



A STRATEGIC PERSPECTIVE OF COMPENSATION MANAGEMENT

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“If you pick the right people and give them the opportunity to spread their wings - and put compensation and rewards as a carrier behind it - you almost don't have to manage them.”

B. — *Jack Welch*

Abstract:

Most of us would have heard the term “compensation” in the context of getting paid for the work that we do. The work can be as part of full time engagement or part time in nature. What is common to them is that the “reward” that we get for expending our energy not to mention the time is that we are compensated for it.

From the perspective of the employers, the money that they pay to the employees in return for the work that they do is something that they need to plan for in an elaborate and systematic manner. Unless the employer and the employee are in broad agreement (We use the term broad agreement as in many cases, significant differences in perception about the employee's worth exist between the two sides), the net result is dissatisfaction from the employee's perspective and friction in the relationship.

Key words: Compensation Management, Strategy, Strategic HRM.

Introduction:

It can be said that **compensation is the “glue” that binds the employee and the employer together** and in the organized sector, this is further codified in the form of a contract or a mutually binding legal document that spells out exactly how much should be paid to the employee and the components of the compensation package. Since, this article is intended to be an introduction to compensation management, the art and science of arriving at the right compensation makes all the difference between a satisfied employee and a disgruntled employee.

Though Maslow's Need Hierarchy Theory talks about compensation being at the middle to lower rung of the pyramid and the other factors like job satisfaction and fulfilment being at the top, for a majority of employees, getting the right compensation is by itself a motivating factor. Hence, employers need to quantify the employee's contribution in a proper manner if they are to get the best out of the employee. The provision of monetary value in exchange for work performed forms the basis of compensation and how this is managed using processes, procedures and systems form the basis of compensation management.

As the module progresses, readers would be introduced to other aspects of compensation management like the components of compensation management, types of compensation, inclusion of variable pay, the use of Employee Stock Options etc. The aspect of how skewed compensation management leads to higher attrition is discussed as well. This aspect is important as studies have shown that a majority of the employees who quit companies give inadequate or skewed compensation as the reason for their exit. Hence, **compensation management is something that companies must take seriously if they are to achieve a competitive advantage in the market for talent.**

Considering that the current trend in many sectors (particularly the knowledge intensive sectors like IT and Services) is to treat the employees as “creators and drivers of value” rather than one more factor of production, companies around the world are paying close attention to how much they pay, the kind of components that this pay includes and whether they are offering competitive compensation to attract the best talent. In concluding this article, it is pertinent to take a look at what Jack Welch had to say in this regard: As the quote (mentioned at the beginning of this article) says, if the right compensation along with the right kind of opportunities are made available to people by the firms in which they work, then work becomes a pleasure and the manager’s task made simpler leading to all round benefits for the employee as well as the employer.

Components of compensation:

Hertzberg’s Hygiene theory refers to how certain factors are necessary to maintain “Hygiene” or ensure that the employees are not dissatisfied.

- These factors alone do not contribute to “quantum” jumps in employee satisfaction. Rather, the absence of these factors makes employees dissatisfied.
- The point here is that if a fair and just compensation is provided, the employee has the “baseline” requirements met which ensures that he or she is now in a position to go for higher things like job satisfaction and fulfilment.
- However, if compensation is found to be lacking, the employee might very well be unhappy and dissatisfied with the company leading to attrition and other such negative outcomes.
- Hence, having the right compensation is the first step in getting the best of employees.

If we take a look at the components of a compensation system, we find that employers decide on what is the right compensation after taking into account the following points.

1. The **Job Description** of the employee that specifies how much should be paid and the parts of the compensation package.
 - a. The Job Description is further made up of responsibilities, functions, duties, location of the job and the other factors like environment etc.
 - b. These elements of the job description are taken individually to arrive at the **basic compensation along with the other components like benefits, variable pay and bonus.**
 - It needs to be remembered that the HRA or the House Rental Allowance is determined by a mix of factors that includes the location of the employee and governmental policies along with the grade of the employee.

- Hence, it is common to find a minimum level of HRA that is common to all the employees and which increases in proportion to the factors mentioned above.
2. The **Job Evaluation** that is a system for arriving at the net worth of employees based on comparison with appropriate compensation levels for comparable jobs across the industry as well as within the company.
 - a. Factors like **Experience, Qualifications, Expertise and Need of the company** determine how much the employer is willing to pay for the employee.
 3. It is often the case that employers compare the jobs across the industry and arrive at a particular compensation after taking into account the specific needs of their firm and in this respect salary surveys and research results done by market research firms as to how much different companies in the same industry are paying for similar roles.

The components of compensation that have been discussed above are the base requirements for any HR Manager who is in charge of fixing the compensation for potential employees.

There are other variables as well that would be discussed in subsequent articles. This article has introduced several concepts around the topic of components of compensation and these concepts are crucial for HR professionals as well as those aspiring management professionals who want to make a career in the corporate world.

Before concluding this article, it needs to be remembered that exit interviews have shown that over 70% of employees who quit their jobs do so because they are dissatisfied with the compensation that they are getting. Hence, all HR professionals and managers must take this aspect into account when they determine the compensation to be paid to employees.

Negotiation in Compensation Management:

It is impossible to talk about compensation management without referring to the process of negotiation and bargaining that is an integral part of compensation management. As anybody who has worked in the formal or even the informal sector knows, the process of negotiating one's salary and perks is fundamental to the process of hiring and selection. In this article, we look at some of the strategies employed by professionals' world over when they negotiate with their prospective employers regarding their compensation.

Have a Plan in Place

The first element of negotiation is to plan for the process by deciding on how much more you want and how much you think the employer is willing to give. The fine art of knowing how much you should ask for and at what point should you strike the deal is something that experienced professionals know and rookies should learn. Without having a clear idea of the target level of compensation that you are aiming for, the negotiation process would turn out to be an exercise in futility.

Communicate Your Needs

Once you have arrived at a figure that you think you deserve, the next step is to communicate the same to the prospective employer without delay. The important point to note here is that the way in which

you articulate your needs is as important as the need to drive a bargain. For instance, without expressing yourself clearly to the HR manager of the prospective employer, there is little chance that he or she would understand your needs and respond appropriately. Hence, once you have sorted out the target compensation that you want, you should also have a strategy to communicate it to the employer.

Timing is Everything

You need to remember that there is something called being too early when you negotiate and too late as well. Hence, the timing of your articulation forms the basis for a successful negotiation. For instance, if you start your demands early on in the hiring process, the prospective employer might stall the process or even put a stop to your hiring. On the other hand, if you put forward your demands as you are about to join the firm, there is precious little anyone can do about your demands. Hence, you should have a keen eye for when you should communicate your demands.

The three aspects of having a plan, communicating the need and then timing it in such a way as to derive maximum advantage are essential to the negotiation process. Of course, there are many firms that do not entertain any sort of negotiation and there are firms that put up pretence of negotiation when in reality, they do not budge at all. In these cases, it is better to adopt a wait and watch policy and make your move once they get into the details of your compensation.

In conclusion, a successful negotiation hinges on the willingness of both the parties to hear each other and an ability to arrive at a common denominator in a spirit of accommodation. Hence, do not be overtly rigid and at the same time do not give in to the employer totally.

Strategic Compensation Decisions

Turning next to the other dimension of compensation strategy, the patterns of critical decisions, Table 1 contains lists of decisions deemed to be strategic in the literature. Both structure and process decisions are included. The list proposed by Lawler (1981), while not the longest, is perhaps the most inclusive. It includes the market position (level of pay relative to competitors), internal versus external orientation, hierarchy (the steepness of the pay structure and the basis--job versus skills--for the pay structure reward mix, and the basis of rewards (performance versus seniority, groups versus individual, criteria used, etc.). Several issues listed by Carroll (1987) (performance measures, size of bonus, timing, etc.) seem consistent with Lawler's more broadly defined issues (e.g. basis for increases). The original issues proposed for executive compensation have also become more broadly defined and applied to all employees. For example, both issues proposed by Ellig, (1981) the relative emphasis to be placed on the various elements of compensation, and the short- versus long-term, are treated as part of the "mix" decision.

Conclusion:

Globalization has created a "global village" where people in different parts of the world are able to not only participate in global supply chains but also partake of the wonders of cultural exchange and assimilation. This has created aspirational values among large sections of people in the developing countries who now demand better compensation at par with their counterparts in the advanced economies of the West. Hence, corporates need to be aware of the complexities of the issue of how

much compensation and in what form that is to be paid to the employees taking into account all the factors.

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