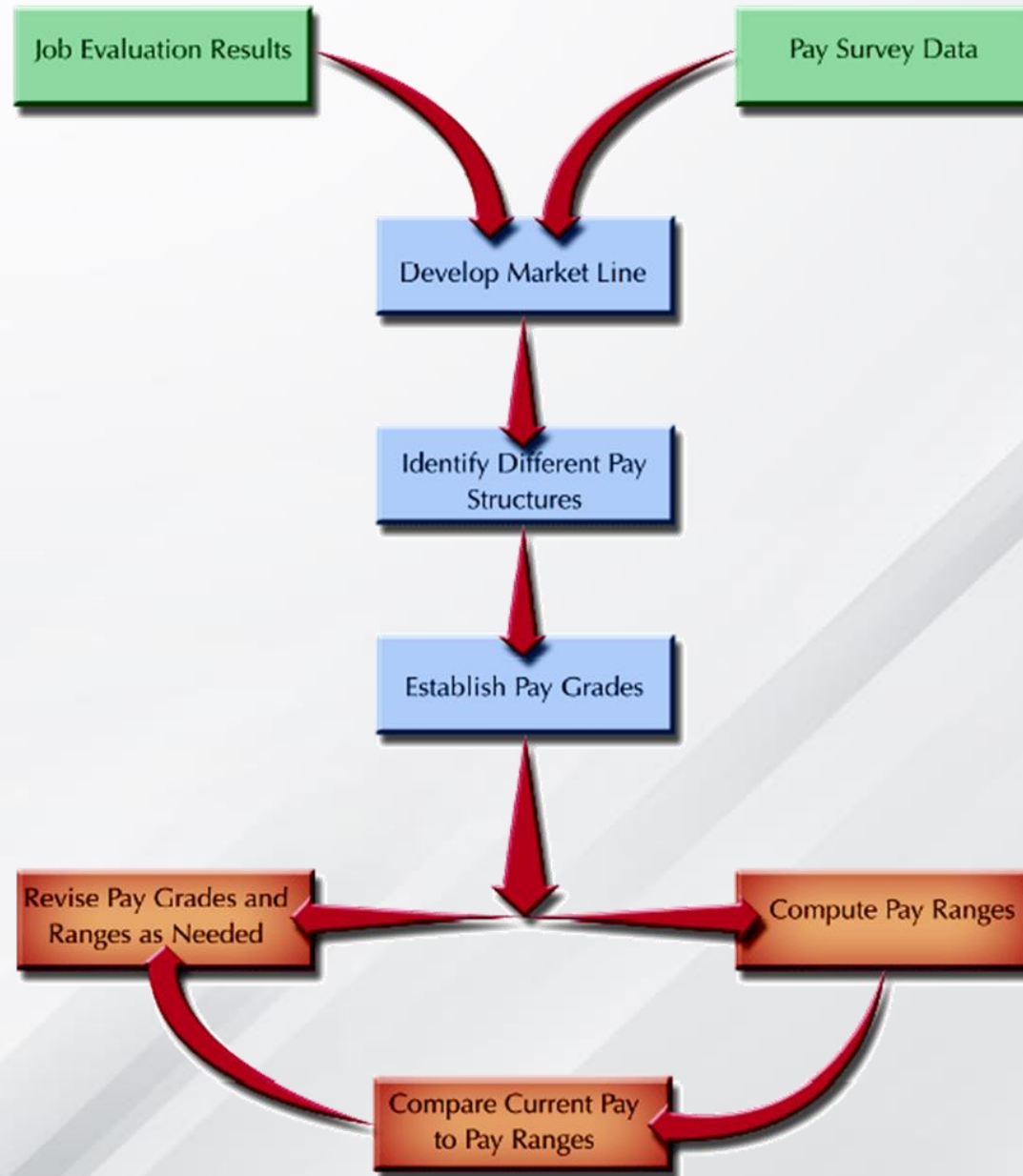


FIGURE 12-5

PAY STRUCTURES

- **Market Line**

- The line on a graph showing the relationship between the job value, as determined by job evaluation points, and pay survey rates.

- **Common Pay Structures**

- Hourly and salaried
- Office, plant, technical, professional, managerial
- Clerical, information technology, professional, supervisory, management, and executive

PAY STRUCTURES CONT.

○ **Pay Grades**

A grouping of individual jobs having approximately the same job worth.

○ **Broad banding**

The practice of using fewer pay grades having broader pay ranges than in traditional systems.

○ **Benefits**

- Encourages horizontal movement of employees
- Is consistent with trend towards flatter organizations
- Creates a more flexible organization
- Encourages competency development
- Emphasizes career development

Example of Pay Grades and Pay Ranges

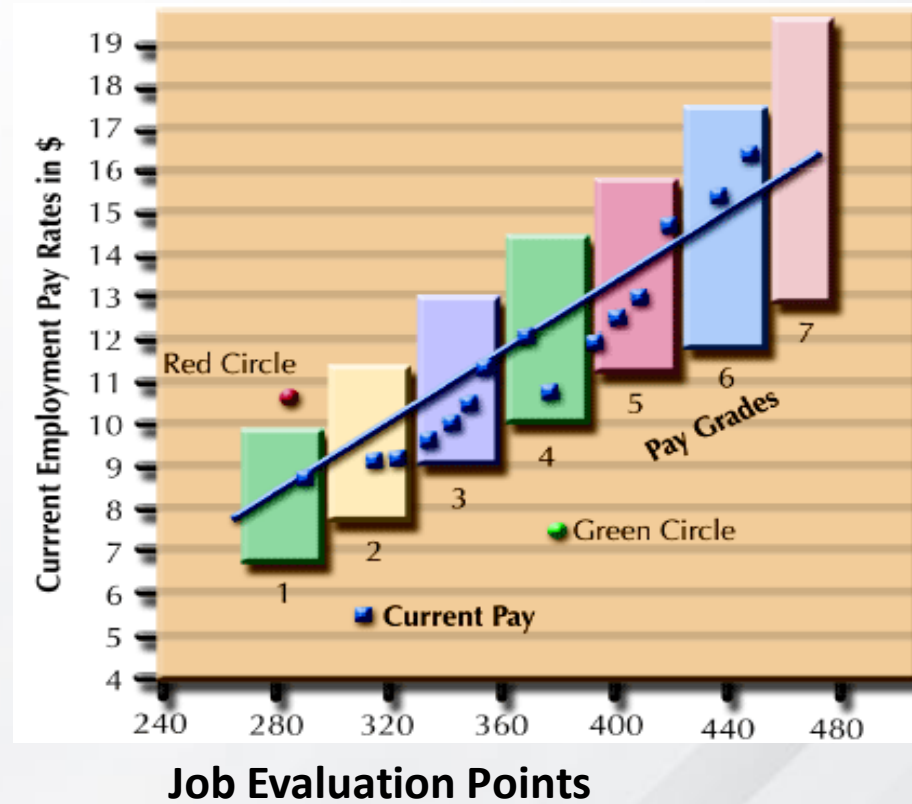


FIGURE 12-6

Grade	Point Range	Minimum Pay	Midpoint Pay	Maximum Pay
1	Below 300	6.94	8.50	10.06
2	300-329	7.96	9.75	11.54
3	330-359	8.98	11.00	13.02
4	360-389	10.00	12.25	14.50
5	390-419	11.01	13.49	15.97
6	420-449	11.79	14.74	17.69
7	Over 450	12.79	15.99	19.18

Pay Rate Issues

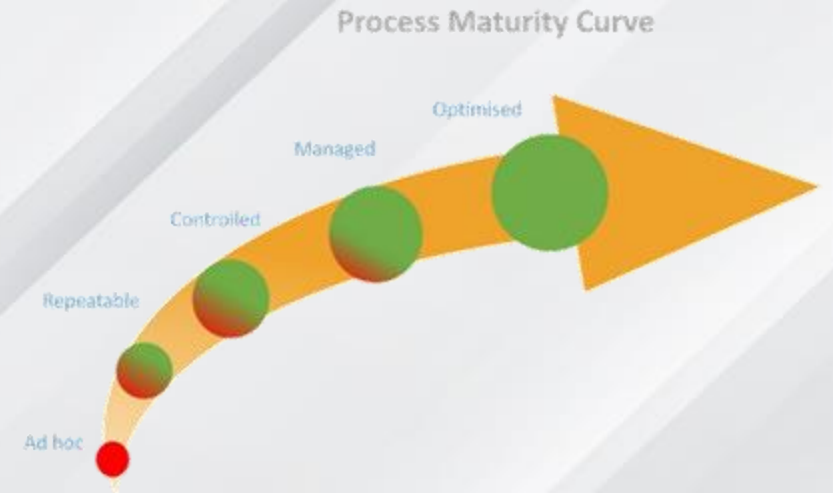
- **Rates Out of Range**
 - **Red-Circled Employees**
 - An incumbent (current job holder) who is paid above the range set for the job.
 - **Green-Circled Employees**
 - An incumbent who is paid below the range set for the job.
- **Pay Compression**
 - A situation in which pay differences among individuals with different levels of experience and performance in the organization becomes small.

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Issues Involving Pay Increases

- **Seniority**
 - Time spent in an organization or on a particular job.
 - Used to determine eligibility for organizational rewards and benefits.
- **Maturity Curve**
 - A curve that depicts the relationship between experience and pay rates.
 - Assumption is that as experience increases, proficiency and performance increase.



Issues Involving Pay Increases Cont.

- **Cost-of-Living Adjustments (COLA)**

A percentage increase in wages that allows employees to maintain the same real wages in a period of economic inflation. Adjustments are tied to changes in an economic measure (e.g., the Consumer Price Index).

- **Lump-Sum Increases (LSI)**

A one-time payment of all or part of a yearly pay increase. Lump-sum payments do not increase base wages

Part 4: Compensating Human Resources

Variable Pay and Executive Compensation

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Chapter
13

Learning Outcomes

After you have read this chapter, you should be able to:

- Define variable pay and identify three elements of successful pay-for-performance plans.
- Discuss three types of individual incentives.
- Discuss why profit sharing and employee stock ownership are common organizational incentive plans.
- Explain three ways that sales employees are typically compensated.
- Identify the components of executive compensation.

VARIABLE PAY: INCENTIVES FOR PERFORMANCE

- **Variable pay** Compensation linked to individual, group/team, and/or organizational performance.
- **The foundation of variable pay rests on several basic assumptions:**
 - Some people perform better and are more productive than others.
 - Employees who perform better should receive more compensation.
 - Some of employees' total compensation should be tied directly to performance and results.
 - Some jobs contribute more to organizational success than others.

Developing Successful Pay-for-Performance Plans

Employers adopt variable pay or incentive plans for a number of reasons.

- Link strategic business goals and employee performance.
- Enhance organizational results and reward employees financially for their contributions.
- Reward employees and recognize different levels of employee performance.
- Achieve HR objectives, such as increasing retention, reducing turnover, recognizing training, or rewarding safety.

Examples of Incentives

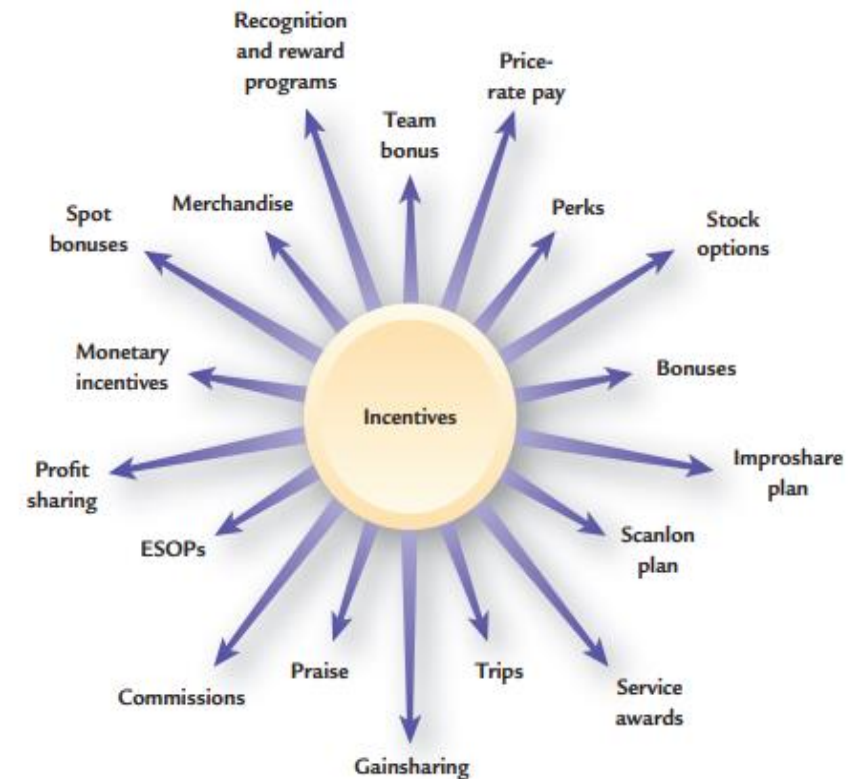


FIGURE 13-1

Factors Affecting Variable Pay Plans

Does the plan fit the organization?

In the case of pay-for-performance plans, one size does not fit all. For a plan to work, it must be linked to the objectives of the organization.

Variable Pay Plan Success

Are the right behaviors encouraged by the plan?

Variable pay systems should be tied to desired performance. Employees must see a direct relationship between their efforts and their financial rewards.

Is the plan being administered properly?

A variable pay plan may be complex or simple, but it will be successful only if employees understand what they have to do to be rewarded.

Types of Variable Pay Plans

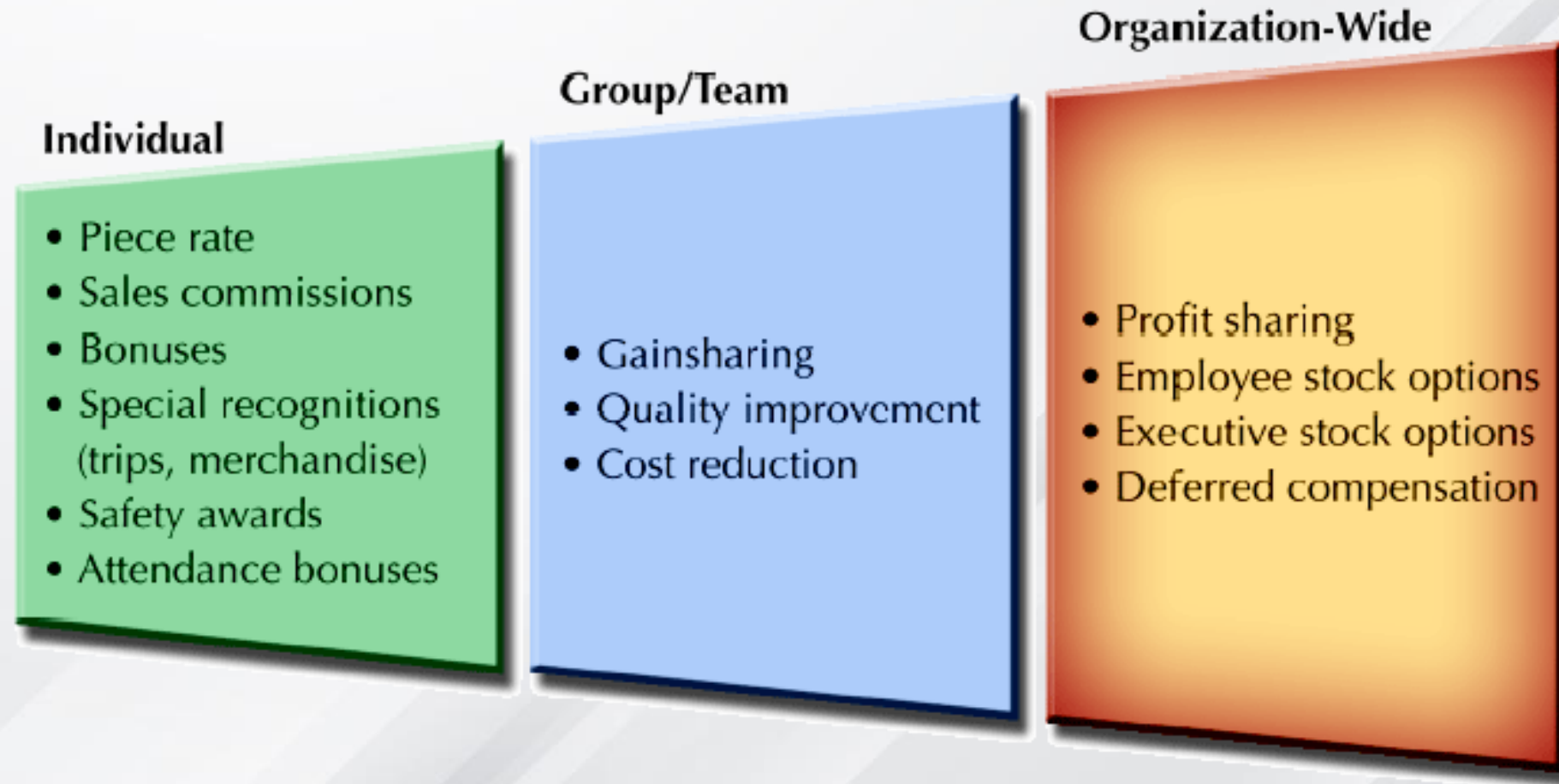


FIGURE 13-2

INDIVIDUAL INCENTIVES

Piece-Rate Systems

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- **Straight Piece-Rate Systems**

- Wages are determined by multiplying the number of pieces produced by the piece rate for one unit.

- **Differential Piece-Rate Systems**

- Employees are paid one piece-rate for units produced up to a standard output and a higher piece-rate wage for units produced over the standard.

Chapter
13**INDIVIDUAL INCENTIVES CONT.**
Bonuses and Special Incentive Programs

- **Bonus**

A one-time payment that does not become part of the employee's base pay.

- **Awards**

Cash or merchandise used as an incentive reward.

- **Recognition Awards**

Recognition of individuals for their performance or service to customers in areas targeted by the firm.

- **Service Awards**

Rewards to employees for lengthy service with an organization.

INDIVIDUAL INCENTIVES CONT.

Types of Sales Compensation Plans

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➤ Salary Only

- All compensation is paid as a base salary with no incentives.

➤ Straight Commission

- Compensation is computed as a percentage of sales in units or dollars.
- To offset this insecurity, some employers use a draw system
- Draw system make advance payments against future commissions to salesperson.

➤ Salary Plus Commission or Bonus

- Compensation is part salary for income stability and part commission for incentive.

Factors for Successful Variable Pay Plans



FIGURE 13-3

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Types of Group/Team Incentives

- **Group/Team Results** : Pay plans for groups/teams may reward all members equally on the basis of group output, cost savings, or quality improvement.
- **Gainsharing**: System of sharing with employees greater-than-expected gains in profits and/or productivity. Also called team sharing or goal sharing.



What is Gains Sharing?



"Congratulations. Your team members increased productivity by 50%. This year you all get a fat bonus!"

An incentive plan to motivate workers to boost productivity and reduce waste

ORGANIZATIONAL INCENTIVES

Profit Sharing

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- **Profit Sharing**

A system to distribute a portion of the profits of the organization to employees.

- **Primary objectives**

- Improve productivity
- Recruit or retain employees
- Improve product/service quality
- Improve employee morale

- **Drawbacks**

- Disclosure of financial information
- Variability of profits from year to year
- Profit results not strongly tied to employee efforts

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ELEMENTS OF EXECUTIVE COMPENSATION

- **Executive Salaries:** vary by the type of job, size of organization, industry, and other factors. In some organizations, particularly non-profits, salaries often make up 90% or more of total compensation.
- **Executive Benefits :** Many executives are covered by regular benefits plans that are also available to non-executive employees, including traditional retirement, health insurance, and vacation plans
- **Executive Perquisites (Perks):** In addition to the regular benefits received by all employees, executives often receive benefits called perquisites. Perquisites (perks) are special benefits— usually non-cash items— for executives.
- **Annual Executive Incentives and Bonuses :** for executives can be determined in several ways. One way is to use a discretionary system whereby the CEO and the Board of Directors decide.
- **Performance Incentives:** Long Term vs. Short Term Use of executive performance-based incentives tries to tie executive compensation to the long-term growth and success of the organization.

SUMMARY**Chapter 12: Total Rewards & Compensation**

- Nature of Compensation
- Total rewards components
- Compensation Philosophies
- Compensation System Design Issues
- Compensation Administration Process

Chapter 13: Variable Pay and Executive Compensation

- Variable pay: incentives for performance
- Developing Successful Pay-for-Performance Plans
- Factors Affecting Variable Pay Plans
- Types of Variable Pay Plans
- Individual Incentives
- Organizational Incentives
- Types of Group/Team Incentives
- Elements Of Executive Compensation



Thank You