Compensation Hiring Guide for Managers

2017

University of Missouri System

COLUMBIA | KANSAS CITY | ROLLA | ST.LOUIS

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DISCLAIMER

This guide is designed to provide managers with the practical tools and basic information for making effective pay decisions. However, it is not intended to address all issues you may encounter. This information is intended to provide general guidance only, and is not intended to override anything found in the university's Collected Rules & Regulations (CRRs), policies or procedures. Nothing in these guidelines confers to any individual or employee any right, express or implied, to employment with the university, to remain in the university's employment, or to any specific base pay, benefits or compensation. The procedures, practices, policies and other matters described herein may be modified or discontinued from time to time, at the discretion of the university. These guidelines do not establish an employment agreement or contract with any individual or employee. The matters set forth in these guidelines are not subject to the university grievance procedure (Collected Rules and Regulations, Chapter 380: Administrative, Service and Support Staff Grievances).

INTRODUCTION

Salaries expense is the largest cost item for most organizations. And with the cost of employee benefits factored in, the **total rewards** package can add up to a significant amount. And the same is true for the university. In FY15 salaries expense was approximately 60% of the university's total expenditures. With the cost of benefits added in, the expenditure for total rewards comprised 78% of total expenditures. Accordingly, the compensation decisions that managers make on a regular, on-going basis can have a significant and lasting impact for the university. In addition to the usual cost of total rewards, there are other potential costs associated with pay decisions that must be considered:

- Pay inequity: there are risks and corresponding potential costs associated with establishing pay levels that cannot be directly associated with job-related factors including skills, performance or experience. Charges of discriminatory pay practices may be advanced even if the pay disparity was unintentional.

- Opportunity cost: ineffective compensation strategies used when recruiting, hiring, promoting and rewarding, or when seeking to retain employees, can lead to lost opportunities and potential corresponding costs. To minimize such losses, it is essential that managers know how to use our total rewards program to maximize success when making these important decisions.

- Employee morale: less tangible, but no less important, is the effect of poor pay decisions or pay communication on employee morale. Morale issues can negatively impact productivity and teamwork, and lead to the loss of quality employees. If employee morale issues do arise, managers are uniquely positioned to detect and address any pay issue that may be a contributing factor.

PARTNERING FOR SUCCESS

The UM System compensation team, campus HR representatives and university managers work together to ensure that pay is administered in a fair and equitable manner, and in alignment with the university's compensation philosophy.

University System Compensation

- Designs and maintains market-aligned pay programs and structures in support of the university's compensation philosophy
- Develops the tools, information and guidance required to support sound pay decision making

Campus HR

- Provides input and feedback to University System compensation team
- Integrates and operationalizes the compensation program for the respective campus
- Serves as primary first-line resource for managers

Management

- Understands the total rewards program and effectively communicates it to prospective and current employees
- Optimizes the use of the compensation resources and information provided
- Ensures that all pay decisions are directly linked to:
  - Job qualifications (required knowledge, skill, abilities, education, etc.)
  - Job performance

THE CHANGING COMPENSATION LANDSCAPE

Our Competitive Edge

Like most employers, the university desires to gain a competitive edge by presenting what we offer to prospective and current employees in the best possible light. One frequently overlooked point of differentiation is the value of our total rewards package, which includes benefits and other job attributes in addition to **base pay**.

Until recent years, most companies offered similar benefits packages, making this element a neutral factor in an employment offer. However, in the current environment where more employers are decreasing benefits programs, the university is gaining a competitive edge.

Accordingly, it is increasingly important that our managers understand and are able to communicate effectively about our pay programs so that prospective and current employees are fully aware of the total rewards packages they are offered.

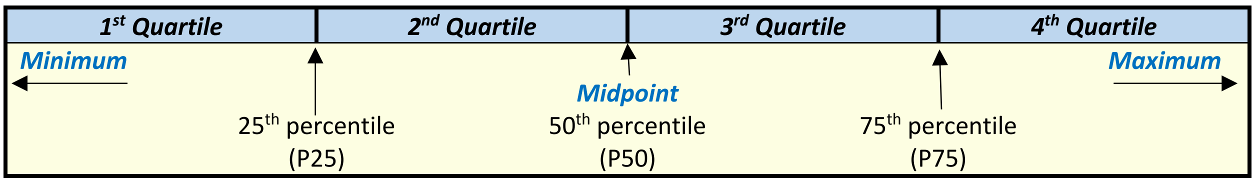
Changing Factors of Pay

Another shift affecting pay is the increasing focus on **pay-for-performance**. This is true even within industries that traditionally linked pay to longevity vs. job performance, and provided across-the-board pay increases without differentiation based on performance. Going forward, it is vital that managers differentiate pay based on job performance.

UNDERSTANDING THE SALARY STRUCTURE

Salary Ranges

A good understanding of the salary structure is foundational to making good pay decisions. Salary ranges provide the context for relating pay for our jobs to the external market. Salary range values are regularly assessed by comparing our **benchmark jobs** to relevant labor markets. Individual salary ranges are arranged within a pay structure, which provides the framework for maintaining appropriate pay relationships between jobs internally. Accordingly, when jobs are placed correctly into our salary range structure, both external and internal pay relationships are appropriately aligned. Salary ranges are typically divided into four parts called **quartiles** as shown in the chart below:



Salary Range Progression

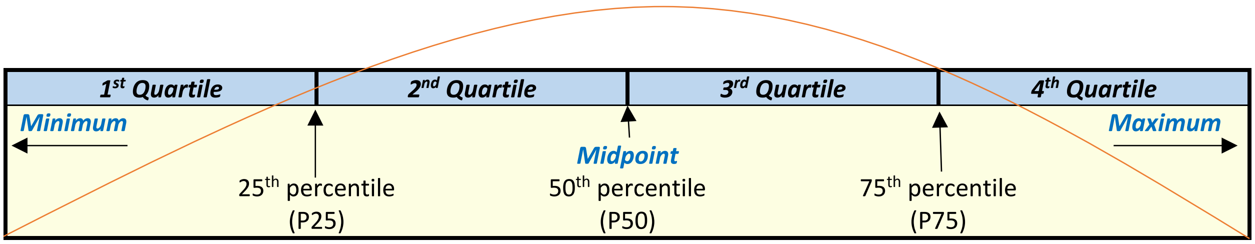
An employee's level of pay compared to the salary range is referred to as **salary range progression**. The measure most often used to indicate salary range progression is **compa-ratio**, which is calculated by dividing the employee's annual rate of pay by the salary range midpoint:

$$\textbf{Compa-Ratio} = \frac{\text{Annual Salary } (\textit{based on 1.0 } \textbf{\textit{FTE}})}{\text{Salary Range Midpoint}}$$

Most employees are expected to progress through their assigned salary range over a period of time based on level of skill, experience and job performance. The time period may vary by job or job level, and is dependent upon sustained "*successful*" or better performance (as well as the university's ability to pay). However, not all employees are expected to reach the top of the salary range. By design (reflecting market realities), pay is expected to be normally distributed across the salary range with a slight skew toward the top of the range. Accordingly, over time, pay for most employees will cluster around (just slightly above) the midpoint of the salary range.

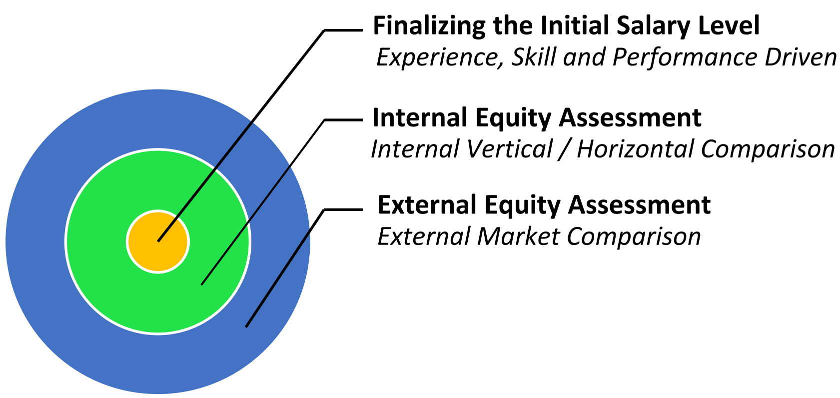
Normally, an experienced, fully proficient employee who is successfully meeting all job expectations is expected to have a compa-ratio of at or near the salary range midpoint[1] (~0.95 – 1.05). Progressively fewer employees are expected to be paid at levels from the salary range midpoint out toward either end of the pay range.

[1] In some cases the actual "target" pay for a job may be above or below the salary range midpoint. One example where this may occur is when the external market is rapidly changing for a specific job or type of skills.



SETTING INITIAL SALARY LEVELS

Determining an appropriate initial level of pay can be complex and challenging. A helpful way to think about this process is fine-tuning the information down to the optimal solution, as illustrated below.



Let's work through these levels of fine-tuning in a little more detail.

External Equity Assessment
The **pay grade** assigned to a job provides the link to the external market value for the job as explained on the preceding Salary Ranges section. Accordingly, the minimum and maximum pay levels assigned to a job serve as the outside parameters for setting the initial salary level for the employee who will be hired into that job.

In most cases, the manager will already know the pay grade for a job before trying to determine a pay level. However, if a new job is being added to the salary structure, or if there is a significant change in an existing job, the job must first be evaluated and a pay grade assigned before the hiring process can continue.

To initiate the job evaluation process, a manager must complete and submit a Position Classification Questionnaire (PCQ). Refer to the *Compensation Leadership Administration Guidelines* (PDF) for more information.

Depending on the situation, there are a couple of different types of external equity reviews that may take place. The most common types are explained in the chart below:

Type of Review	*Typical Application*
Routine Market Benchmarking	A periodic assessment of our jobs compared to the external market to ensure that the salary structure and the individual ranges within the structure are appropriately aligned. The external market consists of the organizations with which we primarily compete for talent.
Ad Hoc Market Benchmarking	Occasional market benchmarking performed outside of the normal market review cycle. This is usually reserved for new jobs, "hot" jobs (where the relevant market may be moving more rapidly than the market overall) or for unique jobs that are difficult to benchmark.

Internal Equity Assessment

The next step in the fine-tuning process is to complete an **internal equity** assessment. For this review we first must estimate a salary level for the job and then compare that estimate with pay for employees in closely related jobs, both vertically and horizontally across the organization.

Estimated Initial Salary Level

To estimate a salary level for the job, work with your local HR representative. They will help you assess the candidate's education and work experience compared to the minimum requirements for the job.

From the salary estimate, calculate the estimated compa-ratio and compare it to the compa-ratio (CR) values in the chart below, and identify the corresponding salary range quartile. Assess if the general description for the quartile "fits" the characteristics of the candidate being considered for the job.

Note that an initial pay level is not usually set above the range midpoint (P50), and almost never above the 75th percentile of the range (P75). The 4th quartile of the salary range is reserved for those employees who consistently demonstrate an "*outstanding*" level of performance.

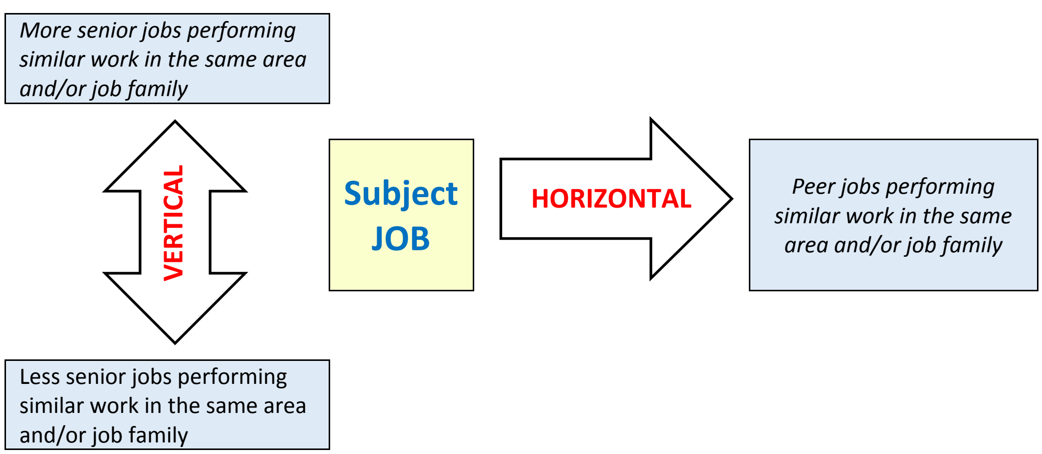
Also, setting an initial pay level within the 4th quartile would limit the potential for pay growth over time for the employee in this new role. If the candidate's relevant qualifications and salary expectations are incompatible with the salary range below P75, then job fit should be questioned (e.g., the candidate may be overqualified for the job.)

	2nd Quartile (P25 to P50)		3rd Quartile (P50 to P75)	
1st Quartile (Minimum to P25)	**CR 0.85 – 0.99**	**Midpoint (P50)**	**CR 1.01 – 1.15**	**4th Quartile (P75 to Maximum)**
CR typically < 0.85		**CR = 1.0**		CR typically > 1.15
▪ Novice employee; new to the job and on a learning curve ▪ Minimal experience related to the position ▪ Meets minimum qualifications and is able to perform basic duties and responsibilities	▪ Gaining experience, skill and proficiency ▪ Consistent "*successful*" performance	▪ Experienced and fully qualified employee ▪ Fully proficient skill level ▪ Performance is consistently "*successful*" and frequently "*exceeds expectations*"	▪ Experienced employees with performance that consistently "*exceeds expectations*"	▪ Highest salary level for an employee with extensive experience with performance consistently rated "*outstanding*"
Entry Level	Intermediate Level	**Career or "Market" Level CR ~ 0.95 – 1.05**	Normally initial pay levels should not have a CR > 1.06, and almost never > CR 1.15 (must demonstrate "*outstanding*" performance)	

If the compa-ratio for is on the borderline between quartiles, that issue will be addressed during the last step of this "fine-tuning" process. There should not be a large disparity between the estimated compa-ratio placement, and the "best fit" description in the chart. If there is, re-check the initial salary estimate to ensure it is correct.

Comparison to Related Internal Jobs

Next, select the group of internal jobs to be used as comparators for the internal equity assessment. These jobs should be those most closely related to the job, both vertically and horizontally across the organization as shown below:



Once the comparator jobs are identified, gather the following data for the employees in these jobs to complete the internal equity assessment:

- Annualized salary - *for accurate calculations and comparisons, annualize the salary for hourly employees (hourly rate x 2080 hours), and for employees who are <1.0 FTE (annual rate / FTE allocation)*

- Pay grade and corresponding salary range - salary range ***minimum, midpoint, maximum***

- Compa-ratio - *annualized salary / pay range midpoint*

- Years of job-related experience - *use 'time in position' + any other directly related experience*

- Performance rating - *use the average of most recent 2 years' performance ratings if available*

As you begin to compile this data, you should find that compa-ratios in this comparator group are differentiated on the basis of each employee's level of skill, experience and performance as compared to the relative job requirements.

Differences in compa-ratio should be directly attributable to job-related factors such as level of skill, experience and performance.

If outliers emerge through this process, make note of the specific issues so they can be addressed separately. Justified outliers should be normalized or eliminated from the data set used for the internal equity assessment. An example of a justified outlier is a salary level that includes a geographic differential for an employee working in a high cost of labor location. Next, align the compa-ratios for the comparator job group to the same quartile chart that was used for the job being assessed (see chart in the Estimated Initial Salary Level section). Consider the following questions, remembering to base the assessment on job-related factors only:

- Are the quartile alignments for all jobs reasonable?

- Is the compa-ratio for the subject job reasonable compared to the compa-ratios for the other jobs? *(Analyzing pay relationships using compa-ratio provides the best overall 'apples-to-apples' comparison for jobs in varying salary ranges.)*

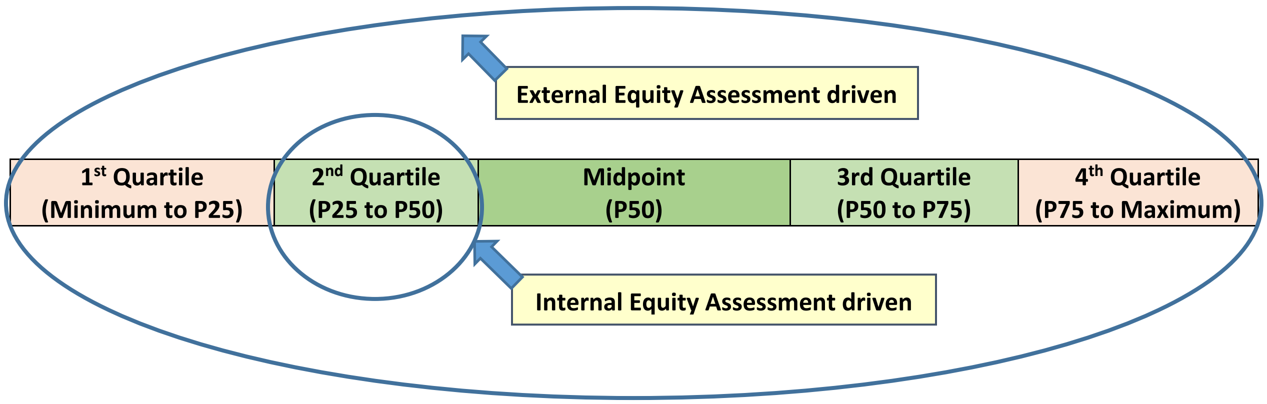
- Is the estimated salary level for the subject job reasonable compared to horizontal jobs (same pay grade) and vertical jobs (pay grades above and below)? *(Look for **pay compression**, and for other significant differences that cannot be explained by job-related level of skill, experience and/or performance which may indicate a pay disparity risk.)*

- Is there a logical and defensible explanation for all significant pay differences noted?

Finalizing the Initial Salary Level
Before we move on to the final step in determining the initial salary level, let's review our progress:

- From the external equity assessments we have established the outside pay parameters that we must work within.

- From the internal equity assessment we have focused further in to the specific quartile of the range where we expect the initial salary level to fall, and we have tested the estimated salary level to ensure it is reasonable.



Note: the example provided in the chart above is for illustrative purposes only.

The fine-tuning process up to this point has been primarily data-driven and objective. Now the emphasis shifts to the more subjective "art" of factoring in the appropriate *qualitative* elements of pay.

The initial steps of establishing an appropriate salary level are anchored in a defensible, empirical process. Finalizing the salary level ultimately is a balance of both quantitative and qualitative variables.

Qualitative Pay Factors
Listed below is a sample of qualitative pay factors that might be considered in the final shaping of the initial salary level. Use the chart to assess if the factor should nudge the salary estimate up, down or if it would have a neutral effect.

Potential Adjustment Factors (remaining within quartile range min / max)	**+**	**-**	**=**
Strength or quality of job-related experience			
Recency of job-related experience			
Additional relevant qualifications (e.g., certifications)			
Strength of the job interview			
Mission critical nature of role			
Scarcity of skill set (very unique/hard to find skill set that is highly sought after)			
"Hot" jobs (the external market rate for these jobs is escalating very quickly)			

If the estimated compa-ratio was on the borderline between two pay range quartiles, nudge toward the quartile with the best overall "fit"			
What other qualitative job-related factors should be considered?			

While the focus in setting an initial pay level must be grounded in job-related factors, a candidate's salary expectation must also be considered. This will be covered more detail in the Formulating the Offer section.

Reasonableness Check

After refining the proposed salary level based on qualitative pay factors, re-check the internal equity data to ensure the updated salary estimate is still reasonably aligned. If any new issues or concerns emerge from this quick re-check you may need to slightly adjust the salary level as appropriate. (Only minor adjustments up or down are expected at this stage of the process.)

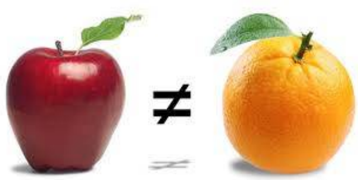
This could be a somewhat iterative process until you finalize on a level that appropriately prioritizes and balances all relevant job-related factors.

FORMULATING THE OFFER

Once we have a final, approved salary level, it is time to formulate the actual offer. *(Note that Human Resources should be consulted, and campus approval processes must be followed.)*

Recalling that it is our total rewards package that gives us our competitive edge, it is imperative that we position all elements of total rewards to their full advantage in making the offer. (*Refer to The Changing Compensation Landscape section for more information about total rewards and our competitive edge*.)

A candidate may expresses their pay expectations in terms of all they are giving up. In an effort to be competitive, the hiring manager may strive to meet that expectation using only the base pay element of total rewards, and overlook the value of the benefits we offer. Only when we align our total rewards offer side-by-side with the candidate's current total rewards package are we are able to accurately assess what is really being given up vs. what is being offered.



Basing pay decisions on inaccurate comparisons could lead to undesirable outcomes including:

Hiring candidate at a salary level that is too high

- Unnecessary budget impact
- Potential for internal pay inequity and pay compression

Loss of a desirable candidate

- Communicating that we cannot meet the candidate's pay expectations by considering base pay only, and "underselling" what we offer in terms of our total rewards package

Total Rewards Comparison
Your HR representative can assist you with formulating an "apples-to-apples" comparison of current and proposed total rewards. This comparison will consider the total package of what the university offers compared to the candidate's current job:

The University's Total Rewards Elements:
- Base salary offer +
- Any **non-discretionary variable pay** (if applicable) +
- The value of the university's employer-provided benefits. Initially, use the cost of single coverage for the lowest level plans until you have an opportunity to get more information from the candidate about what plans they might choose. So that you can quickly model alternate scenarios, be prepared with the current cost of premiums paid by the university for other schemes (e.g., + spouse or family).

Once you have a total rewards estimate for the job, compare this to the candidate's current compensation and benefits values (most likely this data will be obtained during the offer discussion, so be prepared to model the information when it is received)

Note: although the value of paid time off is already included in base pay, it is still important to compare current and proposed plans and highlight the university's generous allowances.

Salary Negotiations
Sometimes a candidate will ask for more compensation. Following are helpful points to consider and strategies for addressing this situation:

- Find out exactly what salary the candidate is seeking. This is important information to collect even if you ultimately decide not to pursue the candidate further. For example, this could provide valuable insight into recruiting barriers for hard to fill positions.

- If the candidate wants more than you had planned to pay, but the requirement is still within the salary range for the job, consider the following to help you decide how to proceed:

    - *Does the candidate possess skills you cannot find anywhere else?*
      If the candidate has skills that far exceed other candidates for the job, and these are skills that are very difficult to find, a higher salary level may be justified.

    - *Were there other applicants who could adequately fill the position?*
      If so, you have more flexibility in negotiations.

    - *What effect would a higher offer have on internal equity?*
      Always recheck internal equity (refer to the Internal Equity Assessment section for details) and obtain additional approvals before proceeding with a counter-offer.

NOTE: there is a growing trend for organizations to adopt a "no negotiation" policy when it comes to establishing an initial salary level. One reason is that male candidates are historically more successful at negotiating a salary level than are female candidates. So even if unintended, this can start a disparity in pay based on gender that will likely grow more pronounced over time since subsequent pay actions are driven off of the initial pay level.

We hope you will find the information in this guide helpful as you make these important decisions. However, these guidelines are not intended to provide an answer for every situation you may encounter. Please do not hesitate to contact your campus HR representative if you have questions or need further assistance.

APPENDIX 1 – GLOSSARY OF TERMS

TERM	DEFINITION
Base Pay	The fixed compensation rate paid to an employee for performing specific duties. (It does not reflect extra pay such as shift premium, call pay or overtime.)
Benchmark Job	A job that is common in the external market and used to make salary comparisons either within the organization or to similar jobs outside of the organization.
Compa-Ratio	Compa-ratios are used to measure and monitor an individual's actual rate of pay to the midpoint or control point of their salary range. It is a useful gauge for leaders to use in assessing experience versus salary level, magnitude of salary adjustment, etc. Compa-ratio is determined by the following formula: ***current base salary (based on 1.0 FTE) / midpoint of the salary range.*** Example: a full-time employee in grade 8 has a base salary of $35,000 per year. ***$35,000 / $46,500 = 0.75*** ▪ A compa-ratio of < 1.0 indicates that the salary range is less than the midpoint. ▪ A compa-ration of > 1.0 indicates that the salary range is greater than the midpoint.
Compensation Leadership Administration Guidelines	A document that contains information to guide Human Resources and university leaders in setting and administering employee compensation. The document is available as a PDF at https://uminfopoint.umsystem.edu/sites/hr/Benefits/COMP/CURRENT/LeadershipAdministrationGuidelines.pdf
FTE	FTE stands for “full-time equivalent”. This is an index to compare full time employees (1.0 FTE) to part-time employees (< 1.0 FTE). The value for part time employees: ***number of hours scheduled to work / 40 hours.*** Example: if an employee is scheduled to work 20 hours per week, they are 0.5 FTE: **20/40 = 0.5**
Internal Equity	The relative relationship of employees’ salaries to one another within similarly situated positions, based upon experience, performance, etc.
Non-discretionary Variable Pay	A plan in which management determines the size of the incentive pool and the amounts to be allocated to specific individuals after a performance period. These use a predetermined formula and a promise to pay.
Pay Compression	Pay differentials too small to be considered equitable. The term may apply to differences between 1) the pay of supervisors and subordinates, 2) the pay of experienced and newly hired personnel of the same job, and 3) pay-range midpoints in successive job grades or related grades across pay structures.
Pay-for-Performance	The practice of using pay to manage and motivate performance. Pay-for-performance links pay (base and/or variable), in whole or in part, to individual, group, and/or organizational performance.
Pay Grade (aka “Global Grade”)	A group of jobs of the same or similar value, used for compensation purposes. All jobs in a salary grade have the same salary range: minimum, midpoint and maximum. The grade assignment for a job is determined through a job evaluation process which includes both internal and external comparator information.
Quartiles	A distribution divided into fourths (e.g., the pay range). The first quartile corresponds to the 25th percentile, the second to the 50th percentile, the third to the 75th percentile and the fourth to the 100th percentile.

TERM	DEFINITION
Salary Range Maximum	The highest level of pay for a position based on its assigned pay grade within the university's pay structure. Pay at this level is intended for employees whose performance levels consistently *exceed* most position requirements.
Salary Range Midpoint	The middle point between the minimum and maximum of the salary range. This value typically represents the market value or "going rate" for an experienced individual in the position.
Salary Range Minimum	The rate paid to an employee who possesses the minimum qualifications of the position and who is expected to be able to perform the basic duties and responsibilities of the position.
Salary Range Progression	The position of the employee's pay level within the pay ranges; the ability for pay movement or progression is based upon performance.
Total Rewards	The monetary and non-monetary returns provided to employees in exchange for their time, talents, efforts and results. Total rewards involve the deliberate integration of five key elements that effectively attract, motivate and retain the talent required to achieve desired business results.
Variable Pay	Compensation that is contingent on discretion, performance or results achieved. It may be referred to as pay at risk.

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