SHRM Compensation and Benefits

Module 9: Establishing Pay Rates



Module 9: Establishing Pay Rates



Time:  2 minutes

Running time: 2 minutes

**Objective**: Introduce the topic of Module Nine: Establishing Pay Rates

**Description**:  Introduction to the topic and why it is important to compensation and benefits

**Instructional Method**: Lecture/ice breaker

**Script:**

How does an employer know what to pay employees and how does an organization go about determining the compensation rates of competitors? Establishing pay rates for each position in an organization is critical to the success of an organization as compensation rates are directly tied to an organization’s ability to attract and retain employees. In this module, we will discover the nuts and bolts of establishing pay rates within an organization.

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Time:  2 minutes

Running time: 4 minutes

**Objective**: Introduce the learning objectives.

**Description**: Show the objectives.  Answer any questions.

**Instructional Method**: Lecture

**Script**:

Here are the objectives for this module:

* Define terms related to establishing pay rates.
* Evaluate various types of external compensation research.
* Differentiate between various types of internal compensation research.
* Identify the difference between exempt and non-exempt employees.
* Generate current compensation data from relevant sources.

**Facilitator Notes:**

Use the objectives topics to create evaluation for the review.

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Time:  15 minutes

Running time: 19 minutes

**Objective**: Define key terms related to establishing pay rates

**Description**: Match Key terms to the correct definition.

**Instructional Method**: Game

**Script**:

Let’s play a game to define some key terms used in the compensation and benefits profession.

**Exercise**:  Key terms

1. Have students write numbers 1 – 16.
2. Show the slide
3. Read a definition (mix them up)
4. Have students choose the letter (term) for the key term.
5. Give them the answers.

**Define Terms:**

**1.** [**Benchmark job**](https://www.youtube.com/watch?v=-j_XeAl76Uc)- A job (or group of jobs) that is typical or representative of the position

     that is used for making internal and external pay decisions.

**2.** [**Salary Survey**](https://www.youtube.com/watch?v=YkMdzhVTRcI)- A market competition evaluation of the pay rates of similar positions to

     determine external pay equity.

**3.** [**Job Evaluation**](https://www.youtube.com/watch?v=Dckn3i35aWY)-  A method of establishing different pay rate within an organization that

      includes job classification, examination of the comparable worth of the jobs, and

      internal and external labor market factors.

**4.** [**Compensable Factors**](https://www.youtube.com/watch?v=Wf0g0K329y0&t=13s)- the knowledge, skills, abilities and other qualities identified in

     the job description that an employee must possess in order to perform their job duties.

     These factors also include working conditions, level of responsibility, and geographic

      location of a job. They must be job-related, and accurately reflect the job duties.

**5.** [**Job Classification**](https://www.youtube.com/watch?v=5DSaNVMUDFQ&t=16s)- “Job evaluation method that involves slotting job descriptions into a

     series of classes or grades that cover the range of jobs and that serve as a standard

     against which the job descriptions are compared” (Milkovich, 2019, p. 708).

**6.** [**Point-Factor Method**](https://www.youtube.com/watch?v=L07rWAQJAoY&t=4s)- Requires users to choose compensable factors and rank jobs

     according to their relative value to the organization.

**7.** [**Ranking Method**](https://www.youtube.com/watch?v=4HBxRczOzM0)- A method for establishing the relative worth of a job to an

      organization.

**8.** [**Classification Method**](https://www.youtube.com/watch?v=5DSaNVMUDFQ&t=16s)- Classifies employee according to skill, education, & experience

     levels.

**9.** [**Comparable Worth**](https://www.youtube.com/watch?v=YOvQS_EvD4c)- “A policy that women performing jobs judged to be equal on some measure of inherent worth should be paid the same as men, excepting allowable differences, such as seniority, merit, production-based pay plans, and other non-sex-related factors. Objective is to eliminate use of the market in setting wages for jobs held by women” (Milkovich, 2019, p. 708).

**10.** [**Internal Alignment**](https://www.youtube.com/watch?v=gyfQUduTB3Y)- The way that jobs are compensated within an organization that

       indicates that similar jobs with similar skill rates are being compensated at similar

       rates.

**11.** [**Exempt employee**](https://www.dol.gov/sites/dolgov/files/WHD/legacy/files/fs17a_overview.pdf)- An employee who is exempt from overtime under the Fair Labor

       Standards Act.

**12.** [**Nonexempt employee**](https://www.dol.gov/agencies/whd/flsa)- An employee who is entitled to overtime compensation at 1.5

       times their base salary for hours worked exceeding 40 in a work week.

**13.** [**Broadbanding**](https://www.youtube.com/watch?v=V1phQVXv6d0)- Occurs when multiple salary grades are pulled into a smaller number of

       pay grades with broader ranges.

**14.** [**Pay Ranges**](https://www.youtube.com/watch?v=nzgCy7j-k-Y&t=1s)- Pay ranges are the steps within a specific pay grade that organizations establish to reflect a difference in skills, seniority, education, and/or experience. It’s not uncommon to have an entry-level pay range, and mid-level pay range, and an experienced pay range, all in one pay grade.

**15**. [**Pay Grades**](https://www.youtube.com/watch?v=nzgCy7j-k-Y&t=1s)- A pay grade is a group of jobs with similar difficulty and value to the

       organization as determined by job evaluation.

**16.** [**Job Families**](https://www.onetonline.org/find/family)- Group of employees such as executive, managerial, professional, technical, clerical, and craft jobs which represent distinct job families. Within each of these will fall several ranges and/or pay grades.



Time:  6 minutes

Running time: 25 minutes

**Objective**: Identify the difference between exempt and non-exempt employees.

**Description**: Discuss the differences between exempt and nonexempt and how pay structures are created.

**Instructional Method**: Lecture - Large group Discussion

**Script**:

When designing pay levels and structures, we must consider several important details.

As we learned in the last exercise, an employee who is exempt from overtime under the Fair Labor Standards Act is exempt.

An employee who is entitled to overtime compensation at 1.5 times their base salary for hours worked exceeding 40 in a work week is nonexempt.

**Ask**:

* What are some professions that are usually nonexempt?
* Which are exempt?

**Facilitator Notes:**

Discuss the differences between exempt and nonexempt and how pay structures are created.

1. [**Exempt or nonexempt**](https://www.dol.gov/sites/dolgov/files/WHD/legacy/files/fs17a_overview.pdf)- Every job in your organization must be identified as Exempt or Nonexempt. These decisions should have happened during the job analysis/job description phase. Some organizations use a separate pay scale for exempt employees so that there is less room for misinterpretation between classes of employees. It is, however, a good idea to express salaries consistently throughout the organization, so we recommend one pay scale that includes every position.
2. **Establish job families**- The point is to place similar jobs from across the organization into job families, so they will be easier to compare and compensate fairly.
3. **Determine market competitive pay line**- Is your organization going to lead, lag, or match the market? How does this tie into organizational strategy?
4. **Pay Grades and Ranges**- How many pay grades does your organization want to manage? How many does it need in order to place jobs into appropriate pay ranges? The pay grades should be broad enough to cover similar positions and have sufficient pay ranges within it to account for experience, time on the job, and COLA increases for employees.
5. [**Pay for Performance**](https://www.youtube.com/watch?v=FjRfhZvWV5E&t=27s)- We will discuss this in-depth in Module 10, but employers must determine if they want to allow any type of pay for performance plan in the overall compensation design.

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Time:  10 minutes

Running time: 35 minutes

**Objective**: Evaluate various types of external compensation research.

**Description**: Discuss the 2 ways to determine if your pay rates are externally competitive via research.

**Instructional Method**: Lecture

**Script**:   The only way to determine if your pay rates are externally competitive is by doing research. This includes several steps:

1. **Benchmark Jobs**- before you can do any external research, you must identify benchmark jobs.
2. [**Salary Survey**](https://www.youtube.com/watch?v=OQubN4NJNu8)**-** Once you have selected the benchmark job in your organization that you want to use for external comparison, it’s time to use those benchmarks to compare compensation rates with your competitors.

**Facilitator Notes:**

**Benchmark Jobs**

**a**. **Select benchmark jobs-** These are comparable positions outside your organization. Compare job descriptions first. Make sure you are comparing objectively as you will use these outside jobs to evaluate the value of your own positions. The time and energy you spend here will be rewarded later on. Get your matches as close as possible so that you are comparing similar KSAO’s.

**b.** **Choose compensable factors-** Use the 4 universal factors first (skill, effort, responsibility, and working conditions). How many compensable factors you choose depends largely on how many are needed to accurately reflect the essential elements of the job. Use a job analysis and job descriptions to make these decisions. It is always a good idea to have the compensable factors also be the essential functions of the position for ADA purposes.

**c.** **Define compensable factor degrees-** Each compensable factor must be broken down into levels or degrees so that the level of proficiency can be determined. This is the area where an entry level administrative assistant would make a lower wage than a more experiences administrative assistant even though they would be in the same pay range. You MUST write out these degree statements so that they are clear and support clear differences in requirements. For example: An Administrative Assistant 1 might be the entry-level degree where every clerical worker enters your organization. Great. But you have 4 levels of Administrative Assistant. How does an employee move from one level to the next? What are the differences in requirements between level 1 and level 2? Having clear degree statements will make your job of educating your employees much easier and will contribute to preparing employee performance evaluations and improvement plans.

       Determine the weight of each compensable factor- This is where you determine

        which compensable factors are most important to the overall job.

       For example, using the 4 universal factors, you might decide that:

- skill is worth 50% of the job                                                                                                                                                                                                      - responsibility is worth 15%                                                                                                                                                                                                                 - effort is worth 25%

* working conditions are worth 10%

·  (P.S.) These weights are also helpful in creating personnel evaluation rubrics (module 10)!

But how do you decide? This is another area where paired comparison ranking or alternation ranking can come in handy. If you take all the job duties for a position and have the review committee rank them in order of most and least importance to the position, then you can accurately assign levels of value to a compensable factor. It’s quick, easy, and can even be accomplished in a manner that makes it a game if you really want to get creative!

**d**. **Determine the point values for each compensable factor-** This is accomplished by assigning point values to each compensable factor up to a maximum level. As an example, if we use our 4 universal factors and determine that 100 would be the maximum point value. Based on our earlier decisions about CF weight in step 4, we can then do some simple math:

- Skill- (50%\*100) = 50 points                                                                                                                                                                                                           - Responsibility- (15%\*100) =15 points                                                                                                                                                                                           - Effort- (25%\*100) = 25 points                                                                                                                                                                                                         - Working Conditions- (10%\*100) = 10 points

Then, using the degrees you defined in step 3, assign a point value to each degree  using the lowest number of points to represent the lowest skill level.

**e**. **Verify compensable factory degrees and point values-** It’s always important to test and verify your point values. Use a committee and reach a consensus that works in terms of your organizational strategy. This type of committee should consist of both those who are highly familiar with the position and a devil’s advocate.

It is critical to identify someone in the organization who is good at playing Devil’s Advocate. They should be someone who gets along with most people so that their approach to asking the hard questions is not viewed negatively. Or you can switch off and assign someone that role in a team. Some people are better at challenging the consensus than others, but in the verification process, you NEED someone who can ask the hard questions and challenge “the way we’ve always done it.”

**f.**  **Evaluate all jobs-** Evaluate all jobs using the same method. Once you have decided which degree definitions (step 3) best fit your job, assign the relevant points. After all the points are totaled, it is easy to rank each of the jobs according to their value in the organization.

**2.** [**Salary Survey**](https://www.youtube.com/watch?v=OQubN4NJNu8)**-** Once you have selected the benchmark job in your organization that you want to use for external comparison, it’s time to use those benchmarks to compare compensation rates with your competitors.

1. **Choose organizations to** [**survey**](https://www.youtube.com/watch?v=vses9KkcW9Y)- These should be your competitors- companies who make the same product or perform the same service. It’s also a good idea to include a couple of ‘stretch’ organizations. These are organizations that are better than yours at doing what you do. Including their compensation information in the survey, it helps to see what your organization must do to make it to the next level.
2. **Identify comparable positions**- Using the benchmark jobs you previously identified, select similar positions within the competitors and note the pay rates they receive. Sometimes this information is hard to come by because not all organizations want to share that information, but in those states where pay transparency is the law, it should be relatively simple to obtain that information.
3. **Compare to published data sets**- Data from O\*Net and the BLS can also be used to compare to your pay rates. This is helpful because you can see both local and national pay rates for each of your benchmark jobs so you can more readily determine your organization’s level of pay competition.

Diagram

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Time:  10 minutes

Running time: 45 minutes

**Objective**: Differentiate between various types of internal compensation research.

**Description**: Have students decide which method they would use and why.

**Instructional Method**: Discussion

**Script**:

Now that the external research has been accomplished, the focus moves back to internal research and planning. Here are various types of internal compensation research.

Job evaluation allows employers to compare jobs against other jobs within the organization to determine their overall worth to the organization. The following steps will help in this process:

**Note**: After discussing each factor and the ranking…

**Ask**: Which method would you use to compare jobs against other jobs within your organization to determine their overall worth to the organization?

**Facilitator Notes:**

**a. Choose Compensable Factors-** Use the 4 universal factors first (skill, effort, responsibility, and working conditions). How many compensable factors you choose depends largely on how many are needed to accurately reflect the essential elements of the job. Use your job analysis and job descriptions to make these decisions. It is always a good idea to have the compensable factors also be the essential functions of the position for ADA purposes.

**b.** [**Job Ranking**](https://www.youtube.com/watch?v=z6Q7cMI1cXM&t=24s)**-** A common error in ranking is to forget that you are ranking POSITIONS, NOT THE PEOPLE IN THEM. Just because a position is currently filled by a rock star or a someone who really needs to be fired, don’t get sucked into ranking jobs according to the people currently filling them. Use the job analysis and job descriptions you created. Make sure your committee is warned about this ahead of time because it is a very easy mistake to get caught up in and could even lead to claims of discrimination! There are several types of ranking plans to choose from.

* 1. **Simple ranking plan-** Utilizes job descriptions to rank the jobs in order of importance on a single criterion. This can be the importance of the job in the overall organization, job difficulty, etc. This method works very well for small organizations that don’t have a wide variety of positions to rank.
  2. [**Paired Comparison ranking**](https://www.youtube.com/watch?v=1q2pCEFM-zA&t=1s)**-** Works well for larger employers with many different jobs to evaluate. This is best done with a committee of evaluators. In paired comparison, each job is paired up against every other job so that every possible combination is reviewed. For each pair, each committee member chooses which job has more value and gives that job with a point. After all the jobs have been evaluated, the numbers are tallied. The jobs with the most points are ranked as highest in value, the jobs with the lowest points are lower in value.
  3. [**Alternation ranking-**](https://www.youtube.com/watch?v=YYNi4I-5d7U)Also uses a committee and a comparison system but asks committee members to rank jobs at extreme ends of the spectrum. For example, the first round would ask the committee members to identify the most valuable position in the organization and the least valuable. Then, those two positions being ranked, they would be asked to identify the next most and least valuable positions, and so forth until all positions are ranked.

**c.** [**Job Classification**](https://www.youtube.com/watch?v=5DSaNVMUDFQ&t=16s)**-** Government employees are classified as GS-1 through GS-15 which are based on a ranking system that evaluates skill level, education, and work experience.

This type of system is fairly straight-forward, and an organization can have multiple classification systems within one organization. For example, an organization might have one classification system for exempt employees and another for non-exempt employees.

**d. Point-Factor Method**- The [explanation below is provided by SHRM](https://www.shrm.org/resourcesandtools/tools-and-samples/toolkits/pages/performingjobevaluations.aspx):

The point factor method is a commonly used quantitative technique. This approach breaks down jobs into compensable factors identified during a job analysis. Points are assigned to the factors, and a pay structure is established for the position.

Using a system for internal equity, such as the point factor system, forces an organization to quantify total points for each unique job, determining its true value to the company. This process often provides value beyond compensation, including benefits for recruitment, promotions and job design. However, designing a custom point-factor system may take additional time and resources and require assistance from senior management.

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Time:  5 minutes

Running time:50 minutes

**Objective**: Discuss how to create pay grades.

**Description**: Have students discuss creating pay grades using the methods in the previous exercise.

**Instructional Method**: Discussion - Optional video

**Script**:

Now that you have established which jobs are most important to your organization, identified which jobs are in the same job families, and identified what the external competition is, it is time to create pay grades.

When establishing pay grades and ranges, it is important to return to our conversation about compensable factors. Jobs with similar compensable factors should be grouped similarly.

This goes back to your decision of which method of job evaluation you chose to use.

* If you used the classification method, then your pay grades are already determined.
* If you used the ranking system, then the grades consist of whatever ranks you imposed on the system.
* If you used the point method, then each grade is determined by the number of points they receive.

**Ask**: How many pay grades should you have?

**Facilitator Notes:**

Video: 3:21 minutes [**Create Pay Grades**](https://www.youtube.com/watch?v=lrWoihnE3P4)

How many pay grades should you have?

*Answer*:

That depends on your organization. If you have a large company with many different types of jobs, then you will need more pay grades. A small organization might have only a few. It’s always a good idea to establish your pay grades with an equal point spread, just to make is easy to manage and understand. Remember, if your compensation plan is confusing, employees will be more likely to make claims of pay discrimination than if your plan is easy to understand.

Diagram

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Time:  5 minutes

Running time: 55 minutes

**Objective**: Decide which pricing system to use based on organizational type.

**Description**: Discuss pricing system based on organizational type.

**Instructional Method**: Lecture -Exercise

**Script**:

The size and organizational strategy of an organization will guide what type of pricing system is used.

**Facilitator Notes:**

**1. Single-rate System**- In a single-rate system, each job in the organization is paid a

       flat rate that is typically close to the external market rate. In this type of system

      there are no pay variances from this rate for education, skill, experience, etc.

**2. Comparable Worth**- Remember that jobs of comparable worth to the

       organization should be compensated at a comparable wage rate.

**3. Internal Alignment**- Recall that internal alignment of compensation is critical to

       avoid claims of discrimination. It refers to how much pay one job receives in

       comparison to other jobs and is tied to comparable worth.

Table

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Time:  5 minutes

Running time: 60 minutes

**Objective**: View pay ranges for different jobs.

**Description**: Show and describe how to create pay ranges.

**Instructional Method**: Lecture

**Script**:

Pay ranges are the steps within a specific pay grade that organizations establish to reflect a difference in skills, seniority, education, and/or experience. It’s not uncommon to have an entry-level pay range, and mid-level pay range, and an experienced pay range, all in one pay grade. These foundational decisions will help you defend your pay practices if you are ever accused of pay discrimination.

Jobs are distributed along the pay grade based on the scores from the job evaluation. Individual employees are then distributed along the pay range within each pay grade based upon an established policy that acknowledges their individual KSAO’s.

Remember, you have to continue to keep the range of your competitors in mind as you develop your ranges. This becomes a delicate balance between internal equity, external competitiveness, opportunity for growth and development, and legal compliance.

It’s not uncommon to have a 30-40% range in any given pay range. This provides ample opportunity to establish a starting baseline, a mid-point, and a maximum range. Each of these various levels provide an opportunity to justify salary differences based on compensable factors and not discriminatory factors.

Diagram

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Time:  3 minutes

Running time: 63 minutes

**Objective**: Understand broadbanding and pay grades.

**Description**: Explain a broadband salary structure.

**Instructional Method**: Lecture

**Script**:

  If an organization has a relatively flat structure without need for many pay grades, they can collapse some pay grades into a broader pay structure that has wider salary ranges. Broadband salary structures are not as sensitive to market pay changes as other pay structures are, but they lead to more transparency about compensation within the organization.

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Time: 10 minutes

Running time: 73 minutes

**Objective**: Generate current compensation data from relevant sources.

**Description**: Have students create short presentations and present to the class.

**Instructional Method**: Pair and share discussions, exercises, homework

**Script:** The CEO has just asked you to bring her some examples of the types of salary data you can get for free on external market competition. Create a short presentation identifying at least three sources of free market pay data, using the HR Manager position as an example.

Exercise:

1. Pair students
2. Have students read the spotlight (on the slide) and identify 3 sources current compensation data for a HR Manager.
3. Have students discuss the sources and why they chose those sources.

**Facilitator Notes:**    
  
**Discussion Prompts:**

1. What steps do you think you could take to determine what pay rates should be if your organization is newly-formed and you don’t have any real market competition because you are also a new industry?
2. How much transparency should an organization provide to employees in terms of how the pay plan is structured and aligned?

* Read the article, [These are the 25 large companies offering the best compensation](https://www.businessinsider.com/large-companies-best-compensation-highest-wages-salaries-comparably-ranking-2021-10) by Madison Hoff. Choose one or two companies and research what they do and why they are considered the best.

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Time:  17 minutes

Running time: 90 minutes

**Objective**: Review main points in this module.

**Description**:  Be sure that students have a fun way to remember the material.

**Instructional Method**: Game – Review

**Script**:

Let’s see how much we remember about this module.

**Facilitator Notes:**

Review Exercise:  Create a fun game to review the material.  Remember to use the objectives to measure learning:

* Define terms related to establishing pay rates.
* Evaluate various types of external compensation research.
* Differentiate between various types of internal compensation research.
* Identify the difference between exempt and non-exempt employees.
* Generate current compensation data from relevant sources.

Ideas:

* Have each student submit a question on a piece of paper, crumple it up and toss it in a bucket (clean wastebasket), Instructor will then read them and give points to each team with the correct answer.
* Any game show – Family Feud, Jeopardy, $10,000 pyramid, Password, Tic Tac Toe
* Extra credit quizzes

*Virtual*

There are many ways to review material virtually or in person.  Students can use their phones or computers to navigate to various online review websites.

A few are:

* Kahoot
* Quizlet