SHRM Compensation and Benefits

Module 3: Compensation Strategy A person sitting at a table

Description automatically generated with medium confidenceModule 3: Compensation Strategy



Time:  5 minutes

Running time: 5 minutes

**Objective**: Introduce the topic of compensation strategy.

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

**Instructional Method**: Lecture/ice breaker

**Script:**

How do we motivate our employees? Is it base pay? Incentives? Benefits? Opportunity for advancement? Flexible workplace? Work-life balance? Working remotely? The answer is: Yes. It is all of these things and much more. Understanding what makes your employees “tick” is crucial to the attraction and retention. What motivates one person won’t necessarily motivate another, but there are some basic rules of human motivation that we can apply to the workplace to help us better understand what motivates us.

Graphical user interface, application

Description automatically generated

Time:  2 minutes

Running time: 7 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 Compensation Strategy
* Analyze the role of compensation in strategic in business decisions
* Discuss the three types of compensation strategies
* Identify four steps for developing a total compensation strategy
* Explain how organizational strategy influences tactical HR decisions

**Facilitator Notes:**

Use the objectives topics to create evaluation for the review.

Text, chat or text message

Description automatically generated

Time:  7 minutes

Running time: 14 minutes

**Objective**: Define key terms for compensation and benefits

**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. The instructor will state the definition of each term.
2. Have students choose which term fits the definition.
3. Click to “light up” the correct answer.

*Virtual*

1. Use chat or annotate/stamp.
2. Read the definition and have students choose the term.

**Define Terms:**

**1. Business Strategy-** A set of identified goals and plan that organizations create in order to plan and prepare for how current and future business operations will take place.

**2. Strategic Compensation-** “refers to the design and implementation of compensation systems to reinforce the objectives of both HR strategies and competitive business strategies. Compensation and benefits executives work with the lead HR executive and the company’s chief financial officer (CFO) to prepare total compensation strategies” (Martocchio, 2019, p. 385).

**3. Pay Philosophy-** A pay philosophy outlines an organization’s approach to compensation. Organizations can lead, lag, or match the market.

**4. Pay Structure-** A pay structure is an outline of the differences in compensation between classes and type of employees. Employee compensation for all positions falls somewhere within the pay structure.

**5. Internal Alignment-** Internal alignment occurs when compensation levels between similar jobs is similar throughout the organization.

**6. Externally Competitive-** A compensation plan is externally competitive when is is matching the market pay scale for any particular position or industry.

**7. Lead the Market-** A compensation philosophy wherein an organization opts to pay the highest wages in the market. This attracts top talent, but costs are high.

**8.  Lag the Market-** A compensation philosophy wherein an organization opts to pay wages that are somewhat behind the market compensation for that position/industry. This results in attracting less talented employees but keeps costs lower.

**9.  Match the Market-** A compensation philosophy wherein an organization opts to pay wages that are similar to those being paid by competitors for a given position/industry.

Graphical user interface, text, application

Description automatically generated

Time:  8 minutes

Running time: 22 minutes

**Objective**: Discuss compensation strategy as it relates to other types of business strategy.

**Description**: Show questions and ask students about their company or the school.

**Instructional Method**: Discussion

**Script**:   Every organization needs a strategic plan. How will you know you’ve been successful if you don’t plan, set goals, and declare methods and strategies to meet those goals? The following questions are foundational questions that any organization needs to realistically answer as a part of strategic planning.

a.  Where is your company now?

b.  Where does your company want to be a year from now?

c.  Where does your company want to be in 5 years? 10 years?

d.  What does your organization need to do now to reach organizational goals in 1, 5, 10 years and beyond?

e.  How many employees do you expect to need to continue operations as usual?

f.  How many employees do you expect to need to develop a new product line? To open another location?

g. What KSAO’s will new employees need to have?

h. What technology will replace humans in our organization?

Diagram

Description automatically generated

Time:  15 minutes

Running time: 37 minutes

**Objective**: Using items given, students will discuss and decide how to establish a compensation strategy using a SWOT analysis as the tool.

**Description**: Have the students do the exercise and discuss how each item fits into a SWOT analysis and how it can be used to establish a compensation strategy.

**Instructional Method**: Exercise and large group discussion

**Script**:

The decisions about how to approach the job market are critical to your organization’s success. Without a clear understanding of the strengths, weaknesses, opportunities, and threats approaching not only your organization as a whole, but your compensation system specifically, there is no way to determine what the best strategy for attracting and retaining top talent will be.

**Exercise**:

1. Break the students into 9 groups.
2. Give each group one of the items below
3. Have each group decide how their item would fit in a SWOT analysis (5 minutes)  
   \*Be sure they realize that it can fit in multiple places depending on the organization.
4. Have each group choose a spokesperson to summarize their discussion for the large group. (1 minute each)

**Facilitator Notes:**

**Note**: You may wish to put each numbered item on a piece of paper to give to each group (if F2F)

For virtual: show the list below and have each group copy their item before going into a breakout room.

1. **Impact on ability to recruit/hire/retain employees**- Your compensation strategy has tremendous impact on your ability to recruit/hire/retain employees. Is your philosophy to pay more than your competitors to get the top talent, or is it to try to stay competitive but not actually pay the highest wages in the industry? No matter the choice the organizations make, there are repercussions for each strategy.
2. **Discuss how this relates to overall business strategy-** The overall business strategy is impacted by the compensation strategy because every organization accomplishes its mission through people (aka employees). If you want to be known as a leading innovative organization, then leading the market with compensation will attract the best and brightest candidates which will translate into highly innovative cultures. If you cannot afford to set the market with compensation, then you have to balance the organizational strategy to hire the best employees you can afford and plan on maintaining a certain market share, but not expecting to be the leader in the industry.
3. **Using benefits to complement/compensate for higher pay to attract and retain employees**- If your organization cannot afford to pay the highest wages in the industry, it might be able to compensate for the lack of base compensation by offering a better benefit offering. Maybe if your organization can offer stock options to compensate for the inability to pay quite as much as your competitors or health insurance for family members at no cost to the employee. These types of incentives are frequently more valuable to some employees than higher rates of pay, but that depends very much on what the employee considers valuable. Having a variety of benefit offerings also make them more attractive.
4. **Lead the market-** If your organization decides to lead the market, you will likely get the highest quality employees because you are able to woo them away with your excellent base salary. If you can offer an outstanding benefits package as well, then your organization will likely have very high labor costs but can also expect the experts you’ve hired to produce high returns.
5. **Lag the market-** If you decide to lag the market as an organization, then you are likely to keep labor costs lower, but may also have trouble attracting top talent.
6. **Offer amazing benefits but lower pay-** Municipal governments have used benefits to attract and retain quality employees for many decades. The pay is much less than most professionals could make in the public arena, but the retirement is outstanding, the benefits historically low-cost, and the turnover very low.
7. **Offer few benefits but higher pay-** Some organizations put all their resources into salaries and encourage employees to purchase their own healthcare in the market. This became more common after the [Affordable Care Act](https://www.healthcare.gov/glossary/affordable-care-act/) went into effect.
8. **Profit sharing-** Does your organization want to share the wealth with employees? Not all organizations do so, but those who do report a sense of ownership among employees that directly contributes to bottom-line savings.
9. **Different compensation/benefit plans for different classifications of employees-** Most organizations offer some variety in their compensation plans, perks, and benefits based on the level of the employee. For example, hourly employees might have one set of benefit options, while middle management has a different set, and upper management has an even different set. This is also true for compensation plans overall.

Graphical user interface, text, application, email

Description automatically generated

Time:  1 minutes

Running time: 43 minutes

**Objective**: Transition from Compensation Strategy to Pay Structure.

**Description**: Describe how to move from the compensation strategy to the pay pay structure.

**Instructional Method**: Transition

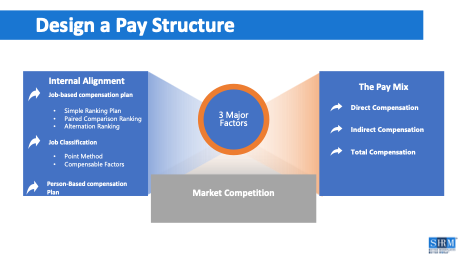
**Script**:

 From the compensation strategy, the pay philosophy is established. Here are some of the questions a pay philosophy should address, but they are not exhaustive by any means.

From the pay philosophy, a pay structure is created.

* How will you compete externally?
* How will you promote and compensate employees internally?
* How will pay structures/grades be determined?
* What measures are in place to ensure that pay discrimination doesn’t occur?
* How does the organization want to position itself in the market in terms of compensation and benefits and how does that trickle down into pay policies?

**Note**: From the pay philosophy, a pay structure is created.



Time:  5 minutes

Running time: 48 minutes

**Objective**: Describe the three major factors in determining a pay structure.

**Description**: Describe the process and different options used in designing a pay structure.

**Instructional Method**: Lecture

**Script**:

The concept of determining a pay philosophy consists of decisions about three major factors: Internal alignment, market competition, and the pay mix.

**Facilitator Notes:**

Design a Pay Structure

**1.** **Internal alignment**

There are a couple of approaches an organization can take to determine internal alignment, and the organizational strategy will likely drive these decisions. It is also completely possible to use a mix of job-based and people-based pay philosophies.

Internal consistency is important because it strongly impacts employee morale and retention and leads to more satisfied employees overall.

a.  **Job-based compensation plan**- One of the first tasks that must take place when creating a compensation plan is defining the value of individual jobs in relation to other jobs within the organization. Consider that within most organizations there exists various levels of employees within any specific job. For example, you might have a plumbing company and each crew has a foreman, a heavy equipment operator, and 6 laborers. Within the foreman category, you might have 3 levels of employee. An employee who works at the Foreman I level has a lower base rate than an employee classified as a Foreman II, and so forth. The employee can move from one level to another through longevity, achievement, merit, or obtaining new skills. Therefore, every organization must define the value of each job through job evaluation. We are going to discuss three common methods of job evaluation:

**1.**  [**Job Ranking**](https://www.youtube.com/watch?v=z6Q7cMI1cXM)

a. A 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.

b. [**Paired Comparison Ranking**](https://www.youtube.com/watch?v=1q2pCEFM-zA)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.

c. [**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.

    1. **\*\*\*Warning\*\*\*** 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 lead to claims of discrimination!

**2**. [**Job Classification**](https://www.youtube.com/watch?v=5DSaNVMUDFQ)**-** Government employees are classified as [GS-1 through GS-15](https://www.federalpay.org/gs/2022) which are based on a ranking system that evaluates skill level, education, and work experience. This type of system is 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.

1. [**Point Method**](https://www.youtube.com/watch?v=L07rWAQJAoY)- The Point Methodrequires users to choose compensable factors and rank jobs according to their relative value to the organization.

**b.**  [**Compensable factors**](https://www.youtube.com/watch?v=Wf0g0K329y0)are the knowledge, skills, abilities, and other qualities identified in the job description that an employee must possess 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

**3.**[**Person-Based compensation plan**](https://www.youtube.com/watch?v=OIBzb3xpY1w)**-** Compensation plans that are based on individual employee contributions in the form of employee knowledge, skills, and abilities is called Person-based or Skill-based compensation. These types focus on the rewards of compensation based on performance. This type of compensation plan attracts high performers who are compensated on the basis of the results they achieve, rather than a position they hold.

**2.**  **Market Competition**- How is your compensation plan competing in the market for your industry? If an organization hopes to remain competitive in the long run, it is imperative that it stay at least close to the market. If not, your employees will move on to organizations that can compete. It’s one thing to lag the market in compensation while you are a young start-up, just doing the best you can to survive, it’s another to consistently pay your employees substantially less than your competitors.

[Market Competitive Compensation](https://www.youtube.com/watch?v=NQJc5Le6x7k)

**3.**  [**The Pay Mix**](https://www.youtube.com/watch?v=gI18I7KEdmI)**-** The pay mix is the combination of direct and indirect compensation that organizations offer to employees as part of a total compensation package. Every organization must determine what combination of direct and indirect compensation will help achieve strategic goals and attract and retain quality employees. This can be a balancing act from year to year, especially during uncertain economic times like we are living in right now. Leave policies and practices should absolutely be updated to remain in compliance with updated laws.

**a.** [**Direct Compensation**](https://hrsoft.com/direct-vs-indirect-compensation/)**-** Payments made to employees for the time the

             work or the results they produce during a given time period.

**b.** [**Indirect Compensation**](https://hrsoft.com/direct-vs-indirect-compensation/)**-** Typically considered to be fringe benefits, items

              such as life and health insurance, gym memberships, and other types on

              non-monetary rewards provided to employees as a part of their total

              compensation package.

**c.** [**Total Compensation**](https://www.youtube.com/watch?v=asuWMK9Ixh8)**-** The total combination of direct and indirect

              compensation offered to an employee.

Graphical user interface

Description automatically generated with medium confidence

Time:  12 minutes

Running time: 60 minutes

**Objective**: Explain the major decisions that need to be made when determining a pay structure.

**Description**: Describe in detail the major decision that need to be made when designing a pay structure.

**Instructional Method**: Lecture

**Script**:

When designing a pay structure each organization must make some major decisions. Some of these decisions are:

**Facilitator Notes:**

**a.** F[**LSA Exemptions**](https://www.dol.gov/agencies/whd/fact-sheets/17a-overtime)**-** The new rule went into effect on January 1, 2020.

·  Every job in an 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 in the organization. You can express annual salaries in terms of hourly wages for consistency, just divide the annual salary by 2080 hours to determine the hourly rate for exempt employees.  This will help you classify your employees as exempt or non-exempt. There is an additional tool in the resources that links directly to the IRS.gov website that will help you correctly identify who is an employee and who is a self-employed subcontractor, as well as some other types of employees.

**b**.  **Job Families-** The next major decision is to establish job families. As you look across your organization, there are groups 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. The point is to place similar jobs from across the organization into job families, as they will be compensated similarly.

**c**.  [**Pay Grades**](https://www.youtube.com/watch?v=Bk1D3PUJXns)**-** When establishing pay grades, 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. How many pay grades should you have? 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.

**d**. [**Pay Ranges**](https://www.youtube.com/watch?v=Bk1D3PUJXns)**-** 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. Under the Colorado Equal Pay Act, some of the justifiable reasons for paying one employee more than another for performing essentially the same work in an established seniority system, performance differences, work locations, etc. 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 must 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.

**1**.  [**Pay for Performance**](https://www.youtube.com/watch?v=FjRfhZvWV5E)**-** Some organizations prefer to motivate employees through use of financial incentives tied to performance outcomes. These include any number of piece-rate plans that reward employees for the number of products they produce daily, bonuses for meeting deadlines, gaining new customers, referring new employees, meeting sales goals, and so forth. While money isn’t the only motivator, it’s certainly an important one. Organizations can choose to add additional compensation opportunities using pay for performance plans. These plans typically still have a normal structure in terms of pay grades and ranges, but certain positions may also have an additional pay scale used to incentivize the successful completion of a task. For example, a car salesperson might make minimum wage for every hour he or she works in the dealership. Some auto dealers have salespersons who work full-time, and others part-time. As such, they have different benefit options. Additionally, all salespersons receive a commission on the sale of each vehicle deal they close. It’s not uncommon to see a new salesperson at a lower commission rate than a more seasoned professional. Some dealerships may raise the commission rate in line with an established seniority program, or by number of vehicles sold, etc. Whatever method you choose, be certain that it is well-publicized and pay close attention to the perceived fairness of the plan. Employees who understand the system are less likely to feel they are being discriminated against.

**2**.  [**Benefits**](https://www.youtube.com/watch?v=L-_fun3yzSI)**-** Be sure you are familiar with the legally required benefits such as worker’s compensation, unemployment insurance, social security, Medicare, healthcare, and more recently, mandatory paid leave. Beyond these, it is up to individual employers to determine what benefit mix they want to offer that meets budget restraints and helps to attract and retain quality employees.

A picture containing chart

Description automatically generated

Time:  5 minutes

Running time: 65 minutes

**Objective**: Describe what roles an HR Professional plays when developing and deploying a compensation strategy.

**Description**: Describe in detail what roles an HR Professional plays when developing and deploying a compensation strategy.

**Instructional Method**: Lecture and discussion

**Script**:

As an HR professional, you could take on any number of roles as compensation strategy is developed and deployed. No strategy is able to be carried out without the establishment of policies and practices that are used to carry out that strategy.

**Facilitator Notes:**

* Usual roles that HR performs in the deployment of compensation strategy:

1.  Create policies and procedures to carry out the compensation strategy.

2.  Conduct research upon which compensation decisions are made.

3.  Identify employer needs in terms of:

a.  Number of employees available

b.  Quality of employees available

c.  Organization and Job Fit

d.  KSAO’s required for each position

e.  Maintenance and updating of job descriptions

f.   Job analysis

g.  Desirable behaviors

h.  Monitor labor market trends

4.  Monitor and measure total rewards metrics and benchmarks

a.  Insurance participation rates

**Note**: Can use for homework or for Instructor research/knowledge - Video explaining   [Compa-ratio](https://www.youtube.com/watch?v=pOBq39fGNtE) 7:46 minute

Graphical user interface, text

Description automatically generated

Time: 10 minutes

Running time: 75 minutes

**Objective**: Students will review the material by answering the questions on the slide.

**Description**: Students will review the material by answering the questions on the slide.

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

**Script:** Please answer these questions in your groups.

**Discussion Prompts:**

1. Several questions were presented to help determine what an organization’s pay philosophy actually is. Develop 3 more questions that an organization should consider when establishing a pay philosophy and cite your sources.
2. How does compensation strategy influence tactical HR decisions?

**HR Skills Exercises:**

Interview someone you know who works in management in an organization of your choice. Ask and record responses to the following questions:

1. Do you know what your organizational compensation strategy is?
2. Does your organization lead, lag, or match the market?
3. What makes people stay at your organization? Great benefits? Good pay? Flexible time off?

Record their responses and write a summary of what you learned that could be presented to the CEO of a competing organization.

**Facilitator Notes:**

* [**How to Define your Compensation Philosophy**](https://lattice.com/library/how-to-define-your-compensation-philosophy)

A picture containing logo

Description automatically generated

Time:  15 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 Compensation Strategy
* Analyze the role of compensation in strategic in business decisions
* Discuss the three types of compensation strategies
* Identify four steps for developing a total compensation strategy
* Explain how organizational strategy influences tactical HR decisions
* 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