What is Compensation and Benefits?

- Compensation and benefits (Reward Management) deals with the strategies, policies and processes required to ensure that the contribution of people to the organization is recognized by both financial and non-financial means.

Objectives of a Reward System:

- To reward people according to the value they create
- To align reward practices with business goals and with employee values and needs
- To reward the right things to convey the right message about what is important in terms of behaviors and outcomes
- To help to attract and retain the high-quality people the organization needs
- To motivate people and obtain their engagement and commitment
- To develop a high-performance culture

The Reward philosophy

- The philosophy recognizes that, if human resource management (HRM) is about investing in human capital from which a reasonable return is required, then it is proper to reward people differentially according to their contribution (ie the return on investment they generate)

Rules of Reward Management:

- Distributive justice
  - People will feel that they have been treated justly if they believe that the rewards have been distributed in accordance with the value of their contribution, that they receive what was promised to them and that they get what they need.
- Procedural justice
  - The ways in which managerial decisions are made and reward policies are put into practice. The five factors that affect perceptions of procedural justice are:
    - The viewpoint of employees is given proper consideration
    - Personal bias towards employees is suppressed

- Thus, if management wishes to increase satisfaction on the job, it should be concerned with the nature of the work itself—the opportunities it presents for gaining status, assuming responsibility, and for achieving self-realization. If, on the other hand, management wishes to reduce dissatisfaction, then it must focus on the job environment—policies, procedures, supervision, and working conditions. If management is equally concerned with both satisfaction and dissatisfaction, then managers must give attention to both sets of job factors.
- The two-factor theory distinguishes between:
  - Motivators (e.g. challenging work, recognition, responsibility) that give positive satisfaction, arising from intrinsic conditions of the job itself, such as recognition, achievement, or personal growth .
  - Hygiene factors (e.g. status, job security, salary, fringe benefits, work conditions) that do not give positive satisfaction, though dissatisfaction results from their absence. These are extrinsic to the work itself, and include aspects such as company policies, supervisory practices, or wages/salary.
- Essentially, motivation factors are needed to motivate an employee to higher performance. Hygiene factors are needed to ensure an employee is not dissatisfied. Herzberg also further classified our actions and how and why we do them. For example, if you perform a work related action because you have to, then that is classed as movement, but if you perform a work related action because you want to, then that is classed as motivation.
- This theory highlights the importance of rewards systems and monitoring when and how employees are rewarded. Herzberg's theory implies that simple recognition is often enough to motivate employees and increase job satisfaction.

Internal & External Equity

- The internal and external analysis allows an organization to evaluate the compensation plan based on the fairness of employee compensation.
- The impact of the internal and external forces is important when dealing with pay structure.
- Equity pay is ensuring that all parties involved are receiving the same benefits based on the internal and external factors.

- The external wage comparisons can be the same union, geographical area, job similarity, certifications, or the size of the company.
- Human Resource Managers is responsible to assess the outside competition properly in regard to the above mentioned to maintain a competitive advantage with similar companies.
- An employee looking to join the organization can easily find the mean or medium pay based on the geographical area and job description.
- An evaluation of the marketing prices can also be used to retain the employees already on staff.
- Competitive business will seek out employees from other company, so it is important to ensure that the organization does not allow the competition to steal their employees.
- This is referred to as poaching or raiding.

♦ **<u>Advantages and disadvantages</u>**

- The advantages of internal and external factors are an important tool used to define and implement a solid base pay, cash compensation, or benefits.
- Internal equity allows the organization to warrant an equal pay among the employees based on the pay scale or performance.
- The disadvantage of internal equity is the perception of the employees.
- An employee can perceive that he or she is doing the same job as another employee and should receive the same pay.
- Perception of employees may differ from the perception of the employers.
- The employee may feel that his or her individual performance is the same or above in comparison to the employees who are performing. It creates tension and lowers morale within the workplace.

- *Pay stabilizes when demand equals supply at the 'market clearing' or 'market equilibrium' wage. This is sometimes known as the theory of equalizing differences*
- *Classical theory is based on 'other things are equal' and that a 'perfect market' for labour exists.*
- *In the real world, of course, other things are never equal. And there is no such thing as a universally perfect market*

Human capital theory

- *conceptualizes workers as embodying a set of skills which can be "rented out" to employers*
- *For the employee, the expected returns on human capital investments are a higher level of earnings, greater job satisfaction and, at one time, but less so now, a belief that security in employment is assured*
- *For the employer, the return on investment in human capital is expected to be the improvements in performance, productivity, flexibility and capacity to innovate that should result from enlarging the skill base and increasing levels of competence.*

Efficiency wages theory

- *Efficiency wages theory proposes that firms will pay more than the market rate because they believe that high levels of pay will contribute to increases in productivity by motivating superior performance, attracting better candidates, reducing labour turnover and persuading workers that they are being treated fairly.*

Agency theory

- *Agency theory, or principal agent theory, in its purest form recognizes that in most firms there is a separation between the owners (the principals) and the agents (the managers).*
- *The employment relationship may be regarded as a contract between a principal (the employer) and an agent (the employee). The payment aspect of the contract is the method used by the principal to motivate the agent to perform work to the satisfaction of the employer*
- *It is desirable to operate a system of incentives to motivate and reward acceptable behaviour.*

- *Conduct market rate survey*
- *Design the pay structure*
- *Implement*

♦ *Advantages*

- The value of the job is expressed in monetary terms.
- Can be applied to a wide range of jobs.
- Can be applied to newly created jobs.

♦ *Disadvantages*

- *The pay for each factor is based on judgments that are subjective.*
- *The standard used for determining the pay for each factor may have built-in biases that would affect certain groups of employees (females or minorities).*

<u>Ranking of a single factor method:</u>

- The simplest and most common technique for job evaluation employs a system whereby human resources associates or consultants rank jobs in an organization based on a single factor, such as difficulty or education required to effectively perform the job. They then base compensation on ranking order with the highest ranked position earning the highest pay. This least expensive method of job evaluation works well for smaller businesses with tight budgets. Although this method can prove effective, its analytical system does not reach deep enough to determine other things associated with job evaluation, such as the value of the job to the individual organization or experiential competencies necessary to properly perform the job.

<u>Factor Comparison</u>

- Factor comparison, a sophisticated, yet time-consuming method, utilizes the techniques found in several job evaluation schemes. The first step in factor comparison involves assessing each job based on characteristics used in the point method, but without assigning points. Next, evaluators analyze their findings against the market rate of pay for the compensation factors ranked in the first step. Finally, they establish external

- *It is not infrequent for organizations to have overlapping pay scales, that is, where the maximum of the lower pay scale or range is higher than the minimum of the next pay scale. Granting Overlap provides managers with flexibility to shift employees to higher grades when promoted without an overly generous pay rise, however too much overlap will lead to pay unfairness.*

Pay Range Design:

- *List the jobs placed within each grade on the basis of job evaluation*
- *Establish the actual rates of pay of the job holders*
- *For each grade, set out the range of pay for job holders and calculate their average or median rate of pay*
- *Obtain information on the market rates for benchmark jobs where available*
- *Agree policy on how the organization's pay levels should relate to market rates*
- *Compare the practice and market reference points in each range and decide on the range reference point*
- *Examine the pay differentials between reference points in adjacent grades*
- *Decide on the range of pay around the reference point*
- *Decide on the extent, if any, to which pay ranges should overlap*
- *Review the impact of the above pay range decisions on the pay of existing staff in order to calculate implementation costs*
- *Calculate the costs of bringing them up to the minimum*
- *Review the decisions made on the grade structure and pay reference points and ranges*

Contingent Pay, Alternatives, and Effective

- *The term 'contingent pay' is used to describe any formal pay scheme that provides for payments on top of the base rate that are linked to the performance, competency, contribution or skill of people.*
- *Contingent pay can apply to individuals (individual contingent pay) or teams, or it can operate on an organization-wide basis.*
- *It is either consolidated in the base rate so that pay progresses within a pay range or it is paid as a non-consolidated cash bonus (the latter arrangement is called 'variable pay').*