

PHRi Functional Area 04

TOTAL REWARDS

International Human Resource Certification Institute

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Professional in Human Resources – International (PHRi) Workbook

Module Four: Total Rewards

2024 Edition

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Introduction

As a subscriber of the PHRi certification workbook series, you have access to the www.ihrci.org learning system. The system includes a Glossary that provides a search box and descriptions of key HR terms. Additionally, the system consists of over 900 practice exam questions and answers with explanations in our database, including pre-tests, review tests, and post-tests:

Pre-test: It contains the same percentage of questions from each content area. Participants can take a pre-test of that module to assess their conceptual understanding of that specific area of the PHRi exam content outline. When the pre-test is completed, an overall correct percentage and the number and percentage of questions answered correctly are provided. Answers with explanations for individual questions are also provided. Our system allows users to save the pre-test results for later improvement.

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Access to the learning system is valid for twelve (12) months from the date of purchase, covering two test windows. Take the pre-test, review, and post-test as many times as possible within 12 months. Access to these practice exams is for your use, and your account should not be shared with others. Your use of the online practice exams indicates your agreement with these terms.

Please note that this workbook is not a textbook. The materials, including workbooks and practice exams, are intended for use as aids in preparing for the PHRi Certification Exam conducted by the HR Certification Institute. While studying these materials will enhance your understanding of the key functional areas that comprise the HR Certification Institute PHRi exam content outline, these workbooks should not be considered legal or professional advice.

Table of Contents

Introduction.....	3
Table of Contents.....	4
Part One: Total Rewards Management	7
1. Total Rewards Programs	7
1.1. Benefits of Total Rewards	7
1.2. Compensation Planning	9
1.3. Strategic Rewards	9
1.4. Individual Differentiation	11
1.5. Market Conformity (Competitiveness).....	13
1.6. Internal Consistency (Equity).....	14
2. Total Reward Strategy.....	16
2.1. Development of a total rewards strategy.....	16
2.2. Total Rewards Statement (TRS)	18
2.3. Implementation of TRS.....	20
3. Compensation Planning	21
3.1. Defining/Reviewing Compensation Philosophy	22
3.2. Industry and Market Research	22
3.3. Analyzing Internal Compensation Data	23
3.4. Aligning with Business Goals	23
3.5. Creating Salary Ranges and Grades.....	23
3.6. Managing the Compensation Budget.....	23
3.7. Monitoring and Adjusting the Plan	23
4. Job Leveling	23
4.1. Key Components of Job Leveling.....	24
4.2. The Benefits of Job Leveling	25
4.3. The Methods of Job Evaluation	26
5. Remuneration Surveys	27
5.1. Purposes of Remuneration Surveys	28
5.2. Market Select	28
5.3. Data Collect	28
5.4. Data Analysis	30
6. Pay Structure	32
6.1. Terms and Definitions.....	32
6.2. Global Salary Grades	35
6.3. Global Pay Structure.....	36
7. Individual Differentiation	39
7.1. Entitlement Orientation	39

7.2. Performance Orientation	40
8. Market conformity.....	40
9. Internal Consistency	41
9.1. Red-Circled Employees	42
9.2. Green-Circled Employees	43
9.3. Pay Compression	44
9.4. Pay Increases	44
10. Job vs. Person Based Pay	47
10.1. Paying for the job	48
10.2. Paying the person	50
11. Compensation Communications	51
11.1. Goal of Compensation Communication	52
11.2. Timing of Compensation Communication.....	52
11.3. Information of Compensation Communication	52
Part Two: Incentive Programs	54
1. Incentive Compensation.....	54
1.1. Principle of Incentive Plan	55
1.2. Line of sight	55
1.3. Individual Incentives.....	55
1.4. Group Incentives	56
2. Individual Performance Pay Plans	57
2.1. Merit Pay	58
2.2. Piecework	59
2.3. Sales compensation.....	59
2.4. Cash Award	60
2.5. Recognition Programs	61
3. Group Performance Pay Plans	62
3.1. Gainsharing.....	62
3.2. Profit Sharing.....	63
3.3. Risk-Sharing Plans.....	63
3.4. Employee Stock Ownership Plans (ESOPs)	64
3.5. Performance-Sharing Plan.....	64
4. Non-Financial Incentive Plans	64
4.1. Team Building and Social Events	65
4.2. Professional Development Opportunities.....	65
4.3. Flexible Working Schedules.....	65
4.4. Green Commuting Incentives.....	65
4.5. Wellness and Health Programs	65

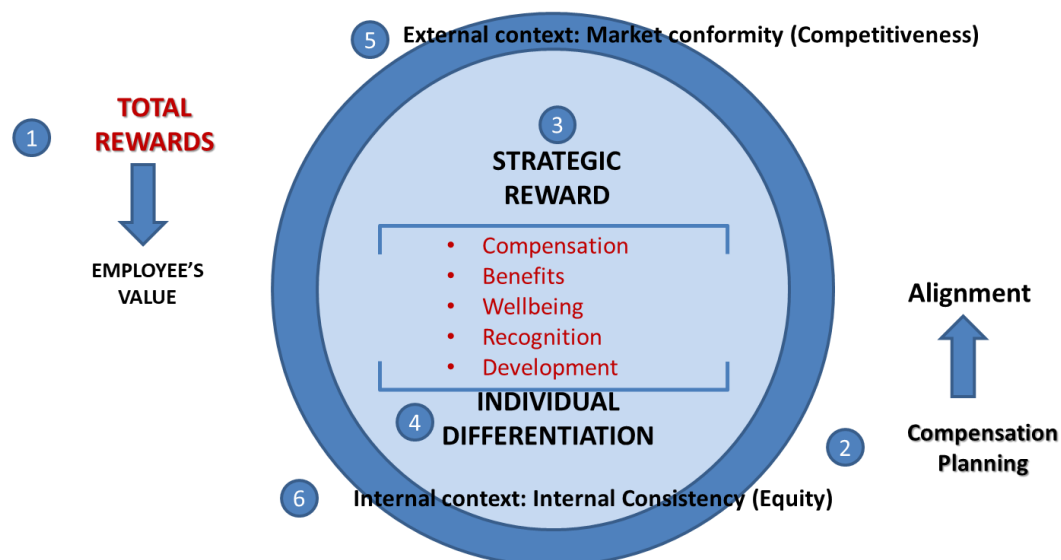
4.6. Workplace Amenities	66
Part Three: Payroll and Benefits	68
1. Employee Benefits.....	68
1.1. Objectives of Benefits.....	68
1.2. Key Employee Benefits	69
1.3. Specific Benefit Plans	70
1.4. Part-Time Employee Benefits	75
1.5. Benefits for different generations	76
2. Benefits Design	78
2.1. Statutory Benefits.....	79
2.2. Industry Standards	79
2.3. Additional Benefits	79
2.4. Flexible Benefits	79
2.5. Part-Time Employee Benefits	79
3. Flexible Employee Benefits.....	80
3.1. Flexible Spending Accounts	80
3.2. Transportation Plans.....	81
3.3. Cafeteria Plans.....	81
4. Benefits Administration.....	81
4.1. Benefits and HR Technology.....	81
4.2. Benefits and HR Outsourcing	82
4.3. Benefits and HR Metrics	82
4.4. Benefits and Cost Control.....	83
4.5. Benefits and Communication	83
5. Retirement and Savings Plan Payments	84
5.1. Defined-Benefit Pension Plans	84
5.2. Defined-Contribution Pension Plans	85
5.3. Cash Balance Pension Plans	85
5.4. Early Retirement Plan	85
6. Payroll Administration	85
6.1. Payroll Calculation	86
6.2. Element of Payroll	87
6.3. Payroll Process.....	88
6.3. Payroll Audit	90
6.4. Payroll System.....	92
6.5. Payroll Outsourcing	93
Reference.....	95

Part One: Total Rewards Management

1. Total Rewards Programs

According to WorldatWork – Total Rewards Association, “Total Rewards refers to a strategic portfolio of commitments employers deploy to attract, retain, and nurture a skilled, talented, and engaged workforce”. Total Rewards Strategy is an integrated approach, aligned with an organization's overarching business objectives, aimed at fostering a workforce that is motivated and committed to excelling and growing alongside the organization. This strategy encompasses a comprehensive package of rewards that includes various benefits, incentives, perks, as well as the guidelines, processes, and programs offered to employees.

Essentially, a robust Total Rewards Strategy is instrumental in enhancing business performance and achieving targeted outcomes. It does so by cultivating a workforce that is engaged and satisfied. The responsibility of implementing and managing this strategy typically falls within the realm of the HR department or a specialized Compensation & Benefits team, underscoring the strategic role of HR in driving organizational success through employee rewards and recognition. There are several important concepts about total rewards designing as follows:



Source: WorldatWork (2021)

1.1. Benefits of Total Rewards

Total rewards encompass far more than just base salary and bonuses. They represent the complete array of benefits and values that an organization offers to its employees,

forming a critical component of both business and people strategies. Accordingly, total rewards include everything the employee perceives to be of value resulting from the employment relationship.

An effectively crafted total rewards program is key to attracting, motivating, and retaining the right talent across all levels, from entry-level positions to executive roles. It plays a significant role in molding the company's culture and shaping its external reputation. Importantly, it aligns the objectives of the business with the genuine desires and needs of its employees.

However, implementing such a program is not without its challenges. With constantly evolving business landscapes, economic fluctuations, and changing workforce expectations, what employees seek from their work is continually transforming. Career trajectories are no longer linear, and new roles and job types are frequently emerging, adding layers of complexity to designing a comprehensive and adaptive total rewards strategy

Organizations benefit significantly from implementing a robust total rewards strategy, and here are some key reasons why:

1.1.1. Attracting Top Talent

A comprehensive total rewards strategy that meets various employee needs is attractive to a wide range of job seekers. This helps in drawing a diverse pool of candidates, streamlining the recruitment process.

1.1.2. Boosting Employee Satisfaction and Engagement

A well-crafted total rewards program can keep up with employees' evolving needs throughout different life stages, leading to higher satisfaction. Fair and effective rewards also enhance employee engagement.

1.1.3. Enhancing Employee Retention

A total rewards strategy that fosters employee wellbeing, motivation, and engagement is crucial in keeping employees committed to the organization.

1.1.4. Increasing Competitiveness

Such a strategy not only elevates an organization's standing within its industry by encouraging high performance but also makes it a more attractive option for potential talent, positioning it as a preferred employer.

1.1.5. Improving Business Performance

The ability to attract and retain talented employees directly contributes to achieving organizational objectives and often leads to superior business performance. Engaged and high-performing employees are typically at the core of successful companies.

1.2. Compensation Planning

HR professionals, in managing the total rewards framework, must ensure administrative efficiency and optimize costs. The optimization process starts with establishing fundamental guiding principles and then involves comprehending what employees value most in their rewards. The subsequent sections outline essential steps in compensation planning to ensure alignment with these principles. Key objectives of compensation planning include:

1.2.1. Aligning Compensation with Business Strategy: Formulating pay and compensation principles that bolster the organization's business strategy, enhance market competitiveness, and align with operating costs and objectives.

1.2.2. Ensuring Fair and Equitable Compensation: Regularly reviewing compensation practices to ensure employees are rewarded fairly and transparently.

1.2.3. Attracting Qualified Candidates: Recognizing compensation as a vital element of the employee value proposition to attract top talent, focusing on competitive base pay, incentives, and benefits.

1.2.4. Creating an Engaged Workforce: Acknowledging and rewarding employee efforts to foster loyalty and longer tenure within the company.

1.2.5. Boosting Productivity and Profitability: Understanding that employee satisfaction leads to higher productivity – as much as 20% more according to Forbes – and, consequently, greater profitability for the company.

1.2.6. Promoting Team Wellness: Emphasizing the importance of work-life balance to enhance team productivity and employee retention.

1.2.7. Reducing Turnover and Improving Retention: Offering compelling compensation packages to reduce voluntary turnover and retain valuable employees.

In summary, effective compensation planning not only involves financial remuneration but also integrates elements that contribute to employee wellness, satisfaction, and loyalty, thereby driving overall organizational success.

1.3. Strategic Rewards

Compensation decisions must be viewed strategically. Because so many organizational

funds are spent on compensation-related activities, it is critical for top management and HR executives to view the “strategic” fit of compensation with the strategies and objectives of the organization. The changes in the global marketplace for products and services have led to organizational changes in business philosophies, strategies, and objectives. Increasingly, organizations are recognizing that compensation philosophies must change also. For example, if a firm wishes to create an innovative, entrepreneurial culture, it may offer bonuses and stock equity programs so that employees can participate in the growth and success of the company, but set its base pay and benefits at relatively modest levels. However, for a large, stable organization, highly structured pay and benefit programs may be more common.

Strategic reward management involves the formulation and implementation of an equitable reward system that is congruent with the organization’s strategic objectives. A strategic reward system is a type of human resource management tool that is used to reward hardworking employees in an organization. It operates on two main principles; the best-fit perspective and the best practice advocates claim. The objectives of a strategic reward system are; attract and retain employees, motivate performance, promote skill development, encourage corporate culture and determine pay costs. Rewards can be either intrinsic or extrinsic. However, it is important when designing, implementing and using a reward strategy, that it meets both individual and organizational needs.

WorldatWork delineates five components of Total Rewards, each corresponding to elements in Maslow’s hierarchy of needs. These components are:

1.3.1. Compensation

This includes pay (both base and variable) given for the application of skills, achievement of qualifications, time commitment, effort, and target accomplishment in support of an organization’s goals. It addresses employees' physiological needs, such as affording food, clothing, and housing, encompassing base pay, variable pay, stock options, and cash bonuses.

1.3.2. Benefits

These packages cater to the physical, emotional, and familial safety of employees. Standard benefits include health, dental, and vision plans, leave policies, life and disability insurance, and retirement plans.

1.3.3. Wellbeing

Increasingly vital, employee wellbeing spans beyond physical health to encompass

overall life satisfaction and motivation. Employers now focus on fostering a culture that supports wellbeing through:

- Employee assistance programs for personal challenges.
- Employee resource groups for social and professional networking.
- Diversity, Equity, Inclusion & Belonging (DEIB) initiatives to ensure a fair and inclusive work environment.
- Company-sponsored events for team building and family engagement.
- Volunteer opportunities for community involvement.
- Remote and flexible work options for better work-life balance and familial safety.

1.3.4. Recognition

Beyond compensation and benefits, employees seek acknowledgment for their achievements. Recognition can manifest as awards (like spot, tenure, or performance awards), promotions for increased responsibility, or simple verbal or written appreciation. While not all employees may desire formal recognition, respect is a universal need for dignity and psychological safety in the workplace.

1.3.5. Development

Investment in employee development signifies an investment in their self-actualization. Through education, training, mentorship, and relevant work experiences, employees can utilize their inherent talents and skills, enhancing their competency and potential for career advancement within the organization. This focus on development empowers employees to realize and fulfill their full potential.

1.4. Individual Differentiation

Differentiation of rewards is supported where there are differences in the scope of the position within an organizational context, and/or due to superior individual or team contributions. For example, a reward program for an organization might look very different from a compensation program for the manufacturing group or the sales team, with varying incentives based on cash compensation and non-cash compensation options. The goal is to attract, develop, and retain a high performing staff, as well as to differentiate the highest performers so you can properly reward them. To achieve this type of compensation structure, follow these four basic steps.

1.4.1. Step 1: Segment the Workforce

Every organization has critical skill sets. To find the value of various employees and roles, first determine how people contribute to the well being of the organization, then tie their value to a meaningful compensation plan. Identify critical roles within your organization and critical skills that impact its success. Based on this understanding you can segment your rewards programs to properly compensate those roles and skill sets that are most important to the company. Once compensation has been awarded, survey employees to learn about what they like and dislike, and whether there are other types of compensation they would value more. This information provides valuable insights for setting compensation budgets in the future, and provides employees an opportunity to have their preferences heard.

1.4.2. Step 2: Create Flexible Compensation and Incentive Plans

As you design your incentive plan, establish clear links between incentives and corporate goals, divisional goals, departmental goals, and individual goals. Each employee should know how their actions impact the company. Executives and senior directors should be incented based on their impact on their respective regions and divisions. Line-of-business professionals often share team-based goals. They should be incented based on how they support critical objectives and by how their individual achievements influence results. Variable compensation plans are most effective if they are structured to pay out over time, based on performance. Don't give away all the money up front. Spend wisely and reward people as they make valuable contributions. As the labor market improves many companies will see increased turnover among their staffs. To retain top employees, consider offering them three-year compensation plans tied to agreed-upon performance metrics.

1.4.3. Step 3: Enforce Equitable Policies with Complete Transparency

Compensation policies must be fair and equitable to everyone, not just to the high-performing segment of the workforce. There can't be any perception of favoritism—not just in the cash compensation plans, but also in non-cash based rewards such as the projects to which they are assigned, opportunities for training, etc.

Even the best planned compensation strategies will fail if employees think they are being treated unfairly. Fostering an environment of fairness requires transparency: you must be able to convey the total rewards philosophy to each employee. HCM systems include employee portals and online compensation statements that paint a complete picture of each employee's pay, benefits, and incentives.

It's also important to facilitate extensive communication between management and staff as well as total transparency into performance and goals. It helps to have good

development plans and performance plans and highly engaged managers who can facilitate goal setting and career planning. HR can support these efforts: first by acquiring the right e-HR solutions to summarize and communicate total compensation plans, second by instituting top-down policies governing effective communication with employees.

1.4.4. Step 4: Use Technology to Simplify Administration

Modern IT applications enable managers to allocate budgets for incentives, manage the salary review process, and generate compensation statements. They typically incorporate business intelligence tools that let authorized users examine salary trends, market developments, salary structures, and distribution scenarios.

Utilizing these platforms can streamline market analysis, program design, and administration of total rewards programs. These platforms also simplify key activities for the compensation team such as defining and editing business rules, verifying employee eligibility, and creating a performance-driven culture with transparency into compensation policies and practices. Additionally, total rewards professionals will be freed up and empowered to add strategic value to the business by consulting with managers, rather than being mired in the tactics of the process.

1.5. Market Conformity (Competitiveness)

In order for a business to operate effectively, the company needs to develop a compensation strategy that achieves the two goals of rewarding considered fair to employees, while providing a financial return on the investment for the employer. Pay equity has two approaches. The first is externally driven by market forces. The second is an internal focus, driven by the employer's valuation of the job.

Using market pricing to establish wages and salaries is called market conformity or competitiveness. Achieving external competitiveness in the area of compensation means balancing the need to keep operating costs (including labor costs) low with the need to attract and retain quality workers. External competitiveness is how a company's rates of pay compare to those of its competitors.

Market based pay systems benefit from being inherently empirical, built from research, through surveys, reporting what similar jobs are paid in the organizations that one competes with in the labor market. Committing to a market base pay compensation structure means that employees will be paid at a competitive salary when compared with rates offered to people in similar positions in peer organizations. The labor market, ruled by supply and demand, drives this approach.

Establishing the pay level balances a company's profit requirements with competition for competent employees. Factors determining pay level include:

- 1.5.1. Competition in the labor market: the supply and demand for employees with various qualifications.
- 1.5.2. Product market conditions: the degree of demand for specific products and the level of industry competition.
- 1.5.3. Organizational characteristics: industry, management philosophy, size, and technology.

Weighing all these considerations, firms can choose to pay more than the industry average, and therefore favor attracting and retaining quality employees, or pay less than their competitors' average hoping to attract and retain employees through non-compensation means such as recognition events, achievement celebrations, and working in a pleasant environment. A competitive pay level—one that balances all considerations—can help contain labor costs, enlarge the pool of qualified applicants, increase quality and experience, reduce voluntary turnover, discourage unionization, and abate pay-related work stoppages. Once a company has determined its pay level relative to its competitors, compensation managers must determine the best compensation package for each occupation.

1.6. Internal Consistency (Equity)

External equity is one side of the coin. There is also the employer's perception of fairness called internal equity. Where external equity is a measure of market competitiveness forming its basis on job functions and duties, internal equity is a measure of internal worth with a basis in job autonomy and responsibility. If you have multiple incumbents in the same job title who are paid differently, the differences in pay are an expression of internal equity.

Arriving at fair compensation is not always easy. Aside from the fact that each position has a unique value to an organization and not all jobs are created equal, employers also face the challenge of recognizing and rewarding exemplary performance in a given role. There are a variety of definitions for internal equity.

“Internal equity is a situation that results when people feel that performance fairly determines the pay for each individual with a certain job or that relative difficulty results in appropriate differences in pay rates between jobs.”

This and other definitions of internal equity have one fact in common: in order to achieve internal equity, it's not enough that compensation be fair according to the

employer, compensation must be seen as fair by employees. Employees will have their own ideas about how their jobs should be valued relative to other roles in the company—and they may not agree with the company's perspective.

One way to achieve a sense of internal equity is by following a consistent set of principles when designing and applying compensation structures and by avoiding ad hoc negotiations. If you're concerned about internal equity in your organization or you hear rumblings of discontent on the topic, you may choose to conduct an internal equity study to help determine whether concerns are justified.

The number of levels and the degree of pay differentials are based on three general criteria: the value of a job and a job's responsibilities, the skills and knowledge needed, and job performance and productivity. Employers can use these criteria to modify employee behavior by indicating what kinds of responsibilities, performance, productivity, skills, and knowledge employees need to move into a different level and receive a higher pay rate. More specifically, six primary but interrelated factors can shape a company's pay structure:

1.6.1. Social Customs

Beginning in the thirteenth century, employees began demanding a "just" wage. This idea evolved into the current notion of a federally mandated minimum wage. Hence, economic forces do not determine wages alone.

1.6.2. Economic Conditions

Demand for labor influences employee wages. Employers pay wages based on the relative contributions employees make to production goals. In addition, supply and demand for knowledge and skills helps determine wages.

1.6.3. Company Factors

Pay structures depend on the kind of technology a company has and on whether a company uses pay as an incentive to motivate employees to improve job performance and to accept more responsibilities.

1.6.4. Job Requirements

Some jobs may require greater skills, knowledge, or experience than others and hence fetch a higher pay rate.

1.6.5. Employee Knowledge and Skills

Likewise, employees bring different levels of skills and knowledge to companies and

hence they are qualified to work at different levels of a company hierarchy and receive different rates of pay as a result.

1.6.6. Employee Acceptance

Employees expect fair pay rates and determine if they receive fair wages by comparing their wages with their coworkers' and supervisors' rates of pay. If employees consider their pay rates unfair, they may seek employment elsewhere, put forth little effort in their jobs, or file lawsuits.

2. Total Reward Strategy

Total rewards is a broad term for an organization's total employee-related costs. It includes the money paid to employees in wages, salaries, bonuses, perks, and other intangible benefits. In short, total rewards are defined as "the sum of all rewards provided by a company to its employees." Rewards as a concept, no matter how broad or narrow you define them, has been the subject of study for many years. The idea of rewarding a human being for a specific behavior or an act is not new. Every time a person is rewarded, some change is expected and desired.

As an employer, you probably put a lot of effort into analyzing your workforce and the performance of your employees. Total rewards encompass all the ways that employees are rewarded for their work.



Source: Gardner (2023)

2.1. Development of a total rewards strategy

A well-executed total rewards strategy can significantly enhance organizational

performance by fostering a workforce that is both engaged and content. Typically, the responsibility for deploying this strategy falls on the HR department or a specialized compensation & benefits team. To develop a total rewards strategy, it's essential to:

2.1.1. Conduct a Current Rewards Assessment

Begin by reviewing what's already in place, analyzing the existing compensation structure, and understanding how each component of your total rewards stacks up.

2.1.2. Solicit Employee Feedback

Understand employee perceptions and identify any gaps in your current rewards system through surveys or focus groups, and by reviewing data from stay and exit interviews.

2.1.3. Engage Organizational Leadership

Share audit findings and employee insights with leadership to highlight the necessity of a robust total rewards strategy and to secure their endorsement, particularly regarding budgetary considerations.

2.1.4. Define Goals and Priorities

Determine what you aim to accomplish with your total rewards revision, ensuring alignment with specific business objectives.

2.1.5. Ensure Alignment With Organizational Values

The total rewards strategy should mirror the organization's core values and cultural ethos.

2.1.6. Balance and Customize Rewards

Ensure the rewards strategy is well-rounded, offers personalization, and meets the diverse needs of your employees in an equitable and fair manner.

2.1.7. Stay Current With Trends

Stay informed about global and industry-specific trends to ensure your rewards remain relevant and competitive.

2.1.8. Communicate Clearly With Employees

Maintain transparency with employees about the total rewards available, utilizing tools like internal wikis and Q&A sessions for clarity.

2.1.9. Monitor and Adjust Based on ROI:

Keep track of expenses and the impact of your rewards strategy, making adjustments as necessary to maintain a positive return on investment and manage the HR budget effectively.

2.2. Total Rewards Statement (TRS)

A Total Rewards Statement (TRS) is a tailored report that outlines the comprehensive value provided by an organization to its employees within the employment relationship. Essentially, it quantifies and details the full spectrum of value that is part of the organization's overarching Total Rewards strategy.

The aim of a TRS is to encompass all aspects of an organization's offerings, including wellness programs, learning opportunities, and various services, especially in well-established companies. It's a practical tool for negotiations with prospective hires and helps current employees recognize the organization's value, thereby enhancing engagement and retention.

Effectively communicating the employee value proposition is a core function of a TRS, which typically garners high engagement and commitment from employees when executed correctly. This is pivotal since many employees lack a clear understanding of the full range of benefits available to them, as evidenced by studies showing a significant gap in employees' comprehension of their total rewards and pay slips.

A TRS can be instrumental in positioning a company as an employer of choice, a crucial factor in today's competitive talent market. It conveys to candidates and employees the unique benefits offered, countering any misperceptions and reinforcing the organization's employer brand authentically.

In showcasing the employment relationship's value, a TRS goes beyond just financial compensation. It includes elements that contribute to the overall employee experience, helping employees see a broader picture of what they receive in return for their work. This is particularly important in times when workforce trends such as the Great Resignation emphasize the importance of understanding the value of one's role.

A TRS also informs employees about the customization options within their total rewards, offering them the flexibility to tailor their benefits and compensation to suit their individual needs. While personalization can pose challenges, such as maintaining pay equity, it is a significant trend in enhancing the employee experience and creating a more personalized approach to rewards.

TRS is a strategic tool used to communicate the company's value to both potential hires and current staff. The components of a TRS can be detailed as follows:

2.2.1. Financial Rewards

This section outlines direct financial compensation, such as base pay, variable pay, bonuses, commissions, and any other forms of cash remuneration that contribute to an employee's income.

2.2.2. Monetary Benefits

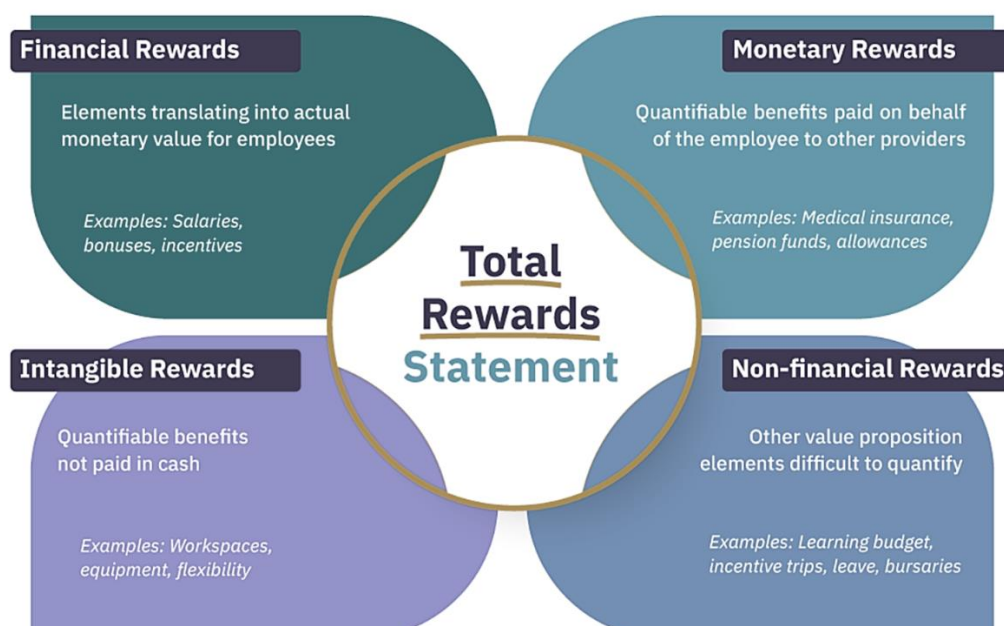
These are the quantifiable benefits that the employer pays on the employee's behalf to third parties. Examples include contributions to medical, dental, or life insurance premiums, retirement plan contributions, and any subsidies for health and wellness programs.

2.2.3. Non-Financial Rewards

This category encompasses tangible but non-cash benefits that have a clear value. Such benefits might cover professional development allowances, subsidized educational programs, company cars, or allowances for travel and accommodations.

2.2.4. Intangible Rewards

These are components of the total rewards that are less tangible and not easily quantified. They include aspects like the flexibility of work hours, the opportunity to work remotely, the quality of work-life balance initiatives, career development opportunities, and the work environment itself, including the quality of the equipment and tools provided for the job.



Source: Veldsman (2023)

A TRS should effectively communicate all these components, demonstrating to current and prospective employees the full value beyond just the paycheck, thus reinforcing the employer's brand as a top choice for employment.

2.3. Implementation of TRS

It's critical to recognize that the process of implementing a Total Rewards Statement (TRS) is as significant as the document itself. Here's a detailed approach:

2.3.1. Employee and Manager Education

The success of a TRS hinges on educating both employees and managers about the rewards and the statement's objectives. Prepare for heightened interest and inquiries, and clarify the TRS's role in broader human capital initiatives, particularly concerning the employee value proposition.

2.3.2. Empowering HR and Management

HR business partners and managers should be well-versed in the TRS to address employee questions effectively. They should understand the reward determination process and how the reward cycle is approached organizationally.

2.3.3. Statement Development and Technology Utilization

Collaborate across departments to craft the TRS. Design, test with employees for relevance, and select HR software that aligns with your HR data systems for visualizing the TRS.

2.3.4. Data Integrity and Quality Checks

Ensure the accuracy of the data used in the TRS by thoroughly checking samples before the full rollout. This step is crucial to maintain the document's credibility.

2.3.5. Launching the TRS:

Launch the TRS with a strategy to manage system load, possibly staggering the release. Align the launch with significant reward cycle events, like bonus distributions, for greater impact.

2.3.6. Impact Assessment

Gauge the TRS's effectiveness through operational metrics, such as employee access rates and error counts, and gather feedback on its influence on employee perceptions.

2.3.7. Continuous Improvement:

Develop the TRS iteratively, starting with essential financial details and gradually including a broader range of rewards. This allows for quick implementation and ongoing employee education.

Outlined below is a potential layout for a one-page Total Rewards Statement template:

Section	Description
Positioning	A short description explaining what a TRS is, what employees can expect to see, and reinforces where the TRS fits as part of the broader EVP. This section acts as a confirmation of the value of the employee & should support your key messaging.
Financial rewards & monetary benefits	This section provides an overview of the financial rewards. <i>Example: Guaranteed remuneration, Retirement scheme contribution, Medical insurance, etc.</i>
Shares	This is an overview of share allocations & options for the employee, if applicable. The purpose is to show long-term value & is often important for retention.
Additional information on benefits	This section can include more information on, for example, retirement benefits with flexible options the employee could explore or risk benefits such as disability cover, life insurance, and family cover.
Leave benefits	This section provides an overview of available leave and reinforces the types of leave employees have access to. <i>Example: Parental leave, Study leave, Sick leave, etc.</i>
Long service benefits	This section showcases long service benefits and when the employee would qualify for these additional benefits.
Learning	This section outlines learning opportunities available to the employee, specifically focusing on where employees formed part of learning initiatives. <i>Example: E-learning licenses, Learning programs attended, Bursaries, etc.</i>
Employee Offerings & Services	This section represents an overview of other services available to the employee with links to access these services. <i>Example: Gap cover services, Employee assistance programs, Sports and social clubs, Daycare, etc.</i>
Legal T&Cs	Lastly, employees must be aware of the TRS's applicable legal terms and conditions. These include conditions of data integrity and where additional support is available to better understand these benefits.

Source: Veldsman (2023)

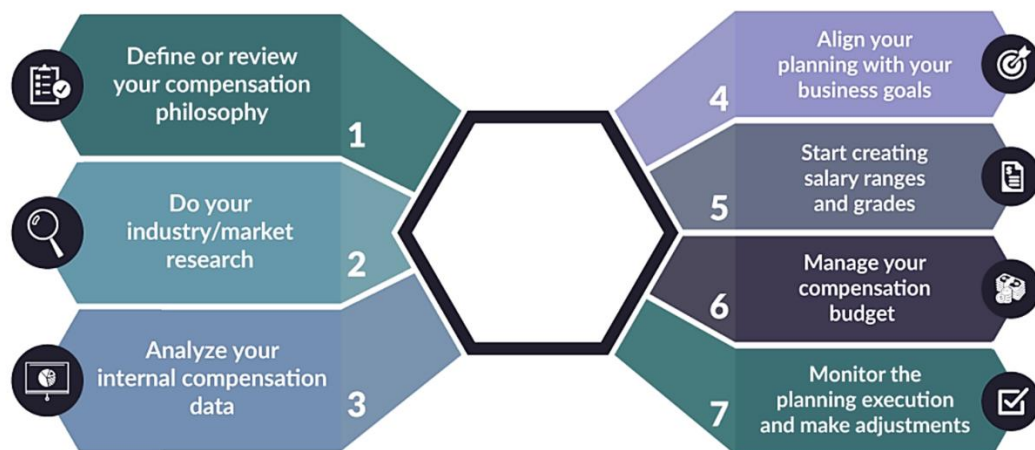
3. Compensation Planning

Compensation encompasses the total cash and non-cash benefits an employee receives in exchange for their work. This includes base salary, bonuses, stock options, and benefits such as insurance, pension plans, and parental leave, which will be explored more thoroughly later.

In the competitive landscape of talent acquisition, compensation is a key factor in attracting and retaining employees and directly influences organizational productivity. Surprisingly, a PayScale study revealed that less than half of companies have a strategic compensation plan in place.

Compensation planning falls under the purview of Human Resources or a specialized Compensation & Benefits department. It involves a strategic approach to align the company's financial interests and operational objectives with the goals of attracting, retaining, nurturing, and rewarding employees.

A comprehensive compensation plan covers the method of employee payment, the company's bonus structure, criteria for salary raises, and other relevant aspects. Understanding these components is essential for HR professionals to effectively manage and strategize compensation in line with organizational goals.



Source: Cosentino (2023)

3.1. Defining/Reviewing Compensation Philosophy

Establish or reassess your organization's compensation philosophy. This should reflect your company's culture, size, and resources, and act as a foundation for your total compensation approach. The philosophy should provide clear guidance for making compensation decisions and be revisited periodically for relevance.

3.2. Industry and Market Research

Conduct thorough research on industry salary standards and compensation practices, known as salary benchmarking. This can be done using online resources like PayScale, LinkedIn Salary, Glassdoor, and U.S. Bureau of Labor Statistics, or by analyzing

competitors' job postings. Alternatively, enlist third-party services like Deloitte or PwC for comprehensive market analysis. This step is crucial to ensure your compensation is competitive and fair.

3.3. Analyzing Internal Compensation Data

Assess your existing compensation structure. Use your HRIS or simple spreadsheets to collate data. A key aspect is conducting pay equity analyses to ensure consistent compensation for similar roles. This helps in identifying discrepancies and planning necessary adjustments to prevent turnover.

3.4. Aligning with Business Goals

Your compensation plan should directly support your organization's mission and vision. While developing the plan, consider the company's financial limitations to ensure sustainability.

3.5. Creating Salary Ranges and Grades

Develop a salary structure with specific ranges and grades. This helps in managing compensation expenses and ensuring pay equity. Begin with critical roles and progress to others. If existing ranges are in place, review and adjust them as necessary. Salary grades should reflect varying experience levels within the same job title.

3.6. Managing the Compensation Budget

Compensation costs typically account for a major part of organizational expenses. Accurate budgeting is essential for financial health. Track and manage these expenses effectively, using tools suitable for your team's size, from Excel for smaller teams to sophisticated compensation management software for larger organizations.

3.7. Monitoring and Adjusting the Plan

After implementing your compensation strategy, establish a process for ongoing review. Collect feedback from different stakeholders, including managers, employees, and applicants, to gauge the competitiveness of your compensation package. Regularly update your salary structure based on industry trends and competitor analysis.

4. Job Leveling

Job leveling, often referred to as job grading or classification, is a systematic method used in organizations to create a structured job hierarchy. It involves evaluating the complexity, responsibilities, and relative importance of different roles. This process is crucial for categorizing positions in a way that accurately reflects their contribution and significance

within the organization.

Integral to job leveling is the process of job evaluation. Job evaluation is the technique through which the relative worth of a job is assessed, based on factors like the skills required, the responsibilities it entails, its complexity, and the conditions under which it is performed. Various methods, including point-factor systems, ranking, and classification methods, are utilized in job evaluation. The results of this evaluation are pivotal as they inform the job leveling process, ensuring that jobs with similar demands and responsibilities are grouped together while distinguishing them from roles with different requirements.

Once jobs are leveled and evaluated, they are then assigned to specific pay grades. These pay grades correspond to salary ranges that reflect the job's level of responsibility and the qualifications needed for it. Pay grades are crucial as they bring consistency to compensation, helping maintain both internal and external equity. They offer a structured approach to remunerating employees fairly, based on their role's level and complexity within the organizational framework.

Therefore, job leveling, job evaluation, and pay grades are interconnected facets of a holistic compensation management system. Job leveling establishes the structural framework, job evaluation provides the necessary information for appropriate placement within this framework, and pay grades determine the compensation range for each level.

4.1. Key Components of Job Leveling

job leveling framework encompasses several essential components, each playing a pivotal role in structuring an organization's workforce effectively:

4.1.1. Job Levels

This element categorizes various roles within an organization based on their level of responsibility and leadership. It spans a spectrum from entry-level positions to the highest executive management roles, providing a clear hierarchy and growth pathway within the company.

4.1.2. Competencies

These are the crucial skills, knowledge, abilities, and expertise required for each job. Competencies cover a range of attributes necessary for job performance, including communication skills, teamwork capabilities, problem-solving abilities, and other relevant professional skills.

4.1.3. Responsibilities

This aspect outlines the specific tasks and duties associated with a particular role. Responsibilities define what is expected from an employee in a given position, helping to clarify the role's scope and objectives.

4.1.4. Compensation Range

The compensation range indicates the financial remuneration associated with a job, from the starting salary to the maximum amount the organization is prepared to offer. This range is determined based on various factors, including the job's level, the required competencies, and the responsibilities it entails.

4.2. The Benefits of Job Leveling

4.2.1. Achieving Consistency in HR Programs:

Implementing a standardized job evaluation system is essential for HR professionals. It enables clear communication regarding job structures, roles, and their importance within the organization. A consistent approach in job leveling helps in differentiating one job role from another, considering various factors like interaction, problem-solving abilities, knowledge application, accountability, and the impact of decision-making. This clarity facilitates the appropriate assignment of job roles within the organizational hierarchy.

4.2.2. Enhancing Career Advancement Opportunities:

Job leveling frameworks are instrumental in creating and showcasing career advancement opportunities within an organization. This is pivotal for boosting employee engagement and retention. It allows employees to understand how their roles can lead to growth and development, aiding in effective career pathing for all levels within the organization.

4.2.3. Improving Administrative Efficiency:

The HR department constantly seeks methods to better administer HR activities. A job-leveling structure is key to enhancing efficiency and simplifying decision-making processes related to job roles and employees. This includes standardizing job titles, discussing pay grades and salaries, and determining eligibility for rewards.

4.2.4. Ensuring Fair and Equitable Compensation:

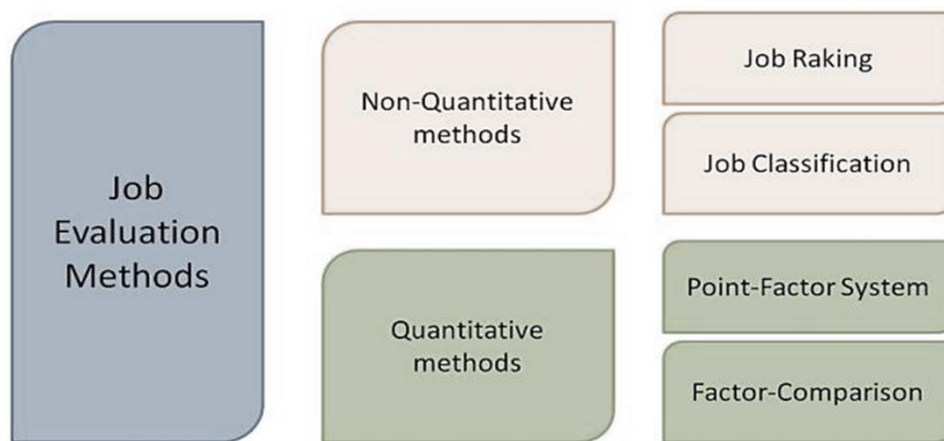
Job leveling ensures that employees are compensated fairly for equivalent work. It's crucial for maintaining legal pay standards and ensuring that employees with similar responsibilities receive equal pay and recognition for their skills and efforts.

4.2.5. Retaining Employees:

Job leveling plays a significant role in employee retention. It allows organizations to offer new roles and compensation based on performance. Employees often compare their growth and opportunities within an organization to those in other companies. A well-structured job leveling system should clearly outline the expectations for each role, enabling managers to guide employees on their progression within the organization.

4.3. The Methods of Job Evaluation

In setting job levels within an organization, four primary methods of job evaluation are commonly used: point factor, factor comparison, job ranking, and job classification. Each method offers a different approach to assessing the value of jobs.



4.3.1. Job Ranking:

The simplest and a non-quantitative method, job ranking is ideal for smaller organizations. It involves arranging jobs in a hierarchy based on their perceived value to the company. Typically, jobs are ranked on the basis of a single factor, like the difficulty of the job or the education required. The jobs at the top of this hierarchy are deemed most important and thus receive the highest pay. This method is straightforward but can be overly simplistic for larger organizations with a wide range of jobs.

4.3.2. Job Classification:

This method involves creating descriptions for each class of job and assigning them a grade based on the required skills and complexity. It's a non-quantitative approach that relies on job titles and duties, assuming they are consistent across different organizations. Each job class might have varying levels, often indicated in the job title (e.g., HR Specialist 1, HR Specialist 2). This method is useful for standardizing job

categories but may not capture the nuances of individual job roles.

4.3.3. Point Factor Comparison:

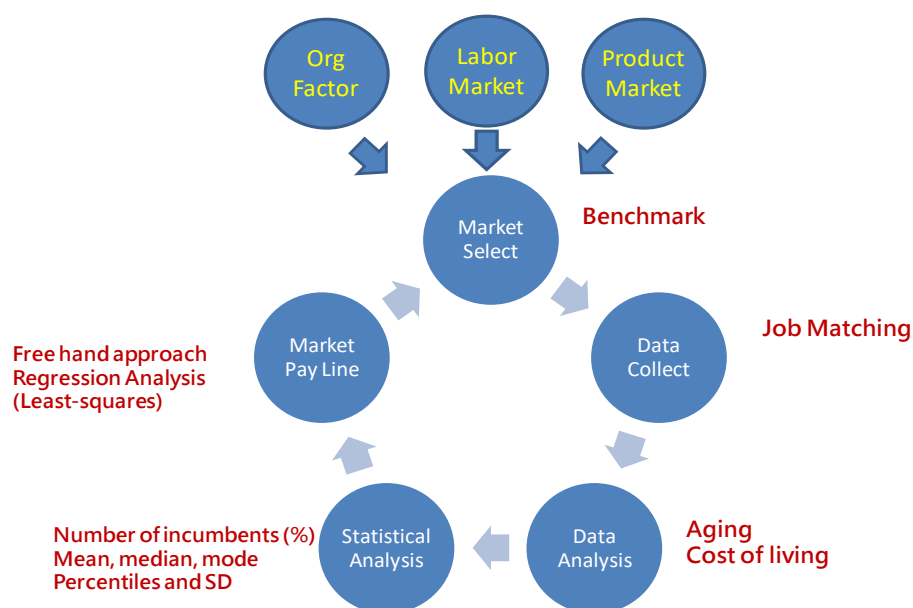
This quantitative method breaks down jobs into compensable factors that are determined during a job analysis. Each factor is assigned points, and these points cumulatively establish the pay structure for the position. Jobs with higher point totals typically receive higher pay. This method helps in creating a rank order of jobs based on their relative importance within the organization.

4.3.4. Factor Comparison:

A hybrid of ranking and point factor methods, factor comparison is also quantitative. It involves identifying benchmark jobs within the organization that have similar responsibilities. These jobs are then analyzed to rank identifiable factors, which are subsequently compared to market rates to assign a monetary value to each factor. This method is praised for its consistency and objectivity but is more complex and costly compared to others.

5. Remuneration Surveys

As discussed earlier, Job evaluation which is considered to determine the relative worth of a job within an organization focuses on internal equity of compensation. Now we would then talk about external competitiveness which can be analyzed by up-to date Remuneration survey.



Remuneration surveys collect information on prevailing market compensation and benefit practices, including base pay, other cash payments (statutory and market), variable

compensation (e.g., short- and long-term incentive plans), and time off. Remuneration surveys allow organizations to recognize and relate their remuneration structures to global and local trends. Many organizations use various remuneration surveys to benchmark or measure themselves against what the industry is paying employees with similar skill sets and experience in that occupation. Most of the remuneration surveys have to be bought from the company directly.

5.1. Purposes of Remuneration Surveys

5.1.1. Adjust the pay level in response to changing rates paid by competitors.

5.1.2. Set the mix of pay forms relative to that paid by competitors.

5.1.3. Establish or price a pay structure.

5.1.4. Analyze pay-related problems.

5.1.5. Estimate the labor costs of product/service market competitors

5.2. Market Select

To determine the prevailing rate for a job, companies can "benchmark" jobs against compensation surveys that are detailed and specific to the companies' industries and regions. A good compensation survey uses standard, proven methods of data gathering and statistical analysis to determine how much companies pay for a specific job in a specific industry. Match your job descriptions to the descriptions in the salary survey. Only match those which strongly resemble the survey description. Not all positions in your organization will match descriptions in the survey. Relevant labor market includes employers who compete:

5.2.1. For same occupations or skills.

5.2.2. For employees in same geographic area.

5.2.3. With same products and services

5.3. Data Collect

Once an organization decides that it needs a remuneration survey, it must decide how the survey should be designed and conducted. The organization has two choices: It may develop and conduct an internal survey, or it may look to an external source. In the global environment, the use of external third-party data prevails.

There are many sources for global and country-specific compensation and benefits data. Typical sources include:

5.3.1. Government sources (e.g., ministries of labor or government statistical offices).

5.3.2. International organizations (e.g., the International Labor Organization).

5.3.3. Private firms (e.g., consulting organizations around the world that provide current global and local information for a fee).

5.3.4. Membership-based business organizations (e.g., employer federations and local chambers of commerce).

5.3.5. Professional, trade, and industrial associations.

Here are some considerations to weigh for a company who is deciding whether to purchase a compensation survey.

- **The background of the survey research firm and cosponsors, if any.** Look for reputable firms that follow proven methods to gather and analyze compensation data.
- **The scope of the survey.** Look for studies that cover industries, jobs, and regions that are most applicable to your purposes; and that provide data on enough jobs to be cost-effective.
- **The survey methodology.** Review the summary of the methodology to make sure it's consistent with standards set forth by reputable industry associations. Be especially sure the research organization is surveying human resource professionals or other people knowledgeable about compensation information within a company, rather than individuals.
- **The number of participants in the survey.** A good survey should cover a representative number of companies for its target population. A survey doesn't have to cover the entire industry or region to be robust; even a few dozen responding employers in some industries can provide enough data for a valid survey.
- **The names of participants.** Look for your competitors and peers. For many jobs, you may be competing for candidates with companies in different industries but the same geographic area. Some firms reveal a list of participants, or at least those well known within the industry. The surveying company may disclose big-name participants to draw more interest from smaller companies. A list of major employers can also add credibility to the survey. An important exception to note is that if a compensation analyst or compensation consulting firm is using multiple surveys to produce their own derivative market numbers, they will aggregate the

data by combining the surveys, placing differing weight on different sources and sometimes even making a qualitative adjustment. When the data has been aggregated in this manner, it is not customary to report numbers or names of participants. The usefulness and relevance of a salary survey depends largely on the survey participants.

- **The number of incumbents covered by the survey; and the sample size for each salary.** Make sure the participants are a good sample of the recruiting market. Generally, eight to ten participating companies is a good sample for positions below the management level. The sample size should increase the more senior the positions being surveyed, both to get a good representation and to allow for more job matches, since each company is organized differently. There could be limited pay data in some industries, or the available data might not be representative of the industry because of a low participation rate in the survey.
- **The relevance of the job descriptions to the positions being benchmarked.** Look for a good match between the survey and your company. Be sure to compare job descriptions, not just job titles.
- **The effective date of the survey data.** The date a survey is published is always later than the effective date of the data within the survey. If necessary, age the data from the effective date to the current month.

As with any form of research, it is important to use multiple data sources to narrow in on the "true" answer. Relying on a single source can be misleading if that source doesn't perfectly reflect the market in question. World at Work suggests that compensation analysts should use multiple data sources wherever possible; consulting firms and academics agree. The exceptions come when there is only one data source, or when there is a spot-on data source, such as a custom survey, that truly describes a precise market.

5.4. Data Analysis

5.4.1. Effective Date

For those surveys conducted on a regular basis, such as annual surveys, the effective date will be until the next survey is released in the following year. Otherwise, knowing the effective date of the survey can prevent companies from using outdated salary figures and causing error in pay budget forecasts.

If the survey is not current, the person using it should age the salaries to the current date. If a survey was conducted in September, the salaries are likely to be as of

September or even August. If you are using the survey in December to benchmark for a new position in the company, you will have to age the number. A simple way to do this is to take the annual rate at which salaries are moving for this job and prorate it, salary increases overall this year are around 3.5% but this may vary by job title.

A similar approach is used in setting pay levels across a company. Sometimes these figures are set at the beginning, middle, or end of the company's payroll year by aging the appropriate compensation data to those dates. When salary data is aged, movement in market rates is used to adjust outdated data.

5.4.2. Job Description

If a job on a survey is similar but not identical to one in the organization, the data can be weighted or leveled for a better match. Therefore conduct job analysis or review job descriptions is important for job matching.

When consulting a compensation survey, match the job descriptions rather than the job titles, even if the survey uses generic or widely used job titles. For example, an associate could be an entry-level position at one consulting firm, or it could be the title for someone with an MBA at another. Companies are structured differently, and different companies use different names for the same jobs, so job descriptions are the best way to match positions. Beware of surveys that use only job titles, as it is unlikely the data will be a reasonable representation of the jobs you're interested in.

A survey job description should list the primary job function in one or two sentences, followed by key responsibilities. While the descriptions should be generic and not specific to any one company, they should contain enough information for participants to match appropriately to ensure the data is accurate. It is also important to match the organizational level of the positions be surveyed. A position that is at the group level at one company may be at the subgroup or the sector level at another.

Job titles are broken down differently in different surveys. Some surveys break them down by levels within the organizations, i.e., senior management, middle management, and entry level. Positions may also be broken down by job families or the types of responsibilities, i.e., business development, marketing, product management, and sales.

5.4.3. Geographic area

Some salary surveys do not provide data for a specific geographic area since wage rates will vary by location, and organization should factor for geography any national salary survey data for the local or regional recruiting area to approximate local wage rates.

5.4.4. Compensation data.

There are many things to consider when analyzing the compensation components of a salary survey. Because companies have different pay structures, compensation data is collected in ranges as well as actual pay. Salary surveys can provide employers more information on the marketplace and how to set competitive pay without overpaying or underpaying employees. Surveys should ask for the minimum, midpoint, and maximum for the surveyed positions, in addition to the actual base salary paid.

Usually, the prevailing practice for any one job is to pay a range of incomes. As a result, although the median pay for a job is likely to be a definable number, the range is just as important. Companies pay employees differently for various reasons. It could be the company's pay philosophy; or it could be the geographic location or the industry practice; or it could be the incumbent's length of service or proficiency in the job. Whatever the reason, it is unlikely that two companies will pay an employee doing the same job exactly the same amount.

When reading the base pay figures, it's important to check how the numbers are calculated. The surveying parties can dictate to the participants how the numbers should be reported. Salaries can be on an annual, monthly, or hourly basis. For example, if the incumbent is a contract employee, hourly salaries are more relevant than an annual figure. The survey may request pay data for individual incumbents or averages for all incumbents matching a specific job description, depending on the types of surveys and their objectives.

6. Pay Structure

When a company has planned to expand into new countries, it is necessary to establish a pay (salary) structure. With all the different economic situation, cultures and exchange rates, it is difficult to come up with one structure that works everywhere. In the following, we will introduce more details with regard to pay structure. There are several terms and definitions to acknowledge first:

6.1. Terms and Definitions

6.1.1. Policy Line

A job structure orders jobs on the basis of internal organizational factors. The pay structure, on the other hand, is anchored by the organization's external competitive position, reflected in its pay policy line.

The pay level that a company sets its pay at compared to the market pay line, typically the midpoint of the pay structure is set to judge the going market rate. In building pay

structure scientifically, the line is a statistically computed least-squares-regression line.

6.1.2. Pay Grades

Pay grades are used to group jobs that have approximately the same relative internal or external worth; in other words, all jobs within a particular grade are paid the same rate or within the same pay range. Grades enhance an organization's ability to move people among jobs with no change in pay.

6.1.3. Pay Range

Pay range typically means high to low or minimum to maximum pay for a certain job grade. The range midpoints, minimums, and maximums reflect career paths, promotions, and other management systems and philosophy within the organization. The differential must be large enough to induce employees to seek and/or accept the promotion or to undertake the necessary training required.

Range spread subtracts the minimum amount from the range maximum and then divides that figure by the minimum. In general, lower-level jobs typically have a narrow range between minimum and maximum salaries, while the salary ranges for higher-level jobs will be wider. People in entry-level jobs have more promotion possibilities and tend to stay at the entry level for shorter periods of time, while people in higher-level jobs tend to stay in their range for a longer period of time.

Range overlap in salary ranges that will allow career development and pay increases without promotion at each level and the percentage of increase the organization will offer an employee for a promotion.

Overlap = $(\text{max rate of lower grade} - \text{min rate of higher grade}) / (\text{max rate of higher grade} - \text{min rate of higher grade})$

6.1.4. Compa-ratios (CP)

CP is a salary expressed as a percentage of or indexed to the salary range midpoint/market rate (salary/midpoint or market rate = CP). The CP may be used as an indicator of how an individual is doing against plan.

6.1.5. Salary Range Penetration

An alternative to compensation ratios called "range penetration" also uses a simple formula that divides the salary rate minus the minimum of the range by the maximum minus the minimum of the range. Here is the range penetration calculation: $(\text{salary} - \text{range minimum}) / (\text{range maximum} - \text{range minimum})$.

$$\frac{(\text{Actual Salary} - \text{Minimum of Salary Range})}{(\text{Maximum of the Salary Range} - \text{Minimum of Salary Range})} \times 100 = \text{Range Penetration}$$

For example, if the range is \$25,000 to \$75,000 and the salary is \$45,000, the range penetration is 40%.

$$\frac{(\$45,000 - \$25,000)}{(\$75,000 - \$25,000)} \times 100 = 40\% \text{ (Range Penetration)}$$

Salary range penetration is a key indicator of pay gaps, promotions, and equity in your organization. By tracking this important metric, you'll know where exactly the salary falls within the range.

6.1.6. Broadbanding

Broadbanding, which uses fewer pay grades having broader ranges than traditional compensation systems, is increasingly being used. Broadbanding, called fat grades, means collapsing pay grades and ranges into just a few wide levels or a band, which includes one minimum and one maximum range, while midpoint often not used. The purposes of using broad banding as follow:

- Provide flexibility to define job responsibilities more broadly.
- Foster cross-functional growth and development.
- Ease mergers and acquisitions.

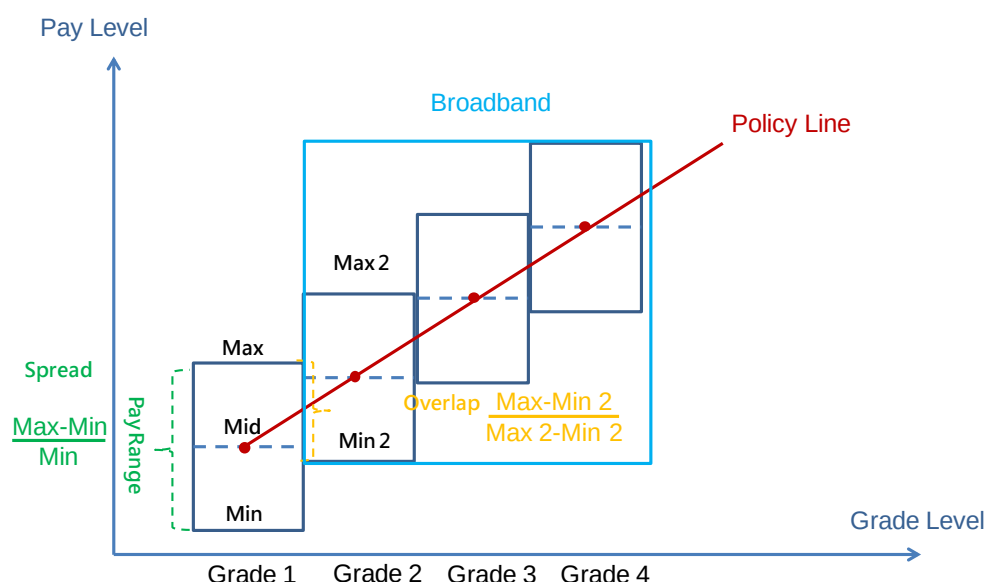
The most important difference between grades and broad banding is where the controls are located. There are several reasons why it is beneficial to reduce the number of pay grades and broaden pay ranges. First and foremost, broadbanding is more consistent with the flattening of organizational levels and the growing use of jobs that are multidimensional. With fewer bands and broader ranges, employees can shift responsibilities as market conditions and organizational needs change. Traditional questions from employees about when a promotion to a new grade occurs, and what pay adjustments will be made for temporarily performing some new job responsibilities, are unnecessary.

Another advantage of broadbanding is that employee career development can be enhanced when the artificial barriers of numerous pay grades are removed. With broadbanding, many of the control mechanisms traditionally enforced by HR

departments also are removed, and authority for more compensation decisions is decentralized to the operating managers. By allowing employees to move into other job areas and broaden their knowledge, skills, and abilities without having to deal with a large number of constraints imposed by a compensation program, the organization encourages employees to move between departments, divisions, and locations. In firms that have adopted broadbanding, employees are encouraged to move across business units and apply for openings in areas of the company other than where they have been working. This cross-functional development is beneficial because it creates more employees who have greater flexibility and broader sets of capabilities.

However, broadbanding is not appropriate for every organization. Many organizations still operate in a relatively structured manner, and the flexibility associated with broadbanding is not consistent with the traditional hierarchical culture in which executives and managers have been operating.

Another problem with broadbanding is that many employees have become "conditioned" to the idea that a promotion is accompanied by a pay raise and movement to a new pay grade. As a result of removing this grade progression, the organization may be seen as having fewer upward promotion opportunities. Furthermore, a number of individuals do not want to move across the organization into other areas.



6.2. Global Salary Grades

Global Salary Grades refers to a standardized method of classifying positions across a

global enterprise. Alternative titles would be global bands or global job evaluation. Employers often adopt global salary grades to enable internal comparisons and standardize certain elements of compensation and benefits, such as short- and long-term incentives. For example, global salary grades helps answer the question “is the Brand Manager position in Greece equivalent to the Associate Brand Manager in France or the Marketing Manager in Kenya?” Or, all staff in band C or higher are eligible for equity compensation awards.

Salary Structure is the term used to refer to the salary ranges associated with salary grades. A Global Salary Structure, by its very name, would imply a single structure for all locations globally. Sometimes you may also see this referenced as an international salary range. Some companies use a global salary structure to manage a cadre of international assignees (usually based on the headquarters market). International organizations such as the World Bank and the United Nations, and many international NGOs, use international salary structures in managing their international (expatriate) staff as well. But it would be very unusual to have a global salary structure applicable to all staff in an organization.

If you are managing a global enterprise, global grades can be very useful in several respects. In addition to the examples above allowing comparison of equivalent positions across different markets with varying titles, and standardization of executive compensation programs, global grades allow the organization to establish leading talent management processes. The global grades will help establish competencies and career tracks, and the related training and development that is required to train future leaders. Global grades also help companies manage succession planning more easily, by providing a common language to describe the challenges and complexities of an individual position.

6.3. Global Pay Structure

Salary structures are a very useful tool for all organizations. They help ensure consistency and avoid discrimination, control costs, and together with a strong performance management process, allow managers to differentiate between different positions and varying levels of performance amongst the team. Each country is a different market, however, and therefore, you need to build your structure separately for each one. Market data plays a key role here, since the structure must be anchored to the market in which you are competing for talent.

In the end, if you design a global grading system with local pay structures, you’ll get it right. The grades will give you global consistency while the structures will be tailored to the local market, guided by your global compensation philosophy, which provides

standards for each country to meet.

A salary structure is commonly used by employers to set out the range of pay, from minimum to maximum, associated with each salary grade or band. By associating each position with a grade or band, employers can use a salary structure to help manage compensation in an optimal way.

Here are ten steps to develop a salary structure for your organization, with some special considerations for international developing markets:

6.3.1. Establish your compensation philosophy

Each employer needs a policy which outlines their desired market position. What percentile of the market is your target? Which comparators are appropriate? Is the target the same for all grades? A well-articulated compensation policy provides valuable guidance for the development of a pay structure. In large organizations, there is often a corporate policy which forms the basis for local policies.

6.3.2. Gather market data

Identify surveys with your desired comparators (as specified in your company policy). Most employers prefer at least two survey sources. In international markets this can be challenging, especially in developing countries and smaller markets. Consider sector-specific surveys as well as multi-sector options – certain jobs are found across many employers, not just your sector. In smaller international markets, leading employers often provide a better proxy for the most competitive market than do sector surveys with many less sophisticated employers. Don't overlook international organizations; they pay very competitively and are often well-established in the smallest of countries.

6.3.3. Identify benchmark jobs

Benchmark jobs are those that are representative of roles found across many organizations – standard roles such as Manager, Accountant, Payroll Administrator, Secretary, Clerk and Driver. Benchmark jobs are easy to understand and match to, and will appear in multiple surveys, enabling the use of multiple sources. For professional roles specific to your sector, sector surveys could be a good source. In other cases, and with multi-sector survey sources, look for those that utilize well-developed career ladders, enabling easy cross-occupational job matching. As an example, such an approach would examine Analyst positions across different functional areas (e.g., finance, HR, procurement, marketing, etc.).

6.3.4. Measure your market position

There are several ways to do this. If you have a lot of benchmark jobs, tabulate the average of all of the roles in the same internal level or grade. Weighted averages incorporating number of incumbents associated with each survey data point is a common approach. Select the market reference from the survey most appropriate under your policy. In developing countries market data is more volatile. A good approach is to use minimum and maximum values to “bookend” the data in these markets. This helps eliminate outliers and capture more realistic market survey values.

6.3.5. Calculate the compa-ratio

Calculate the compa-ratio. This is the ratio of your data to the market — 100 means fully comparable, while a ratio under 100 indicates a below market position, and over 100, above market. There are different approaches to summarizing the data — by position, by grade, etc. Whatever approach you use, the compa-ratio analysis will illustrate which parts of the organization are competitive against the market and which ones require some attention!

6.3.6. Check your budget

This is a critical step. You can calculate the average difference between your current scale and the market. This indicates about how much of an increase would be required to make your scales fully comparable to the market. Your internal budget constraints, though, will dictate how close to this ideal you can achieve. In addition to internal budgets, consider the average market movement in your surveys, and the general inflation rates (never use inflation to determine how much more to pay staff – this is determined by cost of labor, not cost of living).

6.3.7. Start allocating

This is the start of an exercise which will repeat many times, until you get the desired result. Build a model of your organization, ideally with the number of incumbents in each grade. Using your overall percentage of market and budget number, start increasing your scale (use Mid points, or the Mins and Maxs). See how close you can get to fully comparable to the market, and how much it will cost. Does it jive? If not, tweak the data a bit. You can adjust the percentage each grade is increased, as well as examine the spans (range from min to max) and inter-grade differentials, in order to gain better market alignment. Obviously, the incumbent count of each grade will impact the overall costing model.

6.3.8. Final adjustments

Once you have built your new scale and matched it to the market as closely as possible,

and within your budget, give it a once over. Does it make sense? Are the increase amounts distributed in a pattern which will cause unrest amongst your staff? Strive to achieve a scale which will reflect your comp policy and enhance internal cohesion in the organization. This step is the art of compensation, not the science.

6.3.9. Management approval

Review your proposed scale with management, presenting your rationale, budget and overall market comparisons. Discuss concerns you may have uncovered about specific positions or grades, and educate your management about the process used. Outline your implementation plans.

6.3.10. Communicate

Develop appropriate communications for managers and staff. Let them know all of the work that went in to the exercise, and how the organization compares to the market. Be careful here — you need to obviously put on a positive spin — that's why statistics are so flexible!

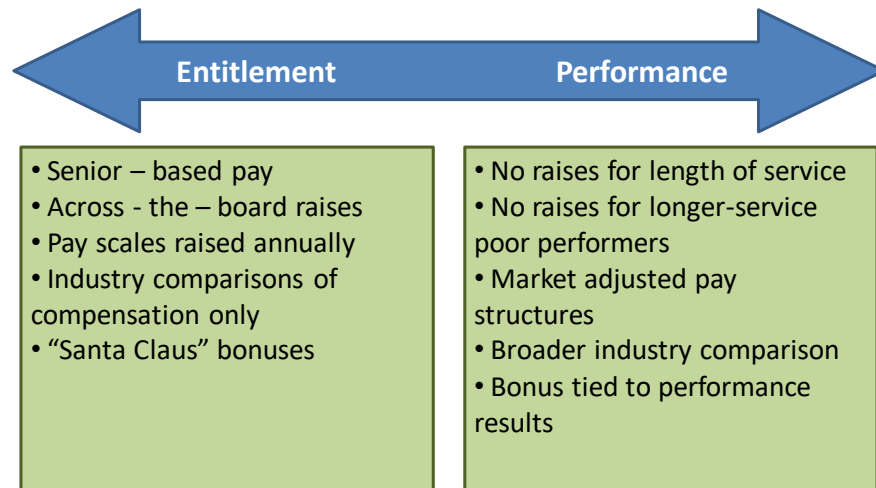
7. Individual Differentiation

There are two basic compensation philosophies, which should be seen as opposite ends of a continuum. At one end of the continuum in the below figure is the entitlement philosophy; at the other end, the performance-oriented philosophy:

7.1. Entitlement Orientation

The entitlement philosophy can be seen in many organizations that traditionally have given automatic increases to their employees every year. Further, most of those employees receive the same or nearly the same percentage increase each year. Employees and managers who subscribe to the entitlement philosophy believe that individuals who have worked another year are entitled to a raise in base pay, and that all incentives and benefit programs should continue and be increased, regardless of changing industry or economic conditions. Commonly, in organizations following an entitlement philosophy, pay increases are referred to as cost-of-living raises, whether or not they are tied specifically to economic indicators. Following an entitlement philosophy ultimately means that as employees continue their employment lives, employer costs increase, regardless of employee performance or other organizational competitive pressures. Market comparisons tend to be made within an industry, rather than more broadly considering compensation in firms of all types. Bonuses in many entitlement-oriented organizations are determined very paternalistically and often do not reflect operating results. Instead, the CEO or owner acts as Santa Claus at the end

of the year, passing out bonus checks that generally do not vary from year to year. Therefore employees “expect” to receive the bonuses as another form of entitlement.



7.2. Performance Orientation

Where a performance-oriented philosophy is followed, no one is guaranteed compensation just for adding another year to organizational service. Instead, pay and incentives are based on performance differences among employees. Employees who perform well get larger compensation increases; those who do not perform satisfactorily receive little or no increase in compensation. Thus, employees who perform satisfactorily should keep up or advance in relation to a broad view of the labor market for their jobs, whereas poor or marginal performers should fall behind.

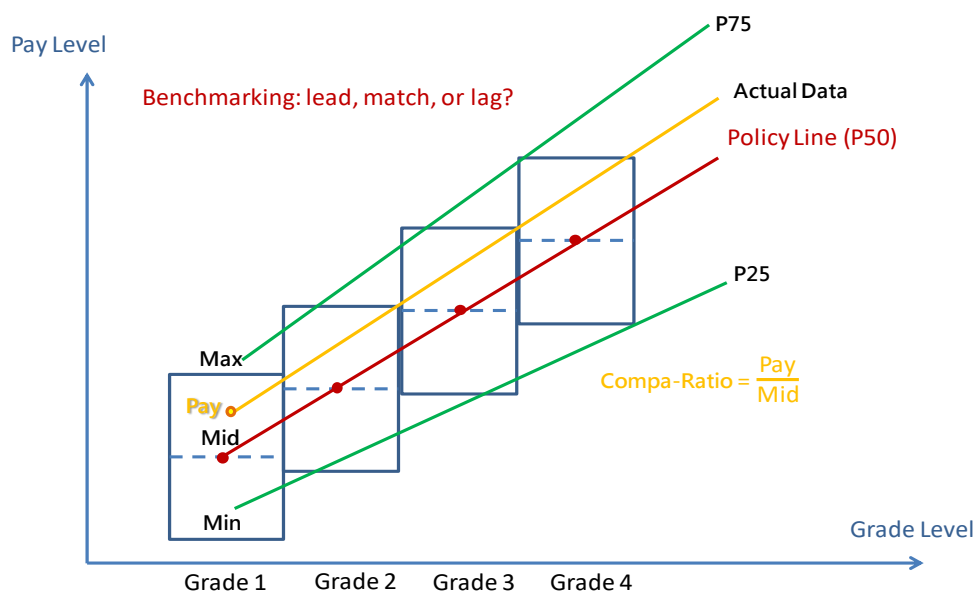
Bonuses are paid based on individual, group, and/or organizational performance results. Few organizations are totally performance-oriented in all facets of their compensation practices. However, breaking the entitlement mode is increasingly occurring in the organizational restructuring common throughout many industries. A study of public-sector HR managers found that there is a desire and need to shift toward more performance-oriented compensation practices in many public-sector organizations. How fast that occurs, given the historical traditions and the strength of public-sector unions, remains to be seen.

8. Market conformity

An organization may choose to match the market and pay approximately the same wages and offer a benefits package similar to that of the competition.

Some organizations strive to lead the market and recruit and retain the most desirable

talent from the labor pool by offering higher salaries and/or better benefits. When using salary survey data, leading the market typically equates to the 75th percentile of the market.



Other organizations deliberately, out of economic necessity or to control labor costs, lag the market and establish their pay rates or benefits levels below those offered by other employers. Reduced labor rates may enable the organization to offset other higher costs such as purchasing, distribution, or sales expenses. When using salary survey data, lagging the market typically equates to the 25th percentile of the market.

9. Internal Consistency

Once managers have determined pay ranges, they can set the specific pay for individuals. Setting a range for each pay grade gives flexibility by allowing individuals to progress within a grade instead of having to be moved to a new grade each time they receive a raise. A pay range also allows managers to reward the better-performing employees while maintaining the integrity of the pay system.

Regardless of how well constructed a pay structure is, there usually are a few individuals whose pay is lower than the minimum or higher than the maximum. These situations occur most frequently when firms that have had an informal pay system develop a new, more formalized one. Red circles green circles refers to salary of employees either above or below the salary range associated with the job which the employee is the job incumbent. If the overall staff compensation is well managed, both green-circle and red-circle rates would be fairly uncommon within the organization.

9.1. Red-Circled Employees

A red-circled job is shown on the graph in the below figure. A red-circled employee is an incumbent who is paid above the range set for the job. For example, assume that an employee's current pay is \$10.92 per hour but the pay range for that grade is between \$6.94 and \$10.06. The person would be red circled, and attempts would be made over a period of time to bring the employee's rate into grade. Typically, the red-circled job is filled by a longer service employee who has declined promotions or has been viewed as unpromotable due to insufficient education or other capabilities. Yet the individual may have continued to receive large pay increases.

Several approaches can be used to bring a red-circled person's pay into line. Although the fastest way would be to cut the employee's pay, that approach is not recommended and is seldom used. Instead, the employee's pay may be frozen until the pay range can be adjusted upward to get the employee's pay rate back into the grade. The employee can also be transferred to a job with a higher grade or given more responsibilities. This method will result in greater job evaluation worth, thus justifying the job's being upgraded. Another approach is to give the employee a small lump-sum payment but not adjust the pay rate when others are given raises. There are some solutions for red circled employees:

- 9.1.1. Regular increase. In this approach a red-circle employee receives the same increase as if he or she were not at or above the maximum.
- 9.1.2. No increase. No merit-based or seniority pay raise beyond the maximum is allowed with this approach. The "no increase" strategy ensures that the company pays only what the job is worth and makes the most sense in the context of a wage/salary structure. This approach may result in the loss of valued personnel, but such turnover can be minimized if the institution provides employees with the encouragement, training, and development opportunities necessary to qualify for higher positions.
- 9.1.3. Freeze salaries until cost of living adjustments to a revised salary range catches up with the employee. This may take years or may never be possible because employees are too far above the new pay range.
- 9.1.4. Limited or minimal increase. Under this policy, only less-than-regular increases are permitted for red-circle personnel.
- 9.1.5. Lump-sum bonus. With this approach eligible employees receive a cash payment "up front" when a rate change is due.

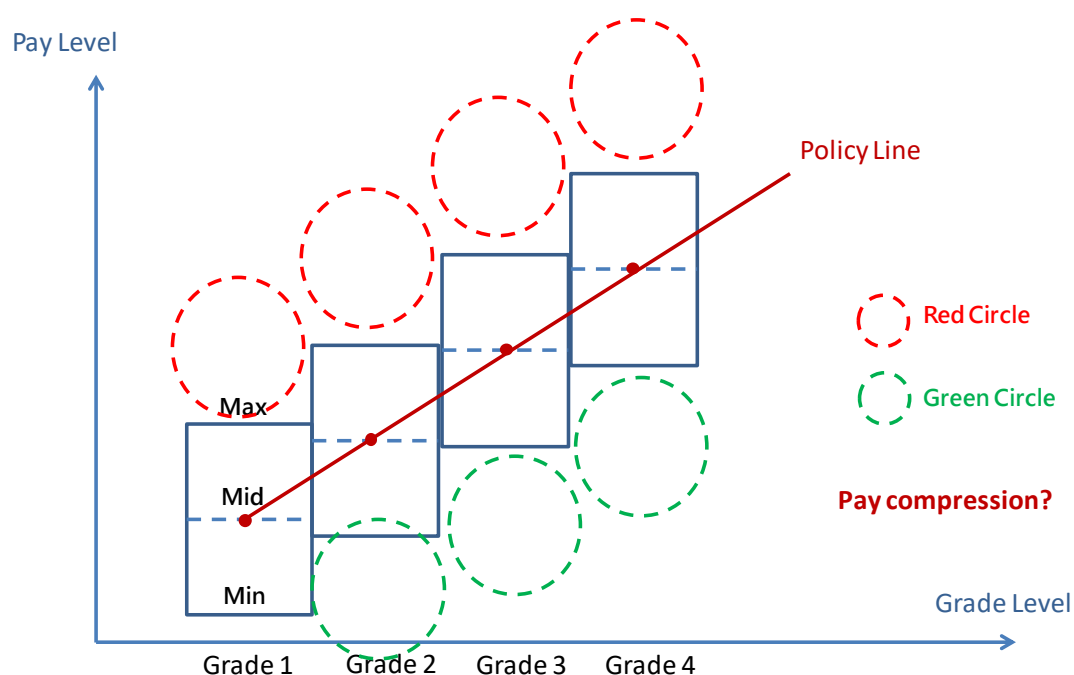
9.1.6. Allow employees to train for and transfer into higher paying jobs.

9.1.7. No established policy. Red-circle situations are handled on a case-by-case basis, with no set approach. Some red-circle employees receive regular increases; others are given limited pay raises or none at all.

9.2. Green-Circled Employees

An individual whose pay is below the range is a green-circled employee. Promotion is a major cause of this situation. Assume someone receives a promotion that significantly increases his or her responsibilities and pay grade. Typical promotion adjustments are 8% to 15%, but such an adjustment may still leave the individual below the minimum of the new pay range. Because the promotion represents such a significant increase in responsibilities, the employer may not work to increase the person's pay to the minimum until all facets of the new job are being fully performed. Generally, it is recommended that the green-circled individual receive pay increases to get to the pay grade minimum fairly rapidly. More frequent increases can be given if the increase to minimum would be large.

In the situation where green-circled employees are members of a protected group, such as union members, when salary ranges had been agreed in the collective agreement, the green circle status could look like discrimination and subject the organization to litigation, especially if other employees in the same job are all paid in the range. There are some solutions for green circled employees:



9.2.1. Immediate increase. With this approach immediately raise the employee's pay to match the adjusted range in accordance with that individual's seniority and performance. This would be the preferred method for an organization whose budget is large enough to allow such immediate action.

9.2.2. Gradual Increase. With this approach gradually raise the individual's wages to the appropriate level, starting first with an adjustment to bring the employee's pay to the minimum of the range. This would most likely be the preferred method for an organization whose budget is small.

9.3. Pay Compression

One major problem many employers face is pay compression, which occurs when the range of pay differences among individuals with different levels of experience and performance becomes small. Pay compression occurs for a number of reasons, but the major one involves the situation in which labor market pay levels increase more rapidly than an employee's pay adjustments. Such situations have become prevalent in many occupational areas, particularly those in the information technology field.

Occasionally, in response to competitive market shortages of particular job skills, managers may have to deviate from the priced grades to hire people with scarce skills. For example, suppose the worth of a specialized information systems analyst's job is evaluated at \$38,000 to \$48,000 annual salary in a company, but qualified individuals are in short supply and other employers are paying \$60,000. The firm must pay the higher rate. But suppose several analysts who have been with the firm for several years started at \$38,000 and have received 6% increases each year. These current employees may still be making less than salaries paid to attract and retain new analysts from outside with lesser experience. One solution to pay compression is to have employees follow a step progression based on length of service, assuming performance is satisfactory or better.

9.4. Pay Increases

Once pay ranges have been developed and individuals' placements within the ranges identified, managers must look at adjustment to individual pay. Decisions about pay increases often are critical ones in the relationships among employees, their managers, and the organization. Individuals have expectations about their pay and about how much increase is "fair," especially in comparison with the increases received by other employees. There are several ways to determine pay increases:

9.4.1. Pay for Performance Systems

Many employers profess to have a pay system based on performance. But relying on performance-appraisal information for making pay adjustments assumes that the appraisals are done well, and this is not always the case, especially for employees whose work cannot be measured easily. Consequently, some system for integrating appraisals and pay changes must be developed and applied equally. Often, this integration is done through the use of a pay adjustment matrix, or salary guide chart. Pay adjustment matrices base adjustments in part on a person's compa-ratio, which is the pay level divided by the midpoint of the pay range.

In many organizations, pay-for-performance systems are becoming a popular way to change the way pay increases are distributed. In a truly performance oriented system, no pay raises are given except for increases in performance. Giving pay increases to people because they have 10 to 15 years' experience, even though they are mediocre employees, defeats the approach. Further, unless the performance-based portion of a pay increase is fairly significant, employees may feel it is not worth the extra effort. Giving an outstanding industrial designer making \$40,000 a year the "standard raise" of 4% plus 1% for merit means only \$400 for merit versus \$1,600 for "hanging around another year."

9.4.2. Seniority

Seniority, or time spent in the organization or on a particular job, can be used as the basis for pay increases. Many employers have policies requiring that persons be employed for a certain length of time before they are eligible for pay increases. Pay adjustments based on seniority often are set as automatic steps once a person has been employed the required length of time, although performance must be at least satisfactory in many nonunion systems. A closely related approach uses a maturity curve, which depicts the relationship between experience and pay rates. Pay rises as an employee's experience increases, which is especially useful for professionals and skilled craft employees. Unlike a true seniority system, in which a pay raise occurs automatically once someone has put in the required time, a system using maturity curves is built on the assumption that as experience increases, proficiency and performance also increase, so pay raises are appropriate. If proficiency does not increase, theoretically pay adjustments are reduced, although that seldom happens in practice. Once a person plateaus in proficiency, then the pay progression is limited to following the overall movement of the pay structure.

9.4.3. Cost-Of-Living Adjustment (COLA)

A common pay-raise practice is the use of a standard raise or cost-of-living adjustment (COLA). Giving all employees a standard percentage increase enables

them to maintain the same real wages in a period of economic inflation. Often, these adjustments are tied to changes in the Consumer Price Index (CPI) or some other general economic measure. However, numerous studies have revealed that the CPI overstates the actual cost of living. Unfortunately, some employers give across-the-board raises and call them merit raises, which they are not. If all employees get a pay increase, it is legitimately viewed as a cost-of-living adjustment having little to do with merit or good performance. For this reason, employers should reserve the term merit for any amount above the standard raise, and they should state clearly which amount is for performance and which is the “automatic” COLA adjustment.

9.4.4. Lump-Sum Increase (LSI)

Most employees who receive pay increases, either for merit or seniority, first have their base pay adjusted or then receive an increase in the amount of their regular monthly or weekly paycheck. For example, an employee who makes \$12.00 per hour and then receives a 3% increase will move to \$12.36 per hour. In contrast, a lump-sum increase (LSI) is a one-time payment of all or part of a yearly pay increase. The pure LSI approach does not increase the base pay. Therefore, in this example the person’s base pay remains at \$12.00 per hour. If an LSI of 3% is granted, then the person received \$748.80 (computed as 36¢ per hour * 2080 working hours in the year.) However, the base rate remains at \$12.00 per hour. It is that base rate upon which overtime is figured, and keeping the base rate static slows down the progression of the base wages. It also allows for the amount of the “lump” to be varied, without having to continually raise the base rate. Some organizations place a limit on how much of a merit increase can be taken as a lump-sum payment. Other organizations split the lump sum into two checks, each representing one-half of the year’s pay raise.

As with any plan, there are advantages and disadvantages. The major advantage of an LSI plan is that it heightens employees’ awareness of what their performance “merited.” A lump-sum check also gives employees some flexibility in their spending patterns so that they can buy big-ticket items without having to take out a loan. In addition, the firm can slow down the increase of base pay, so that the compounding effect of succeeding raises is reduced. Unionized employers have negotiated LSI plans as a way to hold down base wages, which also holds down the rates paid for overtime work. Pension costs and some other benefits, often tied to base wages, can be reduced as well.

One disadvantage of LSI plans is administrative tracking, including a system to handle income tax and Social Security deductions from the lump-sum check. Also, workers

who take a lump-sum payment may become discouraged because their base pay has not changed. Unions generally resist LSI programs because of this and because of the impact on pensions and benefits. To some extent, this problem can be reduced if the pay increase is split to include some in the base pay and the rest in the lump-sum payment.

10. Job vs. Person Based Pay

Pay scales have traditionally been defined by the qualifications, experience and knowledge required to perform job duties at a certain level. In other words, pay is centered on the job, not the person. Skill-based pay, also referred to as knowledge-based pay, is person-focused. Workers are compensated for each new skill that allows them to perform new tasks on the job. As workers gain each additional skill, their pay rate goes up. Some companies believe that learning a certain sets of skills leads to higher productivity and, therefore, embrace the idea of skill-based pay.

The underlying objectives of any compensation system are to attract, motivate and retain good staff. But which compensation system is most likely to achieve that goal? The answer, not surprisingly, is that it depends.

There is no “magic bullet” — only a choice about what's right for your particular practice. There are literally hundreds of variations to choose from, but they are all derived from just a few theoretical models, which can be categorized as either base pay or performance pay. Most practices use some combination of the two categories to leverage the strengths of each. This article will examine two models of base pay — paying for the job and paying the person — as well as models that involve extra pay for performance — merit pay and practice-effectiveness pay.

	Job-Based	Person-Based
Employee focus	Seek promotions to earn more pay	Seek skills/competencies
Procedures	Job analysis Job evaluation	Skill/competence analysis Certification
Advantages	Clear expectations Sense of progress Pay based on value of work performed	Continuous learning Flexibility Reduced work force Lateral movement
Limitations	Potential bureaucracy Potential inflexibility	Potential bureaucracy Requires cost controls

Although no single model is right for everyone, the practice-effectiveness model does offer a number of advantages. Because this formula combines base salaries with variable bonus payments that depend on the performance of the practice, it helps control operating costs; rewards the right behaviors and builds unity; works with a variety of payment structures; encourages self-management and innovation; and breaks down bureaucracy. But before we analyze it, let's look at its rivals.

10.1. Paying for the job

Paying for the job is the “traditional” model that most people know. Each position is slotted into a grade level and weighted based on the education and experience the job requires and the number of staff who report directly to the person in the position. Pay raises are scheduled as an employee's tenure with the practice increases. The traditional model is designed to serve as a cost-control tool and to establish each job's relative worth in a practice.

The traditional model has a number of advantages:

- It facilitates centralized control. It gives an organization criteria with which to evaluate whether individual physicians or managers are paying their staff too much. It also makes budgeting relatively easy and makes salary expenditures predictable.
- It's a useful tool for evaluating internal pay equity. Because compensation for all jobs in the practice is based on one system, you can easily compare what staff across the practice are earning.
- It facilitates market testing of your pay scale's competitiveness. It allows a job in one practice to be scored using measures that are comparable with those used in other practices. With some of the widely used systems, extensive survey data are available to help practices set their pay levels based on what similar practices are paying.
- It has the appearance of objectivity. Although quantification doesn't ensure fairness, it does make a pay system consistent. Staff members may not be completely satisfied with their compensation, but at least they won't see the pay system as arbitrary.

In short, the traditional pay model can be appropriate if your practice needs high levels of internal equity and centralized control of compensation. But the traditional model has several disadvantages:

- It can inflate the pay system's operating costs. After implementing a traditional

base-pay system, a practice may need to hire a consulting firm to provide ongoing compensation audits and survey data. In addition, the traditional model is a high producer of records and administrative overhead because it requires that each job be evaluated (with supporting documentation) and that the pay grades be revised annually.

- It encourages point grabbing and inefficiency. Staff members become quite sophisticated in how to get their jobs scored highly in compensation reviews. The traditional model rewards people for creating overhead and higher costs because overseeing larger budgets and more subordinates leads to higher pay.
- It compromises honesty in job descriptions. People quickly realize that the way to beat the system is to create flamboyant and overly inclusive job descriptions. Over time, the practice can end up paying everyone excessively.
- It rewards the wrong behavior. Giving a person more money simply for taking on new responsibilities rewards job changes rather than outstanding performance or development of needed skills.
- It doesn't accurately reward the performance of talented staff. Because compensation is determined by an employee's level and the job's rating, the model limits your flexibility to reward people based on their individual performance. For example, no matter how well a first-year billing clerk performs, he or she will earn less than someone who has been doing an average job for the last four years. This can hurt the motivation of your best performers and encourage them to look for jobs elsewhere.
- It reinforces a vertical career orientation. More responsibilities, especially supervisory and managerial, lead to more money. This drives your best technical and clinical staff into roles where they may not be as effective, and it does little to encourage the development of technical and clinical skills. This is especially counterproductive in practices that are implementing total quality management (TQM), continuous quality improvement (CQI) or other team approaches to improving problem solving, operational efficiency and clinical outcomes.
- It reinforces hierarchy and bureaucracy. By assigning value to jobs in terms of their hierarchical position and level of control, the traditional model fosters unnecessary and undesirable pecking orders and power relationships.

In short, the traditional model offers consistency and the perception of fairness in a practice's compensation system. But be careful: Once implemented, it can become a dominant part of a practice's culture and have unintended, counterproductive

results.

10.2. Paying the person

The alternative to job-based pay is to compensate staff according to the value of their skills in the market. The most common approach is competency-based pay. This model is designed to motivate staff to develop the competencies — knowledge and skills for performing specific work — that the practice needs to accomplish its objectives. This model is most appropriate for practices that need high levels of intra-group teamwork, intergroup collaboration and adaptability to change.

Advantages of the competency-based model include these:

- It can lead to a broader perspective for staff. When this model is combined with a participatory management style, it encourages and rewards cross-training, learning and the assignment of responsibilities based on the skills that staff possess (rather than their “positions”). In turn, staff learn more about how the practice works, resulting in a big-picture understanding of what improvements are needed. This broader perspective allows staff members to be more innovative in making the practice more efficient.
- It reinforces a culture of improvement. The model delivers a tangible reward to staff for growing, learning and developing new areas of competency. It is compatible with TQM, CQI and similar approaches to improvement.
- It facilitates self-management and enables leaner staffing. Because the model rewards staff members for developing new skills, it prepares them to be more productive, take on greater responsibility and work more collaboratively with other staff. It also reduces the need for physician oversight. Maximizing the staff's potential can lead to leaner, flatter staffing configurations — and substantial overhead savings.
- It improves staff retention. Because they can develop skills continuously, staff members have more control over their pay. They are unlikely to find comparable jobs elsewhere because most organizations still use the traditional model.
- It builds acceptance for change. This model helps staff become more accepting of change because in it change represents the potential for professional growth — and better pay. As staff learn to accept change, the practice becomes better able to react to staff turnover, expansions, mergers or changes in the health care environment.

There are several disadvantages of the competency-based model as well:

- It produces high pay rates. As staff become more valuable to the practice and their tenure increases, individual salaries will increase. This doesn't necessarily mean that total payroll costs will rise. In fact, they can be lower than those generated in a traditional model, if the practice can use its fewer, but more competent, staff more effectively.
- It requires a large investment in training. Because peers train each other, productivity will decline initially. Physicians must be committed to staff training as the means of competency acquisition, and they must be patient early in the implementation process, giving the model a chance to produce the expected results.
- Market comparisons can be more difficult. Since most survey data relate to the traditional pay model, staff-salary comparisons may not be straightforward. You can overcome this challenge by examining data about what others pay for certain competency mixes rather than direct job-by-job comparisons.
- Individuals can “top out.” Practices generally establish an income ceiling for staff who master all competencies, but employees in the traditional model can also reach this kind of limit. In a competency-based model, this is less of an issue since staff have higher pay scales than traditional models offer.
- Administrative involvement can increase. Keeping track of each person's competency assessments, competency mix and pay rate requires time and effort. A computerized record-keeping system can help you deal with this. A competency-based pay model requires practices to commit to ongoing staff training and to developing an administrative infrastructure that will support the system. It may also require some mental effort to step outside the box of traditional thinking.

11. Compensation Communications

Managing a company's compensation program is a balancing act, with your company's needs on one hand and your employees' needs on the other. Your company needs to offer a budget-passing yet competitive salary and benefits package because it translates into better individual, team, and company performance. Your employees want to earn what they're worth and feel valued for their time and talents. You need to create a win-win, and engaging employees in the compensation conversation is a step in the right direction.

If HR stop and think about it, it's really all about managing employee expectations: if they believe they are being compensated fairly and can look forward to future rewards, they are likely to remain loyal employees; if they perceive their compensation as “less than,”

they will seek greener pastures. And the lynchpin to managing expectations with respect to compensation is – you guessed it – effective communications.

11.1. Goal of Compensation Communication

For your employees (present and future) to see their compensation package as the tremendous offering that it truly is, they need to understand it. This starts with grasping your company's compensation philosophy, your base pay system, and the role your culture plays in promoting and supporting career growth. If your compensation communications don't connect the dots between their pay, performance, and career development, maybe now is the time to evaluate your communications plan.

11.2. Timing of Compensation Communication

If you're simply informing employees of their pay when they complete new hire documentation and sign-off on their annual reviews, challenge your HR team and management to make it a regular topic of group or individual discussion. Motivate employees at different points throughout the year. Monthly or quarterly in general terms (promoting a bonus program or employee awards luncheon) and two or three times during face-to-face meetings (formal and semi-formal employee reviews). And take the opportunity to reassure employees during periods of change, such as expansion, downsizing or restructuring, and remind them of your company's goals and how their work contributes to it.

11.3. Information of Compensation Communication

Be as clear, straightforward, and explicit about your compensation up to the level of transparency your company is comfortable with. Remember, you're "selling" this information to employees to help them see the value in all you offer, helping to manage their expectations, and encouraging them to buy-in to your programs. You'll want to include details about:

- How base pay is calculated — pay grade and pay range structures, relative to experience and education levels
- Explanation on any pay changes — increases/decreases and how they're connected to the job market, performance, and cost of living trends; criteria for raises and bonuses (especially in a pay-for-performance system), timing for awards and payments
- Learning and career development opportunities — next steps, performance markers, criteria for advancement

- How benefits such as health insurance, stock options, or tuition reimbursements factor into their total compensation
- Relevant source material such as market data to back-up pay adjustments

And, don't forget to promote your "feel-good" programs or extras that are not necessarily reflected in paychecks. These might include an employee of the week program, free lunch Fridays for top performers, gold star award ceremonies, etc.

Information about compensation should always come from HR or management. Ideally, messages will get shared and reinforced by both. In fact, you may want to develop a separate communications plan and training program for managers to help them understand your company's compensation programs and encourage their buy-in so they can effectively talk to employees about them.

All forms of media can support employee understanding and acceptance of the total compensation package, so conform to your employees' preferences. Outside of one-on-one employee review meetings, you can share personalized compensation-related information with employees through total rewards statements or pay raise letters mailed to their homes. More general, guideline-specific information can be given in educational meetings held by benefits company representatives, through e-mail newsletters, or on the company intranet.

Part Two: Incentive Programs

1. Incentive Compensation

Internationalization or increased global reach is creating pressure for greater consistency in compensation strategies. One might expect just the opposite given the need to be sensitive to culture and local market differences between countries and regions.

However, the convergence toward consistency is primarily at the philosophical or core levels. Performance incentive programs are rapidly being deployed in many parts of the world. There is increasing evidence that the strategies to deliver pay are becoming more uniform from one country to the next.

Incentive pay is paying for performance beyond normal expectations, which is designed to motivate employees to perform at higher levels. Traditionally, all incentive plans are pay-for-performance plans. They all tie employees' pay to the employees' performance.

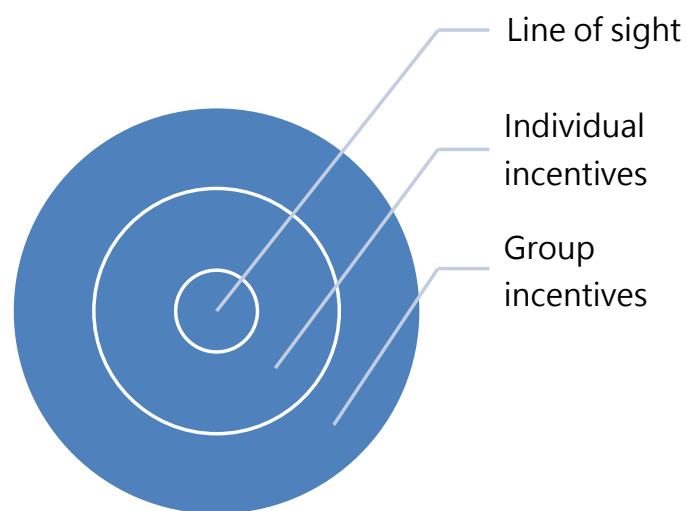
Variable pay is more specific: It is usually an incentive plan that ties a group or team's pay to some measure of the firm's overall profitability.

Individual performance

- Merit pay
- Piecework
- Sales compensation
- Cash awards
- Recognition programs

Group performance

- Gain-Sharing
 - The Scanlon plan
 - The Rucker Plan
 - Improshare plan
- Profit-sharing
 - Deferred profit-sharing
- Risk-sharing plans
- Employee stock ownership plans (ESOP)
- Performance-sharing plans



Incentive Plan

Source: Newman, Milkovich, & Gerhart (2022)

1.1. Principle of Incentive Plan

- 1.1.1. The plan must be in concert with other organizational programs.
- 1.1.2. The plan must be in the line of sight—employees must be able to influence the attainment of the goal and see the direct results of their efforts.
- 1.1.3. The plan must have a sunset clause—outlining a defined time period and have a specified end.
- 1.1.4. The plan must incorporate both short- and long-term perspectives. An overlapping perspective may make it difficult for a key performer to leave the organization without incurring a significant loss of money (sometimes referred to as the 'golden handcuffs' approach).

1.2. Line of sight

"Line of sight" is a favored term among compensation professionals and is crucial in the design of incentive plans—if they are expected to actually impact performance. Its origins stem from the military, where it means "distance to the target." In the context of employee motivation and rewards, it denotes an employee's perceived ability to impact a specific performance metric. This is important because the core purpose of most incentive plans is to direct employee focus and effort towards achieving improvements—increasing revenues, enhancing profits, elevating customer satisfaction, etc. If the chosen improvement metric for incentive awards is perceived by employees as outside their influence, the expected outcome may not materialize.

So, how do you reduce the line of sight and engage employees in effecting change? It often involves more than just selecting a single pivotal metric; it also requires effective communication and education. For instance, if your organization aims to increase profits but most employees are unclear on how the business generates income, there's a disconnect. When employees arrive each day with a clear understanding of what they need to do within their specific role to drive profits, you can dangle the proverbial carrot and anticipate positive results.

1.3. Individual Incentives

Incentive plans are implemented to motivate specific behaviors or performance standards in staff through monetary or other forms of rewards. Individual plans may prompt top performers to excel further, yet they could potentially intimidate or discourage those who perform at lower levels.

1.3.1. Encouraging Maximum Effort

For a high-achieving performer with no ceiling to their potential, an individual incentive plan can spur them to reach peak performance. This is notably impactful in sales, where financial incentives grow with the individual's performance level. The staffer is aware that her income correlates with her performance and that generating more revenue translates to a larger paycheck. For business owners, this model has the advantage of compensating excellence without additional costs.

1.3.2. Motivating Other Staffers

Individual incentive plans can engender a competitive spirit within an organization, motivating employees to match or exceed the performance of their high-achieving peers. These plans eliminate the 'blame game,' with success or failure resting solely on the individual, reinforcing that they are masters of their own financial destiny.

1.3.3. Lack of Teamwork

However, an 'every person for themselves' atmosphere can undermine the propensity for teamwork and collaboration. Staff members may hesitate to assist each other in incentive-driven tasks, fearing that their colleagues may gain an advantage or claim credit for their work. This dynamic can foster a stressful work environment, leading to internal conflict and potentially low morale. Disparities in lead distribution or support can exacerbate these issues if staff perceive the allocation as unfair.

1.3.4. High Turnover Potential

Individual incentive plans are often tied to commission-based earning structures. Simply put, if performance falters, so do earnings. The stress of inconsistent pay can demoralize staff, prompting high turnover as employees seek more stable compensation elsewhere. High turnover is detrimental to business, incurring costs associated with recruiting, hiring, and training replacements.

1.4. Group Incentives

Group incentive plans can motivate staff towards achieving specific goals, knowing that their extra efforts—like reaching earnings targets—will be rewarded.

1.4.1. Group Incentive Pros

Creating a group incentive plan can bolster relationships among staff, urging collaborative efforts to meet group objectives. This approach builds stronger teams, fosters brainstorming, and instills a collective sense of project ownership. Knowing

they must each contribute significantly for the group to succeed can mitigate underperformance, while encouragement and positive peer pressure utilize everyone's strengths towards common goals.

1.4.2. Group Incentive Cons

However, when team members perform at significantly different levels, group incentives can precipitate workplace tension, especially if some feel they are shouldering more work. This can breed resentment and a toxic work atmosphere. Lower-performing employees may feel undue pressure, while high performers might feel undervalued, receiving the same rewards as less motivated colleagues for more effort.

1.4.3. Making it Work

To effectively implement a group incentive plan without fostering discord, objectives and each individual's role within the group should be clearly defined. By setting explicit expectations, it's less likely for a small fraction of the group to end up doing the majority of the work. Regular progress reports on both individual and group levels can help identify and address underperformance early on.

1.4.4. Other Considerations

Consider a hybrid incentive strategy that includes both group incentives and individual rewards for exceptional performance. This approach ensures top performers are motivated to excel, contributing to high-level group outcomes while also acknowledging outstanding individual contributions. This strategy can promote healthy competition and enhance productivity and motivation without breeding resentment.

2. Individual Performance Pay Plans

"Pay for performance is typically a financial incentive that employees receive for meeting certain performance objectives or targets. Companies use this type of system to motivate employees to achieve results that increase profits or improve service. Incentives may include bonuses for perfect attendance, meeting specific service quality targets, and achieving certain sales growth targets. Incentive payments are usually added to an employee's regular salary or hourly pay but may comprise the majority of earnings in certain professions.

Compensation for sales representatives often falls under the pay for performance

concept. Commissions earned are directly related to the sales volume that a representative achieves. While not all sales positions have the same pay structure, many in this profession are primarily based on sales results, and there may be additional bonuses for reaching certain sales volumes within a specified period.

The main idea behind this payment concept is to create a direct link between an employee's job performance and their pay. In short, the more an employee produces, the more financial reward they receive. In addition to cash bonuses and commissions, companies may use other types of pay for performance incentives, such as extra vacation or personal time off.

Individual Incentive Plans are the established standards against which employee performance is compared to determine the magnitude of incentive pay.

2.1. Merit Pay

A merit pay system links increases in base pay to how highly employees are rated on subjective performance evaluations. However, just small pay increase ranges can hinder performance. Merit pay involves giving employees a permanent pay raise based on past performance. Often, the company's performance appraisal system is used to determine performance levels, and employees are awarded a raise, such as a 2% increase in pay. One potential issue with merit pay is that employees may come to expect pay increases. In companies that give annual merit raises without separate raises for cost-of-living increases, merit pay can become essentially a cost-of-living adjustment, creating a sense of entitlement among employees, with even low performers expecting them. Thus, making merit pay more effective depends on its true dependence on performance and the design of a relatively objective appraisal system.

To effectively motivate employees, the size of the merit increase must be significant enough to make a noticeable difference. Generally, any merit increase of 2% or less is seen as inconsequential. Some studies suggest that a merit increase of less than 7% is unlikely to impact employee performance. An alternative increasingly used by companies in today's tight economy is lump-sum payments instead of a merit increase to base pay. As a result, the employee receives the pay increase in one payment, which hopefully motivates them, and the company maintains the same base salary, controlling salary budget costs over the long run.

Ultimately, for a merit pay program to be successful, awards given to top performers must be substantially greater than those given to average or below-average performers. Furthermore, especially in today's economic climate, it is advisable not

to reward below-average performers at all. A well-designed system gives employees a personal stake in ensuring their efforts lead to increased productivity and success for the organization as a whole.

2.2. Piecework

Piecework is the oldest and still one of the most popular individual incentive plans. Workers are paid a sum (called a piece rate) for each unit they produce. In per-piece pay structures, payment is based on the number of pieces of work completed. The worker is paid a monetary rate for each piece of work, with the rate defined in advance. The hourly wage for a worker engaged in piecework will vary based on their skill and the time it takes to complete each piece.

Piecework, especially when done from home, may have no set time frame for completion, but some jobs have hourly or daily quotas. Piecework has been used in manufacturing since the Industrial Revolution and continues today, particularly in developing nations. It is also used in fields like data entry, translation, writing, editing, and call centers, where pieces might be defined as per-minute talk time, per call, per word, per page, or on a project basis.

It is important to note that only employees are protected by minimum wage laws, not independent contractors. Per-piece pay structures are often used as pay rates for freelancers or independent contractors.

2.3. Sales compensation

Both bonus and commission plans are common sales incentive compensation approaches to attract, motivate, and retain salespeople. The structure of the plan—bonus, commission, or mixed—depends on several aspects of a firm's selling process and environment.

2.3.1. Bonus Plans

In a bonus plan, each salesperson is typically given a quota for a territory, and incentive payments are tied to performance relative to defined quota gates, targets, or thresholds. For example, a salesperson might receive a bonus payment at 90% of quota, another at 100% attainment, and another at 110%. Bonus plans often include a sizeable salary component so that if salespeople do not sell enough to earn the bonus, they can still earn a decent living.

Because most bonus plans have a significant salary component, they are often

attractive to salespeople with a long-term focus who want to build a career with a firm. They also appeal to those interested in problem-solving, consulting, and servicing customers in addition to selling.

2.3.2. Commission Plans

Commission plans pay a continuous rate for every sale. A commission rate is multiplied by a performance measure, such as sales or gross profits, to determine the payout. The rate may vary by product, customer, or the level of performance attained. For instance, a salesperson might earn 3% on sales up to a goal and 5% beyond it. Many commission plans include a salary component, but the variable part is typically larger than in a bonus plan. Salespeople on commission plans often rely on their earnings from commissions as an important part of their income.

Commission plans with a high variable pay and low salary can attract result-oriented salespeople confident in their selling abilities. However, these plans may also lead to little firm loyalty, with salespeople potentially leaving for better offers and taking customers with them.

By tailoring the sales incentive compensation plan to the selling process and environment, firms can create a design that drives sales by attracting, motivating, and retaining salespeople, consistent with the desired salesforce culture.

2.4. Cash Award

A performance-based cash award, often known as a rating-based award, recognizes an employee's performance over an entire rating period. The award must be based on a rating of record of "fully successful" or higher. Agencies must design their performance-based cash award programs to reflect meaningful distinctions in performance levels, ensuring higher-rated employees receive larger cash awards.

Employees within the same awards pool should receive awards that reflect meaningful distinctions based on their individual rating of record. However, when comparing awards across different pools or organizations, it's possible that an "Outstanding" employee in one pool may receive a lower award amount than a lower-rated employee in another pool.

Agencies have the flexibility to design their awards programs to meet their needs and reflect their culture, as long as they ensure the performance-based awards amount to meaningful distinctions in performance. Awards may be calculated as a lump-sum dollar amount, a percentage of base pay, or another method, such as assigning shares to rating levels.

2.4.1. Percentage of Base Pay

Agencies can design their awards programs to grant employees with higher ratings larger cash awards as a percentage of base pay than those with lower ratings. Locality pay is included in this calculation as it is considered part of base pay.

2.4.2. Lump-Sum Dollar Amount

Agencies can design their awards programs to grant employees with higher ratings larger cash awards as a lump-sum dollar amount than those with lower rating

2.5. Recognition Programs

An employee goes above and beyond and receives a gift card or lunch with the boss; a team meets a goal and is rewarded with a party. However, these rewards can backfire as they may suggest the employee's worth is limited to a monetary value for a certain level of effort. Recognition should be about more than money; it's about positive feedback, acknowledgment of extra effort, and the celebration of achievements.

Financial rewards are valuable but are not the same as recognition—it's a short-term solution. Recognition is a vital tool in employee retention because people need acknowledgment of extra effort. An effective recognition approach should be timely, contextually relevant, appropriately scaled, authentic, and tied to the employee's perception of value.

2.5.1. In the Moment

Acknowledge exemplary work when you see it. Be specific, descriptive, and measured—routine punctuality does not usually warrant recognition.

2.5.2. In Context

Recognition tied to business goals or results-focused activities is more impactful than random affirmations. Noticing an employee's extra effort in achieving business success is crucial.

2.5.3. Appropriate in Volume/Scale

Recognition should be proportional to the effort and results to maintain its meaning. Avoid arbitrary recognition.

2.5.4. Authentic, Not Automatic

Recognition must be genuine. Automated systems risk losing the personal touch that

makes recognition effective.

2.5.5. Tied to the Employee's Perception of Value

Recognition should reflect an employee's value to the organization beyond monetary terms. Appreciation for extra effort and intelligence often means more than money.

3. Group Performance Pay Plans

A group-based incentive pay plan financially compensates employees for the goals they meet as a collective group, rather than as individuals. Employers who use this method find that the approach brings a sense of urgency to the group effort, resulting in greater performance and goal attainment than when individuals work alone. It also fosters a greater sense of camaraderie among coworkers.

Group performance incentives reward group members for meeting or exceeding performance standards, often in an egalitarian manner (each person receives the same percentage of pay or flat dollar award). However, this system can lead to perceptions among high performers that their contributions are not being individually recognized. It can also allow marginal performers to share equally in the award.

3.1. Gainsharing

In gainsharing, 'gain' refers to savings. An employee or team shares in the savings realized by a business as a result of their suggestion. Gainsharing is based on the premise that those doing the work know best how to improve the product, service, or process. Savings are determined by comparing historical data with actual costs after implementing a suggestion. If a cost saving is realized, those who made the suggestion receive a percentage of the gain.

Gainsharing presents an opportunity for industry to improve plant performance and productivity while reducing costs associated with poor quality (e.g., waste, spoilage, rejects, and customer returns). It is a group incentive, pay-for-performance wage system—a group bonus where the entire workforce shares the benefits of improved productivity and reduced rejects and rework. The productivity gains over a five-year period should be substantial, with costs of rejects and rework significantly reduced.

A successful gainsharing program depends on a sound formula, based on careful examination of past company performance, and thorough training of all workforce levels on their roles in gainsharing.

3.1.1. Scanlon Plan

The Scanlon plan is a model for business organization that involves employees in corporate decision-making processes to benefit from their suggestions and contributions. Employees are rewarded through profit-sharing plans that distribute a portion of the economic benefits generated by an engaged workforce.

3.1.2. Rucker Plans

Rucker Plans employ a committee system where the savings gain is based on 'value added'—the increase in goods' value at each production stage—and is calculated by comparing labor costs with sales minus the cost of goods sold. These plans are typically used in manufacturing, where costs are stable over time.

3.1.3. Improshare Plans

An Improved Productivity Through Sharing (Improshare) Plan sets standards for product or service-delivery time based on historical data. These standards form the baseline against which improvements are measured. Savings indicate a change in the relationship between labor (inputs) and outputs (final product or service).

3.2. Profit Sharing

Profit sharing, a variable pay plan, involves designating a percentage of annual profits as a pool to share with employees. The money generated is then distributed across eligible employees using a formula.

3.2.1. Pros of Profit Sharing

Profit sharing unites employees with common goals and reinforces their shared service to customers.

3.2.2. Cons of Profit Sharing

The weakness of profit sharing is that individual employees may not see the impact of their work on company profitability, potentially leading to entitlement rather than motivation.

3.2.3. Deferred Profit Sharing Plan (DPSP)

A DPSP is a retirement plan where employer contributions are based on company profitability. Contributions grow tax-deferred until withdrawal.

3.3. Risk-Sharing Plans

Risk variable pay plans, sometimes referred to as risk-sharing plans, are compensation

structures that place a portion of an employee's weekly, monthly, or yearly earnings at risk. If employees meet or exceed their performance goals, they not only recover the at-risk portion of their compensation but also receive additional incentives. Conversely, if they fail to meet their goals, they forfeit some of the pay they would have otherwise earned.

The design of shared-risk plans provides sponsors with the flexibility to adjust employee contributions and benefits, or both, in response to fluctuations in the plan's financial status due to market downturns, demographic longevity changes, or inflation.

3.4. Employee Stock Ownership Plans (ESOPs)

An Employee Stock Ownership Plan (ESOP) is a method allowing employees of a company to own shares in the company they work for. There are various ways employees can acquire company stocks and shares. They can receive them as a bonus, purchase them directly from the company, or acquire them through an ESOP.

In a non-leveraged ESOP, the employer contributes stock or cash, or offers employee discounts to buy stock. This stock is then allocated to the employees' accounts. Non-leveraged ESOPs aim to provide employees with an ownership stake in the company at a relatively low cost to the company and help create a market for the employer's stock. In a leveraged ESOP, the employer borrows money from a financial institution or the plan sponsor to finance company stock, instead of directly contributing cash or stock. The employer establishes a trust, known as an employee stock-ownership trust, to manage this process.

3.5. Performance-Sharing Plan

Performance-sharing plans utilize predetermined criteria and standards to measure results, and based on these measurements, they establish a fund for incentive awards. These criteria may include factors beyond profits, such as quality and customer satisfaction. A Performance Share Plan enables employees to earn actual stock in their company. The company sets specific financial objectives, and upon achieving these objectives, stock grants are awarded to the employees.

4. Non-Financial Incentive Plans

While many companies still rely on conventional incentive pay programs, which are straightforward to implement and monitor, this approach may not effectively motivate all employees. For those who don't view monetary rewards as their primary motivator, alternative employee performance program ideas based on total rewards

could be more impactful:

4.1. Team Building and Social Events

Recognizing employees' hard work through social events is crucial. After a particularly demanding week, organizing a party at the office or off-site activities can enhance team spirit. Regular social events, such as monthly team outings to exhibitions, lunches, or engaging in group activities like laser tag, can significantly improve collaboration and interpersonal relationships, leading to long-term productivity gains.

4.2. Professional Development Opportunities

Investing in your employees' professional growth can be a powerful motivator. Providing learning opportunities and allowing staff to choose courses of interest can encourage them to stay longer with the company. Even if they choose courses unrelated to their current roles, the diverse knowledge gained can contribute positively to the team dynamics and overall work environment.

4.3. Flexible Working Schedules

Allowing employees to tailor their work schedules can lead to increased efficiency and job satisfaction. Flexibility in scheduling helps them balance personal responsibilities, leading to better focus and productivity at work. Implementing flexible hours should be gradual, ensuring employees maintain a 40-hour workweek. You might experiment with different models, such as a 9/80 work schedule over two weeks, to find the best fit for your team.

4.4. Green Commuting Incentives

With environmental consciousness on the rise, encouraging employees to adopt green commuting habits can be beneficial. Offering bonuses or transport cost reimbursements for carpooling, walking, biking, or using public transport not only supports eco-friendly practices but also promotes a positive company image.

4.5. Wellness and Health Programs

Everyone appreciates a bit of personal care. Establishing a wellness and health benefits program in your company can be a great way to acknowledge your employees' hard work. Providing gym memberships or on-site massage services can help reduce stress, increase focus, and improve overall health, contributing to a happier and more productive workforce.

4.6. Workplace Amenities

The relationship between workplace amenities and non-financial incentive programs lies in their shared goal of enhancing employee satisfaction and motivation without relying on direct financial compensation. Workplace amenities, such as comfortable office spaces, recreational facilities, on-site childcare, or flexible work options, are part of the broader category of non-financial incentives. Workplace amenities directly impact the day-to-day experiences of employees at their place of work. They are tangible, often visible elements that can enhance the immediate work environment, making it more enjoyable and conducive to productivity. These incentives are used by employers to create a more engaging and supportive work environment.

Companies need to consider what types of amenities they can provide to foster a positive office environment. While not every business can emulate Google with nap pods or volleyball courts, there are basic and more attainable amenities that are cost-effective and can make a significant difference. These amenities, as well as some extra offerings, can distinguish companies from their competitors.

4.6.1. The Basics

Technology and IT Support: Providing up-to-date computers, ample-sized monitors, reliable Wi-Fi, functional printers, scanners, copiers, video conferencing, and wireless charging is essential.

Food Options: Expanding beyond coffee and tea to include a variety of snacks, refreshments, and lunches, with consideration for food allergies and healthy choices.

Comfortable Seating: Ensuring that seating is ergonomic to prevent discomfort and back pain among employees.

Office Design: Creating an aesthetically pleasing workplace with thoughtful design and natural light, which has a direct impact on recruiting and retention.

Pumping Room: Offering a private, clean space for breastfeeding mothers.

Collaboration Spaces: Providing areas where employees can brainstorm and work creatively without disturbances.

4.6.2. Going the Extra Mile

Sit-to-Stand Desks: These desks can contribute to productivity and employee wellness.

Wellness Programs: Implementing programs for gym reimbursement, free flu shots, smoking cessation, weight loss, and stress management.

Outdoor Space: When feasible, providing outdoor areas for benefits in memory, focus, mental wellbeing, and creativity.

Child Care Support: Offering free or discounted childcare, which can significantly help working parents.

Relaxation Areas: Designating spaces for relaxation or napping.

Games: Adding games like ping pong, pool, or video games for recreational breaks.

4.6.3. Above and Beyond

Commuter Shuttles: Providing shuttles can reduce employee stress, increase office time, and boost productivity.

On-Site Fitness Centers and Classes: Helping employees integrate exercise into their schedules.

On-Site Healthcare: This can lower company medical costs, improve long-term employee health, reduce absenteeism, and boost productivity.

Treadmill Desks: Taking the concept of active working further.

Concierge Services: Offering assistance with personal tasks like dry cleaning, booking flights, or grocery shopping.

Before implementing these amenities, some companies conduct surveys to ascertain employee preferences. Strategic planning in designing amenity spaces, considering the placement of quiet versus social areas, is also crucial.

It's important to note that adding meaningful amenities doesn't necessarily require more space but rather the smart utilization of existing space. For businesses actively seeking new space, expert assistance can be invaluable in managing the process.

Part Three: Payroll and Benefits

1. Employee Benefits

A benefit is an **indirect reward** given to employees for organizational membership. These often include retirement plans, paid vacations, health insurance, educational assistance, and many other programs. In many countries, both citizens and employers are taxed to pay for government-provided benefits such as health care and retirement programs. Benefits can be costly for employers in developed countries, averaging 30% to 40% of payroll expenses, and in highly unionized industries like manufacturing and utilities, they may exceed 70% of payroll.

Employee benefits encompass a variety of additional compensation offerings, including health insurance, retirement savings options, and paid time off. Employers provide these benefits to not only attract and retain highly skilled employees but also to boost their productivity and commitment to the organization. The significance of these benefits lies in research findings that suggest employees who perceive recognition and value from their employers tend to demonstrate higher loyalty and productivity. Furthermore, certain benefits are mandated by legal requirements.

1.1. Objectives of Benefits

Employee benefits are a crucial element of the overall compensation package, often tipping the scales for job seekers evaluating multiple offers. They play a significant role in enhancing employee productivity, engagement, and loyalty.

According to a survey by the Society for Human Resource Management, 90% of respondents consider healthcare benefits to be extremely or highly essential. Additionally, 83% regard flexible work schedules and leave as critically important.

1.1.1. Attracting Talent

Employee benefits are a key factor in a candidate's decision-making process when considering job offers. A comprehensive benefits package can be the deciding factor for a candidate choosing between multiple job opportunities.

1.1.2. Enhancing Engagement

Offering benefits such as paid leave, healthcare, retirement plans, flexible working hours, and wellness programs has been linked to higher levels of engagement among employees. These benefits contribute to a more satisfied and motivated workforce.

1.2.3. Improving Retention

Employee benefits play a significant role in an employee's decision to stay with their current employer. A substantial portion of employees considers benefits like healthcare, flexible work options, and retirement plans crucial in their choice to remain with a company, thereby reducing turnover.

1.1.4. Meeting Employee Expectations

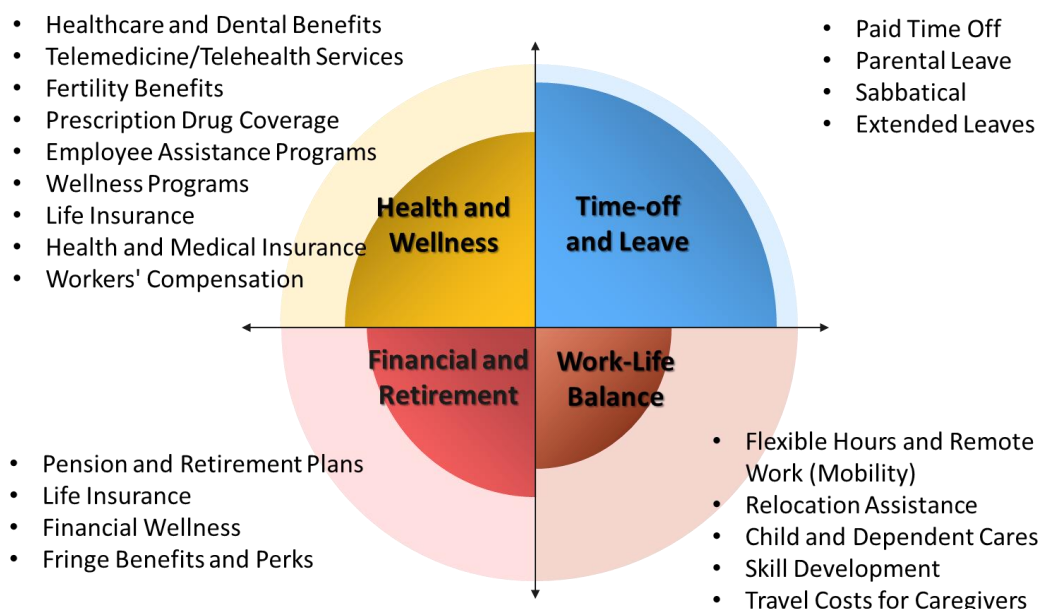
A significant percentage of employees view certain benefits, especially healthcare and flexible work arrangements, as extremely or very important. This indicates that offering these benefits meets and potentially exceeds employee expectations, leading to greater overall job satisfaction.

1.1.5. Legal Compliance

Some employee benefits are not just perks but legal requirements. Offering these benefits ensures compliance with employment laws and regulations, avoiding potential legal issues.

1.2. Key Employee Benefits

Employee benefits are crucial components of employee compensation packages, influencing job offer considerations, productivity, engagement, and retention. Key types of employee benefits include:



1.2.1. Health and Wellness Benefits

This encompasses health insurance, dental and vision insurance, prescription drug coverage, employee assistance programs, and wellness initiatives.

1.2.2. Financial and Retirement Benefits

These involve retirement savings plans such as pension schemes, employee stock ownership plans, profit-sharing arrangements, and financial planning support.

1.2.3. Time-off and Leave Benefits

Encompassing vacation days, sick leave, paid holidays, parental leave, and extended leave options.

1.2.4. Work-Life Balance Benefits

Including flexible work arrangements, remote work options, childcare support, and eldercare assistance.

1.3. Specific Benefit Plans

Certain benefits are mandated by law for employers to provide to their employees. These include assurances of a paid holidays, provision for sick leaves, and specific social security insurance coverages like workers' compensation and unemployment insurance. The details of these benefits can differ based on the labor laws of each country or state. Additionally, employers often provide other benefits, not legally required, to make their employment packages more appealing.

1.3.1. Pension and Retirement Plans

These are financial arrangements that help employees secure their financial future post-retirement. There are two main types: defined benefit plans, which guarantee a certain payout at retirement based on the employee's length of service and salary history; and defined contribution plans, where employees contribute a fixed amount or a percentage of their paychecks in an account intended to fund their retirement. In some cases, employers may also match a portion of employee contributions.

1.3.2. Healthcare and Dental Benefits

These are insurance coverages that pay for employees' medical and dental care expenses. They are typically offered through a group health plan that includes a network of healthcare providers. The coverage can range from preventive care, hospitalization, surgery, and prescription drugs, to dental check-ups, orthodontics, and oral surgeries.

1.3.3. Telemedicine/Telehealth Services

These are healthcare services delivered remotely via digital platforms. They allow employees to consult with healthcare professionals over the phone or video call, get

prescriptions, and manage their health conditions without the need to travel. This not only provides convenience and saves time but can also lead to early diagnosis and treatment of health issues.

1.3.4. Fertility Benefits

These benefits provide coverage for fertility treatments, helping employees who are struggling with infertility. Coverage can include procedures like in vitro fertilization (IVF), intrauterine insemination (IUI), and egg or sperm freezing services.

1.3.5. Prescription Drug Coverage

This is a part of a health insurance plan that covers the cost of prescription drugs. It helps employees afford the medications they need for acute conditions like infections, chronic conditions like diabetes or heart disease, or preventive drugs like vaccines.

1.3.6. Employee Assistance Programs (EAP)

Employee Assistance Programs (EAPs) are initiatives sponsored by employers that provide confidential counseling and support services to employees grappling with personal or work-related challenges. These challenges can range from stress and anxiety to family issues and financial difficulties. The goal of EAPs is to help employees navigate these issues, leading to enhanced mental health, job satisfaction, and productivity.

One of the most popular employee benefits is Mental Health Assistance, which encompasses programs like EAPs. These programs offer support to employees dealing with personal or work-related mental health issues. They grant access to licensed mental health professionals who provide counseling and support through various channels, including in-person meetings, phone calls, and online sessions. The primary objective of these programs is to help employees manage stress, anxiety, and other mental health concerns, ultimately boosting their well-being and productivity.

1.3.7. Paid Time Off (PTO)

PTO policies give employees paid leave from work, allowing them to rest and rejuvenate. This can include vacation days, sick leave, personal days, and sometimes even volunteer days. PTO contributes to work-life balance, employee satisfaction, and productivity. In some cases, sick leave is a type of employee benefit that provides paid time off from work for employees to recover from an illness or injury. It's intended for health-related purposes, allowing employees to address their health needs without losing pay. Sick leave can be used for various health needs, including mental health days and scheduled doctor's appointments. Some policies also allow employees to use

their sick leave to care for sick family members or to address health and safety needs related to domestic violence or sexual assault.

Unlimited Time Off: This is a relatively new approach to employee leave where employees are allowed to take as much time off as they need, subject to certain company policies and manager approval. The idea is to promote work-life balance and trust in employees to manage their own time effectively.

1.3.8. Flexible Hours and Remote Work (Mobility)

These benefits provide employees with flexibility in their work schedules and locations. Flexible hours allow employees to vary their start and end times, while remote work allows employees to work from home or another location outside the office. These options can help employees balance work with personal responsibilities and preferences, and can contribute to employee satisfaction and retention.

Mobility benefits can make your employees' life a lot easier. Because even if they can work from home or elsewhere, they'll still have to come into the office – or workplace – regularly. This category covers things like public transport and cars but also bicycles and carpooling.

1.3.9. Relocation Assistance

This benefit is offered to employees who need to move in order to take a job with the company. Relocation assistance can cover a variety of moving-related expenses, such as packing and transportation costs, temporary housing, and real estate services. Some companies may also provide assistance with job search for a relocating spouse or partner.

1.3.10. Parental Leave

This is a period of leave provided to new parents around the time of childbirth or adoption. Parental leave can be paid or unpaid, and the duration and pay level can vary widely. In some countries and states, parental leave is mandated by law, requiring employers to provide a certain amount of leave to new parents.

1.3.11. Sabbatical

A sabbatical is a period of paid or unpaid leave that allows employees to take a break from work for an extended period of time. Sabbaticals are often used for personal or professional development, such as pursuing further education, conducting research, or traveling. The duration of a sabbatical can vary, but it is typically longer than regular vacation time.

1.3.12. Child and Dependent Cares

These benefits provide support for employees with childcare or dependent care responsibilities. They can include flexible work hours, telecommuting options, on-site childcare facilities, or financial assistance for childcare services.

1.3.13. Life Insurance

This is a benefit where the employer pays a premium for a policy that provides a financial payout to the employee's designated beneficiaries in the event of the employee's death. This can provide financial security for the employee's family.

1.3.14. Health and Medical Insurance

Health insurance policies are designed to cover a broad range of medical expenses, including preventive care, doctor visits, and prescription drugs. On the other hand, medical insurance policies provide coverage for specific medical expenses related to a serious illness or injury. Health insurance is usually part of a comprehensive benefits package that may include other types of insurance and benefits. These can range from basic health benefits such as outpatient and inpatient care, coverage for dependents, and inclusion of pre-existing conditions, to popular additional benefits like maternity and fertility coverage, vision and dental insurance, and extended benefits like health checks and immunizations.

Health insurance and medical insurance are often used interchangeably, but they can have slightly different connotations in certain contexts. Medical insurance could refer to specific types of coverage such as Workers' Compensation Insurance or Disability Insurance, which are designed to protect employees in case of work-related injuries or disabilities.

1.3.15. Workers' compensation

Workers' compensation is a benefit required by law in most countries. This legal mandate ensures that employees who suffer job-related injuries or illnesses receive appropriate medical care and compensation for lost income during their recovery. As a statutory requirement, it provides a uniform framework for employers to support workers in these situations, offering a critical safety net. The coverage typically includes medical expenses, rehabilitation, disability benefits, and, in some cases, death benefits for dependents. This legal obligation underscores a global commitment to workplace safety and the well-being of employees.

1.3.16. Fringe Benefits and Perks

These are additional benefits provided by employers that go beyond salary and legally mandated benefits. They can include a wide range of perks such as employee discounts on company products or services, commuter benefits like transit passes or parking allowances, and amenities at work such as free meals, food and beverage, fitness facilities, or childcare services. These benefits aim to enhance the workplace environment and improve employee satisfaction and retention.

Gifts, clubs, activities as part of employee benefits refer to various non-monetary perks provided by employers to enhance the work environment and employee satisfaction.

Gifts: These can include items given to employees on special occasions, such as work anniversaries, birthdays, or holidays. They can also be rewards for achieving certain milestones or goals.

Clubs: These are organized groups within the workplace that share a common interest. Examples can include book clubs, running clubs, or knitting clubs. They provide a way for employees to socialize and engage in activities outside of their regular work tasks.

Activities: These can range from team-building exercises, company outings, volunteer opportunities, to wellness programs. They aim to foster a sense of community, improve employee morale, and promote a healthy work-life balance.

1.3.17. Wellness programs

Employee wellness programs are a set of initiatives offered by a company to encourage a healthy lifestyle among its employees and their extended families. These programs are designed to maintain or improve well-being through proper nutrition, weight loss, and preventive education. They can include various aspects of wellness such as physical, mental, financial, and spiritual health.

Physical Wellness Program: These programs are designed to encourage a healthy lifestyle among employees. They can include fitness challenges, health screenings, nutritional advice, and preventive care.

Mental Wellness Program: These programs aim to support the mental health of employees. They can include stress management education, counseling services, and resources to help employees manage mental health concerns.

Financial Wellness Program: These programs aim to help employees manage their finances effectively, reducing financial stress. They often include education on budgeting, debt management, and future savings.

Spiritual Wellness Program: These programs support employees' spiritual needs and

encourage personal growth. They can include promoting mindfulness, offering opportunities for reflection, and facilitating open and honest communication.

1.3.18. Skill Development

Skill development for employee benefits refers to the initiatives taken by an organization to enhance the abilities and competencies of its employees. This can include professional training, learning opportunities, and courses or training sessions provided for an entire team, department, or organization. These initiatives aim to help employees gain knowledge, improve their skills, and better equip them to advance in their careers. They can lead to increased growth in one's career, continuous learning, and upskilling.

Allocating resources towards the growth of individuals is beneficial, irrespective of whether they continue to utilize these skills within the organization or not. This approach called "professional development funding" is effective as it provides individuals with the autonomy to choose their learning path and challenge themselves. However, when this component is absent, individuals tend to become unsettled in their quest to tackle new issues or learn about subjects that hold more significance for them.

1.3.19. Travel Costs for Caregivers

A rising trend among companies is to offer benefits that cover travel costs for caregivers. This is particularly useful for employees traveling with a baby or toddler under the age of two. For instance, some companies will cover the cost of a plane ticket for a caregiver to accompany the employee and child. This is especially beneficial for nursing mothers. In addition, some companies offer to cover the cost of shipping breast milk home if a mother is traveling for work and needs to pump.

1.3.20. Experiential Benefits

As the influence of artificial intelligence and the metaverse grows in our daily lives, companies are increasingly offering experiential benefits that connect employees with nature. This trend is a response to the desire for balance, encouraging employees to step outside of their digital environments and engage with the natural world. Some companies have even introduced unique offerings that combine leadership development with interactions with animals, including wolves, wild animals in Kenya, and horses.

1.4. Part-Time Employee Benefits

These are benefits offered to employees who work less than full-time hours. The scope

of these benefits can vary, and they may include pro-rated versions of the benefits offered to full-time employees, such as health insurance, retirement plans, and paid time off. Some companies may also offer unique benefits for part-time workers, such as flexible scheduling or job sharing options.

1.5. Benefits for different generations

Different generations of workers (often) want different things. We've already seen this in our article about generational differences in the workplace.

As each generation is in a different stage of their lives, it's no surprise that they tend to appreciate different types of employee benefits. After all, young Millennial parents have other priorities than a close-to-retirement Baby Boomer, right?

Employee benefits can be classified into two categories: those that employees find most important and those they most appreciate. Let's see what the overview looks like per generation.

When we look at the benefits that are most appreciated by employees, the top 5 per generation looks slightly different. All of a sudden things like food & beverage and mobility pop up on various lists. The number one among pretty much every generation, however, is health & wellness.

It's interesting to see that financial wellness is something that the youngest generation in the workforce, Generation Z, has in its top five. As companies will increasingly hire people from Generation Z, financial wellness will probably become a more important employee benefit.



Source: www.aihr.com

- Baby boomers are anyone born from 1946 to 1964
- Generation X is anyone born from 1965 to 1980.
- Millennials are anyone born from 1981 to 1996.
- Generation Z is anyone born from 1997 to 2012.
- Generation Alpha is from 2012 to 2024.

1.5.1. How to Motivate Baby Boomers

For many in the Baby Boomer generation, work is closely tied to self-worth. They are often motivated by titles, traditional perks, and prestige. Recognizing and rewarding their work accomplishments is effective for managing Baby Boomer employees. Generally goal-oriented, they usually prefer minimal feedback, operating under the assumption that no news is good news. They respond well to motivational milestones like promotions and prestigious job titles. However, Baby Boomers may find it challenging to adapt to flexible, non-hierarchical workplace structures.

1.5.2. How to Motivate Generation X

Gen X-ers, often having grown up with significant alone time, are comfortable working independently. They introduced the concept of work-life balance, influenced by witnessing their parents' experiences during economic downturns in the 1980s. Consequently, they value perks like flexible schedules and telecommuting. Gen X appreciates autonomy and being able to make their own choices in the workplace, including task selection and methods of work.

1.5.3. How to Motivate Gen Y (Millennials)

Millennials are known for frequently changing jobs, with pay and benefits being key factors in their employment decisions. However, they also value flexibility, options, and professional development opportunities. To retain Millennials, HR managers should focus on offering mentorship and career advancement opportunities to prevent feelings of stagnation and encourage growth.

1.5.4. How to Motivate Gen Z

Similar to Millennials, Gen Z seeks fulfillment and purpose in their work. They value corporate social responsibility and diversity and inclusion efforts. Having witnessed the Great Recession of 2008, they are motivated by financial security, appreciating benefits like bonuses, defined contributions, student loan repayment, and tuition reimbursement. Gen Z's tech-savviness means they adapt quickly to new technologies

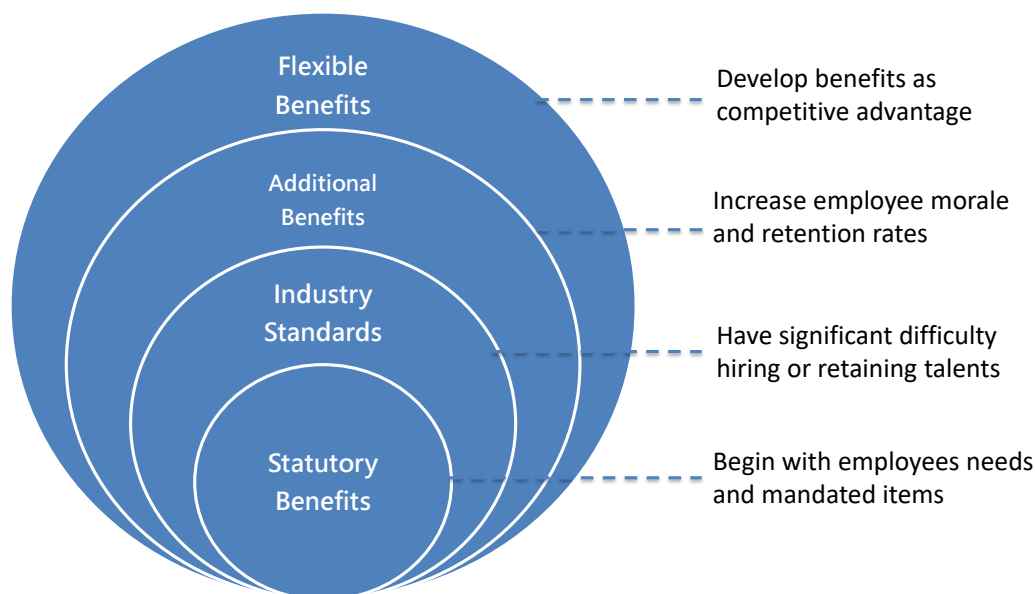
and often prefer technological solutions in the workplace.

Both Millennials and Gen Z are digital natives, comfortable with technology from a young age. While this doesn't mean that Baby Boomers and Gen X are less capable with technology, their approach may differ. Implementing technology that streamlines processes can satisfy employees across all generations.

2. Benefits Design

An effective employee benefit program aims to achieve several key objectives. Firstly, it should provide financial security for employees and their families in cases of illness, disability, death, or unemployment. Secondly, it enhances employee morale, thereby supporting the overall productivity of the company. Lastly, a well-designed benefits program serves as a powerful recruitment and retention tool, attracting quality talent without incurring excessive costs for the business.

Benefit plans can offer flexibility and choice to employees or be standardized across the organization. Many employers are discovering that providing some level of choice and flexibility enables employees to customize their benefits according to their individual needs. However, offering a wider range of choices also increases the administrative burden.



Corporate strategies and a well-defined compensation philosophy are crucial in developing employee benefits. This strategic decision positions the business in the marketplace and influences how employees perceive the company compared to competitors. Considerations include the company's values, the available benefits budget, and the types of employees the company aims to attract and retain.

For example, a company excelling in innovative product design needs to hire and retain top-notch product engineers, necessitating competitive compensation to minimize turnover. Similarly, a business focused on exceptional customer service must attract and retain the best customer service representatives, and the benefits offered to these two employee groups may vary significantly.

2.1. Statutory Benefits

Start by including basic, legally mandated employee benefits such as unemployment insurance, workers' compensation insurance, and social security.

2.2. Industry Standards

Next, consider which optional benefits are essential. Some benefits have become industry standards, and their absence might hinder the hiring and retention of talented staff. These often include health insurance, life insurance, paid and sick leave, retirement plans, and flexible compensation plans.

2.3. Additional Benefits

Further enhance your benefits program with options like tuition reimbursement, flexible spending accounts, child care subsidies, retail discount programs, telecommuting options, legal insurance, bonus plans, and wellness programs. These additional benefits can significantly boost employee morale and reduce turnover.

2.4. Flexible Benefits

Assess which benefits are most valued by your employees. Surveys can help determine which benefits are most appealing. A cafeteria plan is an employee benefits plan that allows employees to select from various options, tailoring a benefits package to meet their and their family's needs. Such plans can include different health insurance levels, other insurance options, tax advantages like flexible spending accounts, and retirement plan contributions.

2.5. Part-Time Employee Benefits

Deciding whether to extend benefits to part-time employees is another important consideration. While many companies don't offer extensive benefits to part-timers, some provide benefits proportional to the amount of work they contribute. For businesses opting to offer part-time benefits, establishing a minimum number of hours for eligibility is common. Starting with relatively easy and inexpensive benefits like flextime and telecommuting can be beneficial. Consult a labor attorney or your state's department of labor for detailed guidance on offering benefits to part-time

employees.

3. Flexible Employee Benefits

As part of both benefits design and administration, many employers offer employees choices for benefits. A flexible benefits plan allows employees to select the benefits they prefer from groups of benefits established by the employer. Sometimes called a flex plan or cafeteria plan, these plans have a variety of “dishes,” or benefits, available so that each employee can select an individual combination of benefits within some overall limits.

As a result of the changing composition of the workforce, flexible benefits plans have grown in popularity. Flexible benefits systems recognize that individual employee situations differ because of age, family status, and lifestyle. For instance, dual-career couples may not want the same benefits from two different employers. Under a flex plan, one of them can forgo some benefits that are available in the partner’s plan and take other benefits instead.

A problem with flexibility in benefits choice is that an inappropriate benefits package may be chosen by an employee. A young construction worker may not choose a disability benefit, but if that person is injured, the family may suffer financial hardship. Part of this problem can be overcome by requiring employees to select a core set of benefits (life, health, and disability insurance) and then offering options on other benefits.

Another problem can be adverse selection by employees, whereby only higher-risk employees select and use certain benefits. For example, only employees with chronic illnesses might choose health insurance. Because insurance plans are based on a group rate, the employer may face higher rates if insufficient numbers of healthy employees select an insurance option.

Because many flexible plans have become so complex, they require more administrative time and information systems to track the different choices made by employees. Despite the disadvantages, flex plans will likely continue to grow in popularity.

3.1. Flexible Spending Accounts

Flexible spending accounts, often called reimbursement accounts, are conceptually similar to a bank savings account. Employees deposit funds through the year and use them for health care, dependent care and other qualified expenses. An employer may also contribute to these accounts but is under no obligation to do so. The three basic

types of flexible spending accounts are premium-only, medical and dependent care. Premium-only plans allow employees to deposit funds for medical and life insurance premiums. Medical FSAs allow employees to set aside funds for health costs not covered by health insurance, and dependent care FSAs allow savings for day care and other expenses.

3.2. Transportation Plans

Transportation benefit plans allow employees to deposit funds to pay for commuting expenses, parking expenses or both. Eligible commuting expenses include passes, tokens and vouchers purchased for travel on buses, trains, ferries and other forms of mass transit. Eligible parking expenses include parking at or near the workplace and transit station park-and-ride lots. Ineligible commuting and parking expenses include transportation by personal car, cab fares, traffic tickets, tolls and gas.

3.3. Cafeteria Plans

As discussed, cafeteria benefit plans give employees the choice of receiving a selection of nontaxable benefits, cash or some other taxable benefit. Employers can offer only some benefits through these plans, such as health and life insurance, disability and dental coverage, pension plans, day care and elder care. The funding may come from the employer, the employee or both. Employers may also provide spending credits, which employees can use to select benefits from a range several options.

4. Benefits Administration

Benefits administration is the process of establishing, maintaining, and managing benefits for the employees of an organization. Employee benefits typically include medical insurance, pension plans, individual retirement accounts (IRAs), vacation time, sick time, and maternity leave.

A good benefits administration program creates and maintains an enrolment profile for every employee, keeping track of information such as the date hired, marital status, number of dependents, total hours worked, and attendance records. The program offers flexibility, taking into account special employee needs, part-time and temporary hires, and changes in government regulations. The benefits administration program can function in tandem with tax preparation software, ensuring that all allowable deductions are taken and maintaining detailed records for reference in case of an audit.

4.1. Benefits and HR Technology

The spread of HR technology, particularly Internet-based systems, has significantly changed the benefits administration time and activities for HR staff members.

Internet and computer-based systems are being used to communicate benefits information, conduct employee benefits surveys, and facilitate benefits administration. Recent research shows that these systems can decrease expenses, increase positive communication, and effectively connect people across many different HR functions, including benefits management.

4.2. Benefits and HR Outsourcing

Administering employee benefits can be quite complex. Understanding the considerations involved in the process will assist you in deciding whether you should handle your benefits administration on your own or outsource all or part of it. However, administering even a few employee benefits can be complex and will be time-consuming. Only you can make the decision as to whether you should handle your employee benefit administration or hire someone else to take over the job.

In today's market, HR departments are able to find an able administrator for a fair price, so that they can concentrate more of their time on what they know best. Among those who provide administrative services for a fee are insurance companies, consulting firms, banks, payroll service companies, and investment brokers.

One significant trend affecting HR is that outsourcing of benefits administration may be necessary. A study indicated that they were outsourcing more benefits functions. The most frequently outsourced item is Employee Assistance Plans (EAP). Administrative activities related to retiree benefits, pension plans, and flexible spending accounts also are often outsourced.

4.3. Benefits and HR Metrics

The significant costs associated with benefits require that analyses be conducted to determine the payoffs for the benefits. With the wide range of benefits that are offered, numerous HR metrics can be used.

- Benefits as a percentage of payroll (pattern over a multiyear period)
- Benefits expenditures per full-time-equivalent (FTE) employee
- Benefits costs by employee group (full-time vs. part-time, union vs. nonunion, management, professional, technical, office, etc.)
- Benefits administration costs (including staff time multiplied by the staff pay and benefits costs per hour)
- Health care benefits costs per participating employee

Some common benefits that employers track using HR metrics are workers' compensation, wellness programs, prescription drug costs, leave time, tuition aid, and disability insurance. The overriding point is that both benefits expenditures generally, and costs for individual benefits specifically, need to be measured and evaluated as part of strategic benefits management.

4.4. Benefits and Cost Control

Because benefits expenditures have risen significantly in the past few years, particularly for health care, employers are focusing more attention on measuring and controlling benefits costs, even reducing or dropping benefits offered to employees. The common means of benefits cost control is **cost sharing**, which refers to having employees pay for more of their benefits costs. A lot of global companies use this means. The next three means of health care cost control are using wellness programs, adding employee health education efforts, and changing prescription drug programs. Sometimes it is more cost effective for individuals to purchase benefits directly from providers, and some companies also are negotiating contracts with providers to offer benefits at reduced rates. Companies might also consider consolidating benefits packages into more streamlined offerings so that costs can be minimized.

4.5. Benefits and Communication

Benefits communication and satisfaction of employees with their benefits are linked. For instance, employees often do not fully understand their health benefits, a situation that can cause individual dissatisfaction. Consequently, many employers should consider developing special benefits communication systems to inform employees about the monetary value of the benefits they provide. Employers can use various means, including videos, CDs, emails, electronic alerts, newsletters, and employee meetings. All these efforts are done to ensure that employees are knowledgeable about their benefits. Some of the important information to be communicated includes the value of the plans offered, why changes have to be made, and the fundamental financial costs of the plans.

When planning benefits communication efforts, it is important to consider factors such as the timing and frequency, the communication sources, and the specialized content. Any significant changes to benefits should be communicated by the top managers in the organization, and these communications should be supported by HR professionals and other key managers who are well-informed to answer any questions. HR professionals should also collect feedback about benefits programs.

Some employers give individual employees a "personal statement of benefits", as well

as total reward statement, that translates benefits into dollar amounts. Increasingly, firms are using the Internet to provide statements, and these statements often are used as part of a total rewards education and communication effort.

5. Retirement and Savings Plan Payments

A pension plan is a type of retirement scheme created and financed by both employers and employees. There are two primary types of qualified retirement plans: traditional defined benefit plans and defined contribution plans. A defined benefit plan calculates benefits using a formula that factors in salary and length of service, such as one percent of compensation for each year of service, favoring employees with longer tenures. On the other hand, a defined contribution plan involves specific contributions from both employees and employers into individual accounts for each participant. Hybrid plans exist as well, blending features of both defined benefit and defined contribution plans.

Relative Advantages of Different Pension Alternative

<i>Defined Benefit Plan</i>	<i>Defined Contribution Plan</i>
1. Provides an explicit benefit which is easily communicated	1. Unknown benefit level is difficult to communicate
2. Company absorbs risk associated with changes in inflation and interest rates which affect cost	2. employees assume these risks
3. More favorable to long service employees	3. More favorable to short-term employees
4. employer cost unknown	4. Employer cost known up front

5.1. Defined-Benefit Pension Plans

A “traditional” pension plan, in which the employer makes the contributions and the employee will get a defined amount each month upon retirement, is no longer the norm in the private sector. Through a defined-benefit plan, employees are promised a pension amount based on age and service. The employees’ contributions are based on actuarial calculations on the benefits to be received by the employees after retirement and the methods used to determine such benefits. A defined-benefit plan gives employees greater assurance of benefits and greater predictability in the amount of benefits that will be available for retirement. Defined-benefit plans are often preferred by workers with longer service, as well as by small business owners. If the funding in a defined-benefit plan is insufficient, the employer may have to make up the shortfall.

5.2. Defined-Contribution Pension Plans

In a defined-contribution plan, the employer makes an annual payment to an employee's pension account. The key to this plan is the contribution rate; employee retirement benefits depend on fixed contributions and employee earnings levels. Profit-sharing plans, employee stock ownership plans (ESOPs), and the US 401(k) plans are common defined-contribution plans. Because these plans hinge on the investment returns on the previous contributions, the returns can vary according to profitability or other factors. Therefore, employees' retirement benefits are somewhat less secure and predictable. But because of their structure, these plans are sometimes preferred by younger, shorter-service employees.

5.3. Cash Balance Pension Plans

Some employers have changed traditional pension plans to hybrids based on ideas from both defined-benefit and defined-contribution plans. One such plan is a cash balance plan, in which retirement benefits are based on an accumulation of annual company contributions, expressed as a percentage of pay, plus interest credited each year. With these plans, retirement benefits accumulate at the same annual rate until an employee retires. Because cash balance plans spread funding across a worker's entire career, these plans work better for mobile younger workers.

5.4. Early Retirement Plan

Many pension plans include provisions for early retirement to give workers voluntary opportunities to leave their jobs. After spending 25 to 30 years working for the same employer, individuals may wish to use their talents in other areas. Phased-in and part-time retirements are alternatives being used by individuals and firms. Some employers use early retirement buyout programs to cut back their workforces and reduce costs. Employers must take care to make these early retirement programs truly voluntary.

6. Payroll Administration

Payroll administration involves organizing and managing the compensation of employees for their work hours. This includes recording hours worked, determining pay rates, and processing employee payments. Businesses using commission-based systems particularly benefit from having a dedicated payroll administrator to effectively handle these tasks.

In small businesses, the owner often initially handles payroll duties due to a smaller number of employees. To streamline this process, software solutions are commonly used for easy payment processing and tracking. Such software not only simplifies issuing

paychecks but also aids in maintaining financial records, facilitating direct deposits, and managing company accounts for payroll funding.

As a business grows and the number of employees increases, maintaining accurate payroll records becomes more critical. Proper payroll management ensures accurate compensation for each pay period and timely payment delivery. Payroll administrators play a key role in this process, ensuring accuracy in accounting and payroll.

An essential part of payroll management is the accurate deduction of payroll taxes from employee earnings. This task can become complex and may lead to hiring a payroll specialist, particularly for small businesses. A specialist can navigate challenges like direct deposit issues, tax exemptions, and accurate tax deductions. Avoiding errors in tax deductions is crucial to prevent serious complications for the business. Efficient and effective payroll management is therefore vital for smooth business operations.

Payroll administration also includes making sure that company payroll policies adhere to employment laws. This can apply to overtime that has been worked, holiday pay or other payroll changes. As businesses grow and employ more workers, it becomes increasingly important to have someone who is capable of processing payroll.

6.1. Payroll Calculation

Payroll is the record of employees receiving payment from the company. It also signifies the total sum of money an employer disburses to the employees. As a business operation, payroll encompasses:

6.1.1. Development of the organization's pay policy, including flexible benefits and leave encashment policies.

6.1.2. Definition of components in the pay slip such as basic pay, variable pay, House Rent Allowance (HRA), and Leave Travel Allowance (LTA).

6.1.3. Collection of additional payroll inputs (for instance, the company's food vendor might provide data regarding the amount to be deducted from employees for meals consumed).

6.1.4. Accurate computation of gross salary, mandatory and voluntary deductions, leading to the determination of net pay.

6.1.5. Distribution of salaries to employees.

6.1.6. Remittance of dues like Tax Deducted at Source (TDS), Provident Fund (PF), etc., to the relevant authorities and completing necessary tax filings.



Source: www.greythr.com

In summary, the payroll process is about calculating the 'net pay' or the amount due to employees after adjusting for applicable taxes and deductions.

The formula for calculating net pay is:

Net Pay = Gross Income - Gross Deduction

Gross Income or Salary comprises all regular income, allowances, and any one-off payments or benefits.

Gross Deduction includes all regular and statutory deductions, plus any one-off deductions.

6.2. Element of Payroll

6.2.1. Hourly Pay

The first step in payroll processing is to calculate the wages to pay each employee. The most frequent pay cycles are weekly, biweekly, semi-monthly and monthly. Hourly employees are usually paid weekly or biweekly. Most companies will have hourly employees complete a time sheet to be turned in at the end of each week. The payroll professional must ensure the employee and her manager/supervisor signs the time sheet; if not, it is invalid. Typically, regular, personal/sick or vacation hours are recorded on the time sheet and are paid at regular pay. Overtime pay should be listed on the time sheet as well to be paid at time and a half.

6.2.2. Salaried Pay

Salaried employees are usually paid biweekly, semi-monthly or monthly. They are not

required to complete a time sheet for they are paid the same amount of hours each pay date. The only time a salaried employee's hours will change is if she had a salary change or is to be paid on a prorated basis (this could be due to termination or other unpaid days). Typically, the payroll professional does not need to make any changes to a salaried employees pay, as the system automatically pays the amount due.

6.2.3. Benefits

Employees may opt to participate in the company's health insurance. These amounts are usually deducted from the have to be changed unless the employee is making a change to his deductions. In this case, he should notify the payroll professional in writing of the change. If the changes are submitted timely, they are made effective on the next payroll.

6.2.4. Taxes

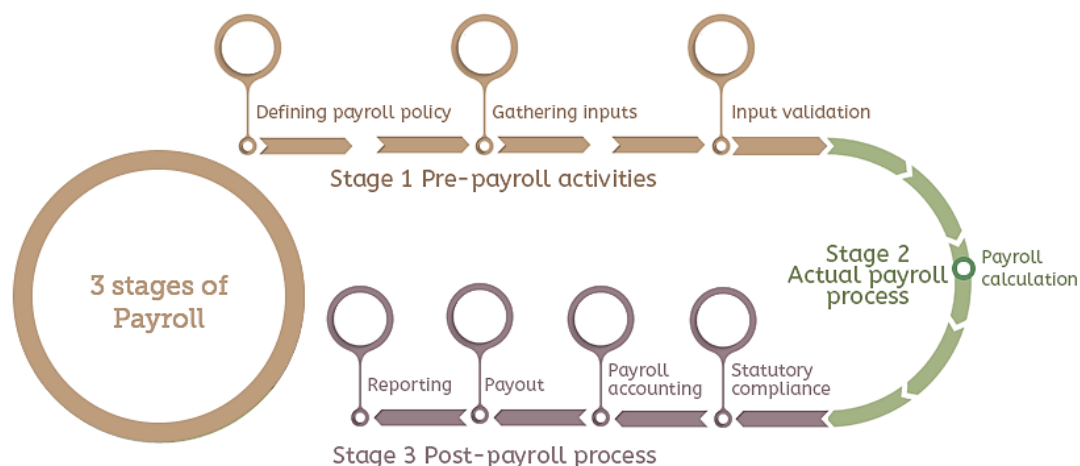
The employee and the employer may be both required to pay payroll taxes. Some companies use payroll software that will compute these taxes, automatically deducting the amounts from the employees' paychecks. The payroll professional is also responsible for depositing taxes to the government, for filing quarterly and annual taxes, and for issuing yearly income withholds to employees.

6.2.5. Payroll Adjustments

Once the hours to be paid are entered in the system, the payroll professional must double-check the information. She can run reports from the system and use them to check for errors. Any errors detected before the payroll closes can be corrected and reflected on the current payroll. Once the payroll is closed, changes or adjustments can be manually done (e.g. a manual check) or adjusted on the next payroll.

6.3. Payroll Process

A payroll officer must undertake meticulous planning, continuously addressing ongoing tasks and staying updated with changes in withholdings, contributions to social security funds, and more. The payroll process is typically divided into three main stages: pre-payroll, actual payroll, and post-payroll activities.



Source: www.greythr.com

6.3.1. Pre-Payroll Activities

Defining Payroll Policy

The net pay is influenced by various factors, including the company's pay policy, leave and benefits policy, and attendance policy. These policies must be clearly defined and approved by management to standardize payroll processing.

Gathering Inputs

The payroll process requires collaboration with multiple departments. Information such as mid-year salary revisions and attendance data are crucial. In smaller organizations, these inputs might come from fewer sources, but in larger organizations, data gathering can be complex. A sophisticated payroll system with integrated features like leave and attendance management and an employee self-service portal can simplify this process.

Input Validation

Once inputs are gathered, it's crucial to validate them for adherence to company policies, authorization, correct formats, and to ensure that all active employees are included and no inactive employees are processed for payment.

6.3.2. Actual Payroll Process

Payroll Calculation

In this phase, the validated data is processed in the payroll system. The result is the net pay after adjusting for taxes and deductions. Post-processing, it's prudent to reconcile and verify the figures for accuracy.

6.3.3. Post-Payroll Process

Statutory Compliance

Statutory deductions like Employees' Provident Fund (EPF), Tax Deducted at Source (TDS), and Employee State Insurance (ESI) are made during payroll processing. The company then remits these amounts to the respective government agencies, often using challans. Subsequently, returns or reports, such as the Electronic Challan cum Return (ECR) for EPF, are filed.

Payroll Accounting

Organizations maintain records of all financial transactions, including salaries, a significant operating cost. Accurate entry of salary and reimbursement data into the accounting/Enterprise Resource Planning (ERP) system is crucial.

Payout

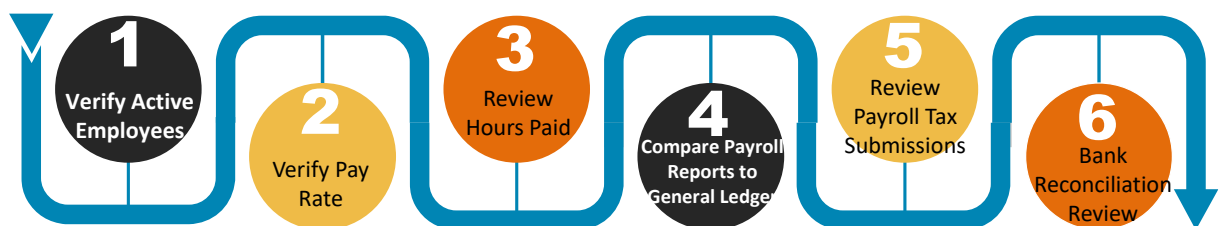
Salaries can be paid via cash, cheque, or bank transfer. Many organizations provide employees with a salary account. After completing payroll, ensure the company's bank account has sufficient funds for salary payments. Then, issue a salary bank advice statement to the relevant branch, detailing information like employee ID, bank account numbers, and wages amounts. Payroll management software with an employee self-service portal can simplify the process of publishing and accessing pay slips.

Reporting

After completing a payroll run, the finance and management teams often request reports like department-wise or location-wise employee costs. As a payroll officer, you need to extract and share this information as required.

6.3. Payroll Audit

Employers should audit payroll processing as part of regular business operations. A small business usually has the advantage of fewer employees making a thorough audit possible rather than sampling data for further review. A good time frame for scheduling a payroll audit is at the end of each quarter of business.



6.3.1. Verify Active Employees

For each person that received a paycheck during the quarter, verify that the person was employed during the time period for which the check was issued. Although it is more difficult to commit payroll fraud on a smaller business, one method of financial theft is by cutting checks to terminated employees and then altering the checks for cashing or colluding with the terminated employee to cash the checks and provide a kick back.

6.3.2. Verify Pay Rate

Verify the pay rate entered into the payroll processing system for each employee. Payroll rates should always be in writing, approved by an owner or manager, and filed with other employee paperwork.

6.3.3. Review Hours Paid

Compare the hours paid to employees for each pay period to the time clock reports or other tracking device used to record employee hours worked. Pay special attention to overtime hours as the cost of overtime can add up quickly and push a small business over budget in salaries and wages expense. If you offer paid time off, such as paid holidays, sick time and vacation days, review each entry of paid time off to ensure the employee who received paid time off pay was eligible for the pay.

6.3.4. Compare Payroll Reports to General Ledger

Compare the totals, such as gross payroll expense, taxes withheld and net check amount, to the general ledger to ensure each payroll processing is correctly recorded on the general ledger. If you have multiple salaries and wages accounts, such as manager payroll, administrative payroll and sales payroll, ensure that each category of payroll reflects the correct expense for the employees in those specified positions.

6.3.5. Review Payroll Tax Submissions

Business payroll taxes include Social Security taxes, Medicare/Medicaid taxes, state unemployment taxes and federal unemployment taxes, as well as the remission of federal withholdings for the employee. The total amount of payroll processed determines how often you remit payroll taxes to the respective taxing authorities, but most payroll remissions will occur at least quarterly with the exception of federal unemployment taxes, which can occur once a year if the business has low payroll amounts.

Compare the payroll totals on the tax remittance reports with reports generated by the payroll system to ensure proper reporting of all payroll amounts. Perform manual calculations of all computer-generated totals to ensure proper calculation of amounts due. Verify that electronic or check remissions equal the exact amount recorded on tax remittance reports.

6.3.6. Bank Reconciliation Review

Review the bank reconciliation for the payroll account to ensure that all checks cleared for the issued amount and make a note of any stale-dated payroll checks to research. Make sure you receive the hard copy of all payroll checks from your bank, even if you have to pay an additional fee for the service. Review each payroll check to ensure the check does not appear altered in any way.

6.4. Payroll System

A payroll system is software which organizes all the tasks of employee payment and the filing of employee taxes. These tasks can include keeping tracking of hours, calculating wages, withholding taxes and deductions, printing and delivering checks and paying employment taxes to the government.

Payroll software often requires very little input from the employer. The employer needs to input employee wage information and hours—then the software calculates the information including withholdings automatically. Most payroll software is automatically updated every time a tax law changes and will remind employers when to file various tax forms.

Choosing a payroll system that best fits your business is essential. It may be difficult to decide which system to choose, but there are some factors to keep in mind when deciding. First, analyze the size of your business and how much of your budget you are willing to spend on payroll processing.

While it is possible for smaller businesses to handle payroll duties in-house through a manual process, a lot of time can be wasted attempting to calculate everything correctly. Payroll system software can eliminate errors in the payroll process and eliminate excessive effort involved in put calculating employee hours, wages and tax withholdings. Payroll software is easy to use often times very affordable for small businesses.

Employers or HR departments can purchase an affordable system accessible on their local computer or via a cloud service. Purchasing software eliminates the expense of hiring an in-house accountant for payroll processing. Lastly, small business owners

can maintain more control of the payroll process by using software. Using payroll software allows the business to compile reports at whatever pace they desire.

When choosing a payroll system, you'll want to look for security. Is the software password protected? Having a password protected software ensures there is no tampering of information. Next, is the software compatible and flexible? It is important to have payroll software that functions well with your other business systems and will grow with your business.

Another factor to consider is systems credibility. Make sure the software is made by a well-known brand. Lastly, you'll want a payroll system which will allow the employer to still have control and the option of viewing reports and historical information. Once you choose your payroll system it is up to you how much control you want over it.

6.5. Payroll Outsourcing

Payroll outsourcing is a business practice that involves contracting with a business service to handle all functions related to a company payroll. Using an outsourcing service makes it possible to manage the payroll process without the need to maintain a large payroll department. Payroll service providers manage such diverse functions as the calculation of wages and salary, withholding of taxes, the distribution of withheld funds to the proper government agencies, and the direct deposit of net pay into the bank accounts of employees.

There are many reasons why a company may choose to go with a payroll outsourcing option. The most common is to save time and money on the handling of financial tasks associated with a payroll. By contracting with an outside vendor, it is possible to restrict the payroll team to one or two individuals within the company. Often, these two designated individuals are authorized to supply basic data to the payroll service, which then handles the rest of the details. As a result, there is no need for anyone to spend a majority of the workweek calculating hourly wages, taxes, and dealing with various types of withholding issues.

Since most payroll outsourcing services offer the option of cutting checks or direct deposit, it is possible for each employee to choose which format he or she prefers. When checks are selected, they are usually sent by courier to the client, who then distributes them to the employees. In situations where the direct deposit option is selected, employees often find their money is credited to their account the evening before their actual pay date, or early on the standard pay date.

Another benefit to using a payroll outsourcing service is that the employer does not

have to keep up with changes in regulations that impact the calculation of taxes. Since the outsourcing service constantly updates their information to comply with current laws, the employer never has to worry about incurring late charges and other penalties, due to an improper calculation of the taxes due. This benefit alone can save a large corporation a significant amount of money over the course of a year.

Payroll outsourcing also prevents an employer from having to deal with technology woes. Since the payroll is processed off-site, there is never a need to upgrade payroll software or spend time and money on program or hardware glitches or any of the system issues that can occur and slow down the payroll process. As a result, employees are consistently paid on time and remain happy.

While payroll outsourcing does mean incurring another business expense on a regular basis, even small businesses often find that using this type of service saves time and money each month. Most outsourcing vendors will offer several different payroll plans that are likely to be ideal for businesses of different sizes. In terms of convenience, keeping the payroll records up to date, and keeping the withholding accurate, going with a payroll outsourcing service just makes sense.

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