Dr. Pallabi Mund, Assistant Professor (HR)

MODULE 1: CONCEPTUAL ASPECTS OF COMPENSATION AND REWARD MANAGEMENT

❖ Concept and Definition of Compensation:

Compensation refers to money and other benefits received by an employee for providing services to his/her employer. Money and other benefits received can be in different forms:

- Base Compensation: in terms of money
- Benefits: Provident Fund, Gratuity, and Insurance scheme, etc

According to Cascio, "Compensation includes direct cash payments, indirect payments in the form of employee benefits, and incentives to motivate employee to strive for higher levels of productivity"

❖ Concept and Nature of Compensation:

- Compensation is basically time-based: hourly, weekly, monthly, or yearly.
- It is simple and measurable: Overtime and under time .
- It is purely extrinsic as it contains all forms of tangible services and benefits.
- It is kind of rewarding an employee's worth to the organization and in turn acts as a motivator.
- It acts as a tool for an organization to foster the values, culture and the behaviour of the employees.

❖ System of Compensation:

Compensation is a tool used by management for safeguarding the existence of the company. The main characteristics of the compensation system are as follows:

- A hierarchy of jobs
- A hierarchy of pay levels
- A set of rules and procedures
- Qualities required for movement from one level to other

Compensation in terms of money can be claimed –On Time or Deferred. Compensation in terms of "in-kind" claims. Therefore compensation is mainly of two types: **direct and indirect**.

Direct Compensation: Cash compensation like –

- Basic pay,
- Dearness Allowance (DA)
- House Rent Allowance (HRA)
- Leave Travel Allowance (LTA)
- Medical Allowance
- Shift allowance (SA)
- Variable pay,
- Superannuation Allowance
- Long-term incentives (equity),
- Bonuses and commission

- **Indirect Compensation: are the Non-monetary benefits provided to employees:**
    - Provident fund
    - Pension schemes
    - Health insurance
    - Gratuity
    - Stock Options
    - Overtime Pay
    - Vacations (paid leaves)
    - Sick leaves
    - Other benefits and perks (company cars, mobile phones, Staff dinner, in office snacks, hotel suites)

- **<u>The 3P Compensation Concept</u>**

1. **Pay for Position:** Pays employee for the job to which they are assigned, regardless of the skills they possess. Pay is centred on the job or position one holds in the organization; and not on the person. This is a traditional pay structure wherein each position is assigned a pay range based on the job duties they perform. Employee's compensation is set in broadband based on qualifications, education, experience and seniority. Through broad banding, narrowly structured pay grades determined through job evaluation are replaced by fewer and wider bands. For example, everyone working in customer service, or all administrative assistants (regardless of department), are paid within the same general band.

2. **Pay for Person:** Person-focused pay or skill based pay, or knowledge based pay or competency based pay structures is also a market-based pay approach. This pay structure is linked to the skills, abilities, competencies and knowledge a person acquires and applies at work. The market demand for the person's unique skills is also considered. Payment is based on all the "certified skills" regardless of whether the work they are doing requires all or just a few of those particular skills. Here, increments in payment, is based on the **3 types of skills:**
   Horizontal skills (broadening of skills – range of tasks)
   Vertical skills (higher level skills)
   Depth Skills (higher level of skills related to a specialized area and the same job.
   Employees become multi-skilled and more flexible in their work, in the long run

3. **Pay for Performance:** Performance based pay is a financial reward system given to the employees when their performance is assessed related to certain stated criteria. These criteria may be based on individual, group or organizational performance or a mix of them all. An individual's performance is managed through a "performance contract" which comprises of the clarification of the goals, setting of objectives and the review of performance. When individual performance is difficult to measure, team-based criteria of appraising the performance of the team becomes appropriate.

❖ **Dimensions of Compensation:**

a. **Payment for Work and Performance**: Payment for work and performance includes the disbursement of money within a short-term period (weekly, monthly and bonus/annual awards). The total amount of payment given to the employee will depend on the following: - Needs for the specified job. - Results that meet or exceed the standards of quantity, quality or time. - Innovations that lead to the increase in productivity, loyalty, trustworthiness and a combination of some or all of these features. The components that are usually included in the payment for work and performance are basic pay, premium and premium differences, short-term bonus, merit payment and certain allowances.

b. **Payment for Non-working Days**: The past few years have seen a reduction in working hours. In addition, employees today enjoy more official non- working days and longer paid leave. Components of payment for non-working days raise labour costs. On the other hand, such payment allows for lifestyle change and enhancement of the quality of life.

c. **Loss of Job Income Continuation Benefit**: Job security has always been an important aspect of employment. Employees need to be assured of their job and economic security. Accidents, personal problems, work performances are some of the reasons that will cause a temporary cessation of employment or a permanent termination. The change in the current technological and economic climate will limit, and at times eliminate the need and demand for certain products and services. This will lead to the reduction or disintegration of an organisation. Various components, like unemployment insurance, unemployment added-benefits and salary during the severance period, have been generated to assist affected employees who have neither been offered any alternative position by the organisation, nor found other work.

d. **Disability Income Continuation Benefit**: When an employee suffers from a disability due to an illness or accident, he is unable to execute his tasks effectively. In addition to paying for daily living expenses, the employee also has to pay for the hospital bills. Employee compensation, in the form of medical leave and short-term and long-term disability plans, exists to assist an employee who is incapable of working due to poor health.

e. **Deferred Income:** Most employees depend on programmes provided by their employers to ensure a continuous income after retirement. There are two main reasons why such programmes exist. First, most people do not have enough savings upon retirement to enable them to continue enjoying the comfortable lifestyle they were accustomed to when they were working. Therefore, programmes like the retirement allocation planning programme, savings and thrifty plans, annuities and additional income plans are drawn up by organisations to provide employees an ongoing income after their retirement. Secondly, the laws and tax regulations make the deferred income plans more attractive to the employees.

f. **Spouse/Family Income Continuation Benefit**: Employees with families worry that they will not be able to provide and care for and support their dependents in the event of their death or disability. To this end, certain plans have been created to provide the dependents with the financial means to go on if an employee dies or is incapacitated due to temporary or permanent disability.

g. **Health, Accident and Liability Protection**: Apart from income to sustain a comfortable lifestyle, income for products and services to heal an illness or disability is also of great concern to employees. Therefore, an organisation offers various insurance plans to assist employees in paying for their medical care and treatment.

h. **Income Equivalent Payments:** Income equivalent payments are also known as perquisites or perks. Some of these special benefits are exempted from tax, and this is advantageous for employers and employees. Examples of special benefits are provision of credit cards, allowance to attend official meetings, subsidized food and childcare services.

❖ Organizational Compensation Policy:

Employee incentives are a part of some employers' **compensation policies**. Incentives can be based on number of factors, such as performance, sales or other standards the company uses to reward employees for attaining **organizational** and career goals.

D. S. Beach in his book, 'The Management of People at Work' provides 7 principles of compensation administration:

1. The enterprise should have a clear-cut plan to determine differential pay level in terms of divergent job requirements involving varied skills, efforts, responsibilities and working conditions.
2. An attempt should be made to keep the general level of wages and salaries of the enterprise in-line with that obtained in the labour market or industry.
3. Adequate care should be taken to distinguish people from the jobs.
4. Irrespective of individual considerations, care should be taken to ensure equal pay for equal work depending upon flexibility of jobs, of course, variations may be permitted within the pay range.
5. There should be a plan to adapt equitable measure for recognizing individual differences in ability and contribution.
6. Attempt should be made to provide some procedure for handling wage grievances.
7. Adequate care should be taken to inform the employees and the union, if any, about the procedure followed in determining wage rates.

❖ Wage Payment – Features

- It should be simple to operate and easy to understand.
- It should guarantee a minimum wage to each and every worker.
- It should be acceptable to the employer and the employee.
- It should be flexible enough so that changes may be made in future according to the requirements.
- It should ensure the establishment of industrial peace.

❖ Methods of Payment:

1. Time Rate System:

Payment is based on the time, irrespective of the quantity of work done. Predetermined rate per day/ hour/ week or fortnight for the actual time the employees have worked. **Calculated as - Time spent by the worker * Rate per unit of time.**

This system prevails more in engineering and processing industries where it requires skilled workers. Nature of work is unstandardized and less rigid. The minimum wage rate, the need-based minimum wage, fair wage or the living wage fixed by the government or the wage board or through collective bargaining mechanism - are all payments on time rate principles.

Advantages:

- Simplest and economical method.
- Develops a sense of security in workers.
- The quality of the output is maintained.
- Best method suitable for any kind of artistic work.
- Quality of output is of prime consideration
- Minimizes material wastage.

Disadvantages:

- May decrease the moral of the efficient workers.
- Increases the cost of supervision.
- Production may suffer.
- Workers usually work very slow.
- Lack of motivation in workers.

2. Payment by Results:

The payment is based on the output of work produced by an employee/worker or average output of the group of workers to which he belongs. **Calculated as – Number of units produced * Rate per unit.**

The earning of the workers depends on the speed of the work and his own individual skills and efficiency. It is more applicable for simple manual operations where the effort of an individual can be measured in terms of quantity. More appropriate where the nature of work is repetitive and standardized.

Most common schemes of payment by results (individual in character):

- **Straight Piece Rate** – on the basis of number of pieces produced and the rate per piece; that is – payment of a uniform price per unit of production. Mostly seen in industries where production is repetitive in nature and can be easily divided into sub-units.
- **Differential Piece Rate –** payment based on a worker's output which may be higher/lower than the standard level of performance. This system is mostly used where there is heavy non-labour costs involved.

❖ **Scheme of payment by results (group):**

Used mainly in jobs which are interdependent, either because they are performed in sequence as in assembly.

Advantages:

- Induces workers to work more and produce more.
- Reward is related to one's own efforts.
- A very fair method.
- Decreases the cost of supervision.

Disadvantages:

- The workers may feel highly exhausted and fatigued.
- Develops a sense of insecurity among workers.
- Loss of payment due to failure in the machines.
- Affects the quality of production

3. Measured Day Work:

Payment is based on a specified level of performance. This required level of performance can be defined and actual work level monitored with the help of Work Measurement Methods. Emphasizes on incentives paid to the worker for meeting a specified level of performance. Therefore it is often referred as an incentive based payment system. Both the time and speed are considered as the basis of wage payment. These systems provide incentives to the workers to produce more and more maintaining the quality as well. The workers are paid bonus or premium for the additional work.

Advantages:

- Provides opportunity to workers to earn more.
- Reduction in supervision cost.
- Enhances creativity and encourages innovation among workers
- Reduces absenteeism.

Disadvantages:

- Creates jealousness among workers
- Some workers tend to overwork and undermine their health.
- Risky and hazardous to health of workers.
- Quality of work might be affected

- **New Trends in Compensation Management:**

- Performance based bonus for employees emphasizing on their KPAs.
- Tax benefit on fringe benefits.
- Effectiveness of incentives – change in work culture.
- Implementing reward policies and determining monetary and non-monetary incentives.
- Team based incentives enhancing collaboration among individuals.
- External market-sensitive based pay, not internal consistency.
- Risk-sharing partnership, not entitlement.
- Variable pay based on performance factors and not annual increases.
- Employability, and not job security.

- **Concept of Reward:**

Reward is a thing given in recognition of service, effort and achievement. Definition of Reward in Oxford Dictionary "The rewards of something are the benefits that you receive as a result of doing or having that thing." Rewards may be – Monetary or Non-Monetary Reward

- **Money as a motivator: Limited role of financial rewards**

Money is the means for many ends. Maslow's hierarchy of needs theory – Money is essential to meet basic needs (lower order needs).Hertzberg's theory – money is considered as a hygiene factor and motivator, both. Monetary benefits and long-term asset building schemes also provide limited benefits. Money is basically limited to material contract between employer and employees.

- **Non-financial rewards :**

Career opportunities, job-security, learning opportunities, achievements, job responsibility, recognition, learning and likewise. Maslow's hierarchy of needs theory – Non-financial rewards cater to higher order needs. Non-financial rewards strengthen the psychological contract between the employer and the employee. Fairness, Equity, Consistency, security, opportunity to demonstrate and enhance competence, career advancement, involvement, commitment, loyalty and trust of the employees can be developed through non-financial rewards. From an individual's point of view, it essentially contributes to personal growth and fulfilment.

- **<u>Reward Systems:</u>**

Pay, Promotions, Fringe benefits, status symbols are perhaps the most important rewards. Organizations typically rely on reward systems to motivate employees:

- To perform effectively
- To join the organization
- To continue to work
- By indicating their position in the organization structure

<u>Principles for an Effective Reward System:</u>

- Give value to the reward system
- Make it simple to understand.
- Lay down performance standards within the control of the team.
- Make the system fair and effective.
- Ensure participation in the rewards system.

Involve people in the rewards process and empower them to do the need

- **<u>Rewards Influencing Behaviour:</u>**

In order to be effective in influencing behaviour, reward systems should satisfy four key design requirements:

1. Contingency
2. Equitable
3. Value
4. Saliency

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- **Reward Management Strategies:**

  Creating a positive and natural reward experience for employees to understand, accept and support the reward system. Aligning rewards with business goals to create a win-win partnership for both the company and its workforce. Establishing clear linkages between performance appraisal and reward systems. Rewarding results with variable pay, which helps people extend their line of sight to company needs and values. Provide flexibility within the reward framework so that individual business units can vary their programme based on their particular business needs. Clearly articulated, so that recipients must know what is being rewarded and why.

- **Rewards and Employee Satisfaction**

- How much is received and How much an individual feels should be received.
- Comparisons with what happens to others – both, inside and outside the organization. They usually rate their inputs higher than others.
- Reward to their internal feelings of competence, achievement, personal growth, and self-esteem.
- Basis of monetary and non-monetary rewards.
- Many extrinsic rewards are important and satisfying only because they lead to other awards, or because of their symbolic value.

MODULE 2: THEORETICAL DIMENSIONS OF WAGES, COMPENSATION AND REWARD SYSTEMS

No matter how exciting and fascinating a job assignment is, pay affects the way people work, how much they work and how well they work. A large part of the compensation that people receive from work is monetary. Wages, salaries and many employee benefits and services are forms of compensation. Although managers are expected to conserve money and distribute it wisely, many employees feel that they should get more of it for what they do.

Wage Concepts:

Money paid to the workers (blue collar workers), is considered as wages.In earlier ages, the remuneration was determined in the quantum of commodities to be exchanged for labour. With the advent of money, the wages are now paid in coins/notes and/or in commodities. Etymologically, any remuneration paid for services is regarded as Wages. The Oxford English Dictionary defines "wages" as "a payment to a person for service rendered…., the amount paid periodically, especially by the day or week or month, for the time during which work-man or servant is at employer's disposal."

Wages, in the widest sense, means any economic compensation met by the employer under some contract to his employees for the services rendered by them. Normally, they are composed of two parts:

a) **Basic Wage:** is the remuneration which is paid or payable to an employee in terms of his contract of employment for the work done by him.
b) **Other allowances:** are paid in addition to the basic wage to maintain its value over a period of time. Ex – Dearness Allowance.

<u>Wage Structure and Components:</u>

In the Indian context, soon after the independence, Government of India set up a Committee on Fair Wages in 1948 which has defined various concepts of wages which govern the wage structure in the country specially in those sectors which can be termed as underpaid and where workers do not have bargaining power through unions. These concepts are:

i. Minimum wage,
ii. Fair wage
iii. Living wage, and

Later, the concept of need-based minimum wage was added.

Minimum Wage: A minimum wage is one which has to be paid by an employer to his workers irrespective of his ability to pay. According to the above committee,

"Minimum wage is the wage which must provide not only for the bare sustenance of life, but for the preservation of the efficiency of the workers. For this purpose, minimum wage must provide some measure of education, medical requirements and amenities. "

This Act empowers the Central Government as well as State Governments to fix minimum wages from time to time. Wherever this Act applies, the payment of minimum wages is mandatory.

In **1957, Indian Labour Conference** elaborated the concept of fixation of minimum wages which were termed as need-based minimum wages. For the calculation of wages, the Conference suggested the following guidelines:

1. 1. The standard working class family should be taken to consist of three consumption units for the earner; the earnings of women, children and adolescents should be disregarded.
2. 2. The minimum food requirements should be calculated on the basis of the net intake of 2.700 calories for an average Indian adult.
3. The clothing requirements should be estimated at a per capita consumption of 18 yards per annum per person, which could give for the average worker's family of four, a total of 72 yards.
4. In respect of housing, the norms should be the minimum rent charged by the Government in any area for houses provided under subsidized housing scheme for low-income groups.
5. Fuel, lighting and other miscellaneous items of expenditure should constitute 20 per cent of the total minimum wage.

Fair Wage:

The concept of fair wage is linked with the capacity of the industry to pay. A fair wage is, in the opinion of the Indian National Trade Union Congress, " a step towards the progressive realization of a living wage." The Committee on Fair Wages has defined fair wage as follows:

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"Fair wage is the wage which is above the minimum wage but below the living wage. The lower limit of the fair wage is obviously the minimum wage: the upper limit is to be set by the capacity of the industry to pay."

Calculation of wage depends on various factors like labor productivity, prevailing wage rates, the level of national income and its distribution and the capacity of industry to pay.

Living wage:

Along with the minimum wage the Committee on Fair Wages has given the concept of living wage which has been defined by Justice Higgins is as follows:

"A living wage is one which should enable the earner to provide for himself and his family not only the bare essentials of food, clothing and shelter but a measure of frugal comfort including education for his children, protection against ill-health, requirements of essential social needs and a measure of insurance against the more important misfortunes including old age. "

Living wage is more than the concept of minimum wage. Such a wage is determined keeping in view the national income and paying capacity of industrial sector. It was recognized that the present level of our national income does not permit the payment of "living wage" on standards prevailing in more advanced countries, Therefore it should be implemented in three phases. In the initial stage the wages to be paid to the entire working class were to be established and stabilized. In the second phase fair wages were to be established in the community and industry.
In the final phase the working class was to be paid the living wage.

There are **three possible ways** of obtaining some indication as to what constitutes a living wage:

1. It should be sufficient to purchase the minimum theoretical needs of a typical family, calculated in accordance with some more or less scientific formula.
2. It should be sufficient to pay for a satisfactory basic budget, as revealed by a survey of actual family expenditures.
3. It should be comparable with a living wage already established in similar circumstances.
4. It is a difficult task to fix a living wage in terms of money as it differs from country to country and from time to time, according to national economy and social policies.

<u>Wage Theories:</u>

Traditionally, labourers did not have any bargaining power and therefore never had a say in the determination of wages paid out to them. This led to the advent of many wage theories. A variety of new social ideas, institutional forces, ethical considerations, political and economic factors, demands of social justice and equity are at work in the establishment of a wage level and a wage structure. The first wage theories were economic theories.

J. Dunlop opined, the history of wage theory may roughly be divided into three periods.

1. Upto 1870 – Wage Fund Theory
2. Upto 1914 – Theory of Marginal Productivity
3. Extending from the 1st World War till the present day – Collective Bargaining and Keynesian enquiry into the General Wage level and employment.

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1. Subsistence Theory:

This theory is originated from the physiocratic school of the French economists and was commonly accepted during the 19th century. The German economists Lassalle, called it **the iron law of wages or the Brozen law of the wages**. Karl Marx made it the basis of his theory of exploitation. Ricardo's name is also associated with this theory although he did not agree entirely with it. Really speaking there is bargain between the capitalist and the workers over the division of product. Interest of these two parties is by no means the same.

The men desire to get as much and the master to give as little as possible. Both try to combine together to improve the bargain each in his favour. In disputes with their workmen masters must generally have advantage. This would suggest that wages usually tend to be kept down to the minimum possible level.

Subsistence theory of wages is linked to the notion of population. According to this theory wages tend to settle at the level just sufficient to maintain the workers and his family at the minimum subsistence level if wages rise above the subsistence level, the workers are encouraged to marry and to have large families. The large supply of labour brings wages down to the subsistence level if wages fell below these level marriages and births are discouraged and under nourishment increases the death rate. Ultimately labour supply is decreased, and the wages again rise to the subsistence level.

❖ **Criticisms:**

- Ignores the demand side of labour
- No direct relationship between wage level and population
- Ignores trade unions
- Not flexible wage level
- Exploitative

2. Wage Fund Theory:

This theory is associated with the name of J.S. Mill. "Wages" according to Mill, "depend upon the demand and supply of labour, or as it is often expressed, on the proportion between population and capital. By population here, he means the number of the labouring classes or rather of those who work for hire, and by capital, only circulating capital and not even the whole of that but the part which is expended on the direct purchase of labour; Mill asserted "wages not depend upon the relative amount of capital and population but cannot under the rule of competition be affected by anything else".

Mill implies that if a legal minimum wage were to raise wages in one industry the result must be either to cause unemployment or lower wages elsewhere. This view that wages were limited by capital was called by Marshall the Vulgar form of the wage fund theory.

According to this theory, therefore, wages are depended upon two quantities, viz, (i) the wage fund or the circulating capital set aside for the purchase of labour and (ii) the number of labourers seeking employment. Hence, the level of wages can be ascertained by means of a simple arithmetical operation, by dividing the wages fund by the number of workers. In other words, wages vary directly as the quantity of capital and inversely as the number of workers. Wages, thus, cannot rise unless either the wage fund increases or the number of workers decreases but since the theory takes the wage funds fixed; wages could rise only by a reduction in the number of workers. It would appear, therefore, that according to this theory efforts of trade union to raise wages would prove full. If they succeeded in raising wages in one trade, it can only be at the expense of another, since the wage fund is fixed and the trade unions have no control over population, accordingly to this theory, therefore, trade unions cannot raise wages for the labour class as a whole.

$$wage\ level = \frac{\text{wage fund}}{\text{no. of workers employed}}$$

$$W = \frac{\text{W.F}}{\text{N}}$$

$$W \propto \frac{1}{\text{N}}$$

The exponents of this theory explain that wages cannot be generally higher than the normal rate without utilizing same of the funds that are necessary to purchase raw materials and other items of expenditure such a condition tends to drive capital out of an industry and thus, automatically reduces amount available for wages available for wages.

- **Criticisms:**
  - Lack of source and estimation methods
  - Unscientific and Illogical
  - Neglects the quality and efficiency of workers
  - Failed to explain the differences in wage rate.

3. Residual Claimant Theory:

This theory of wages has been advanced by the American Economist Walker. According to this theory, the labourers are paid what is left after making payments to other factors of production in the form of rent interests and profits. Rents, interest and profits, according to Walker, are determined by definite law but as there is no specific law by which wages are determined, the workers get their what remains after payment of rent interest and profits, therefore, if an account of greater efficiency the national dividend it is increased, the wages may also increase.

This theory has certain obvious defects. It does not explain how trade unions are able to raise wages. Besides, wages are generally fixed even before production takes place and the residual claimant is not the worker but the entrepreneur then, if rent, interest and profits can be explained by definite laws, as walker says there is no reasons why wages also cannot be similarly explained. Further the theory is criticized on the ground that it ignores influence of supply of labour on wages.

Criticisms:

1. This theory assumes that the share of landlords, capitalists and entrepreneurs are fixed and it is absolutely wrong.
2. It does not explain the influence of trade union in wage determination.
3. The supply side of labour has been totally ignored by the theory.

4. Marginal Productivity Theory:

It was a direct out-growth of this intellectual movement and dominated sound economist though from the theory represents on approach to the problem of
wages from demand side. It holds that labour market is in equilibrium when price at which labour is hired is equal, at the margin to its demand price, wages are thus determined in accordance with marginal productivity of labour which varies directly with the tools it has to work with.

Marginal productivity is defined as the additional product, resulting from using an additional unit of labour together with a constant amount of other factors of production. It is held that employers go on employing more and more units of labour as long as the net product of labour is greater than the rate of wages payable. It assume that a point will came when the value of increase on the product due to employment of a given unit of labour is marginal one and its rates of wages will settle wage rate payable to other.

To put it in other way marginal productivity provides the basis for a adjustment of wages from time to time. The marginal worker is marginal in the sense that his employment at existing prices and wages completes supply of labour for a given employer as he cannot go beyond this limit of engaging labour in his economic interest. The general level of wages in the long period is as such determined by capital labour ratio. If capital investment is high, relative to the number employed, the wage will be high, if capital investment is low, there will be limited equipment for workers to use productivity will be low and the wage which comes out of product can only be small.

❖ **Assumptions of this theory:**

1. There is perfect competition in market.
2. Labour is homogeneous.
3. Perfect substitutability.
4. All factors of production would be kept constant except labour.
5. Country should have full employment.

❖ **Criticism:**

- Assumption of a perfect competition in market is wrong.
- Deals with demand side only.
- Unjust theory as workers should be paid based on their productivity.
- Factors of production are neither mobile nor perfect substitutes.
- Other factors of production may vary.
- Fails to explain the differences in wages.
- Full employment is a myth, not reality.

5. Surplus Value Theory:

Karl Marx accepted Ricardo's subsistence theory of wages but for a different reason than that given by the classical economists. In Marx's estimation, it was not the pressure of population that drove wages to the subsistence level but the existence of large numbers of unemployed workers. He blamed unemployment on capitalists.

To Marx, in capitalism, production was not simply production of commodities, but was production of surplus value.The worker produces not for himself but for the capitalist. From capitalist point of view, that labourer alone is productive who produces a surplus. Under capitalism, labour power itself becomes a commodity and is bought and sold in the market. The main aim of the capitalist is to maximise profit. It is possible for him because labour power has the peculiar character of being able to create more value than is needed for its own production.

In other words, the worker can produce more in a day's labour than is needed for his own subsistence. The capitalist pays only those wages with which the latter can purchase the means of subsistence. Thus Marx divided the labour into two kinds-necessary labour and surplus labour.

For example, let us assume that if a labourer works for eight hours a day to produce a commodity, it is sufficient to maintain himself. Then the exchange value of the product should be equal to 8 hours labour. But if the wages paid to the labourer are equal to four hours labour-this labour is the necessary labour and the remaining four hours is known as surplus labour (which goes to the capitalist)

Thus surplus value is the difference between the selling price of the commodity and the actual wages paid to the labourer. In a capitalist society the workers are thus exploited by the capitalists.

Marx classified capital as constant capital and variable capital. Capital invested in stocks or raw materials or equipment's which directly assist the productivity of labour was called by Marx as constant capital. Capital spent for the purchase of labour power in the form of wages was called variable capital. According to Marx, it was only the variable capital which was capable of creating surplus value.

Criticisms:

- Ignores the demand side
- Labour alone does not create surplus
- Exaggeration of the scope of exploitation
- Rate of profit does not only depend on variable capital

6. Bargaining Theory:

Earlier theories of wages have been rendered invalid or at least inadequate, as a result of collective bargaining by trade unions. Bargaining Theory was propounded by **John Davidson** in 1989.
According to him, wages are determined by the relative bargaining power between workers or trade unions and employers; and basic wages, benefits, job differentials and individual differences tend to be determined by the relative strength of the organization and the trade union.

Collective bargaining provides an example of what is sometimes called bilateral monopoly, the trade union being the monopolist supplier and the employer's association, the monopolist buyer of a particular kind of labour.

Davidson viewed that there should be upper and lower limits for the rate for the given type of labour. The upper limit is that rate above which the employer will refrain to hire a certain group of workers, and the lower limit is the rate below which workers refuse to work. Demand and supply analysis play an important role in formulation of the limits. The wage paid within this range depends on the relative bargaining power of labour and employees.

7. Employment Theory:

There are essentially two schools of thought which propounded the inter-relationship between wages and employment. One was by the classical economists like J. B. Say and Pigou. According to this school, unemployment would disappear if the workers were to accept a voluntary cut in wages. They strongly pleaded for wage flexibility as a means of promoting employment at a time of depression in an organization. These wage-cuts, according to them, would lead to a consequent fall in prices in the economy. This fall in prices would cause additional demand necessitating increased production and hence employment of more workers.

A new approach was developed by **John Maynard Keynes** in his book ***General Theory of Employment, Interest and Money*** (1936). In his theory of employment, he advocated **wage rigidity** in place of wage flexibility. Keynes viewed that a wage cut leads to a serious reduction in aggregate effective demand on account of a cut in the purchasing power of the working class and thereby leads to reduced employment.

8. Competitive Theory:

Economists have traditionally stressed on demand and supply as the two important forces behind wage determination.

Adam Smith, argued that if wages were fixed according to demand and supply, the workers would be attracted by high wages to industries, occupations and localities where they were most needed and would tend to leave industries and places where the supply was greater than the demand.

The basic assumption of this theory is that – employers compete among themselves by offering a higher wage to attract employees during excess demand situation; While the employees compete with others for jobs by offering their services for a lower wage, when there is excess supply.

Competition, therefore is essentially a disequilibrium process by which excess demand and excess supply cause changes in wages.

Basic assumption of this theory is – Neither employers nor employees combine together to influence demand or supply conditions and that markets are perfect.

Criteria for Wage Fixation:

- The organization's ability to pay
- Supply and demand of labour
- The prevailing market rate
- The cost of living
- Living wage
- Productivity
- Trade Union’s bargaining power
- Job requirements
- Managerial Attitudes
- Psychological and sociological factors
- Levels of skills available in the market

Broad banding:

It is a method of grouping jobs with similar duties, responsibilities and determining pay that makes compensation system more flexible. Broad banding reduces number of salary levels. **This** method evolved as organizations wanted to flatten their hierarchies. It has a fixed minimum and maximum level, which overlaps with each other. For example, if a salary band for entry level is 10,000- 18,000 then salary band for next level can be 12,500-22000. But the traditional narrow band: salary band for entry level will be 10000-12000 & for next level it will be: 12500-14500.

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Advantages of Broad banding:

- Gives manager a free hand to fix the pay of individual workers.
- It reduces employee resistance to being shifted laterally in organization.
- Helps organization to avoid unnecessary distinction based on level or status.
- Variable compensation
- Designed to pay in accordance with performance not in accordance with position.

MEANING AND DEFINITION OF EXECUTIVE COMPENSATION:

Executive compensation is how top executives of business corporations are paid. This includes a basic salary, bonuses, shares, options and other company benefits. Over the past three decades, executive compensation has risen dramatically beyond the rising levels of an average worker's wage. Executive compensation is an important part of corporate governance, and is often determined by the company's board of directors. According to Tapomoy Deb, "Executive compensation refers to short-term and long-term financial and non- financial rewards given to the top ranking executives under, a contractual, legal and contractual mandate".

The importance of compensation system in executive compensation is their impact on attracting, retaining and motivating the executives.

The **Five basic elements** of Executive Compensation are: basic salary, employee benefits, short-term incentives, long-term incentives and perquisites. The Executives not only expect to be properly paid for their performance and to receive promotions when they have demonstrated their ability to assume greater responsibility, they also expect formal recognition.

ELEMENTS OF EXECUTIVE COMPENSATION:

- **Salary** – is the first component of executive compensation and makes up for 40-60% of top managers' annual compensation. Job evaluation plays only a part, a senior executive is paid for his capabilities and for the job he/she performs. Salary for the executives varies by the type of job, size of the organization region of the country and the type of the industry.

- **Bonus or Profit-sharing bonus –** is a type of short term incentive paid annually and is based on performance or profit-sharing. The bonus for executives vary from one organization to the other. In some, the board of Directors and CEO make a subjective judgement, and some others tie it to return on investment, and few others pay it based on a target of 10% increase in corporate earnings from the previous year.

- **Long term incentives/stock options –** Companies allow their managers to purchase their shares at fixed prices. The stock options are valuable as long as the price of the share keeps increasing. When the company starts incurring losses, the share price crashes. It is a king of offering large rewards to executives.

- **Fringe Benefits –** The top level executives receive benefits like other employees – the protection program benefits but with supplemental coverage that provides enhanced benefit levels. They also get employees services in terms of exclusive benefits known as perquisites or perks. These perks can be company car, recreational facilities (country club and athletic club memberships, travel perks (first class airfare), Tickets to sporting events, etc.

Theoretical explanations for setting executive compensation:

1. **Agency Theory:** The central issue of this theory is "How to pay the executives rather than determining how much to pay?" According to this theory, shareholders delegate control to top executive to represent their ownership interests. However, top executives usually do not own majority shares of their companies' stocks. Consequently, executives do not share the same interest as the collective shareholders. This makes executives to pursue activities that benefit themselves rather than the shareholders. The actions of the executives on behalf of their own self-interest are known as the agency problem. Hence, executives may emphasize on the attainment of long-term objectives. As a result, the BODs may pay Annual bonuses on short-term gains or award company stock to align executives' interest with the shareholders' interest.

2. **Tournament Theory:** This theory casts lucrative executive compensation as the prize in a series of tournaments or contests among the middle and top level managers who aspire to become CEO. Winners at one level of the tournament enter the next-level of tournament. In other words, an employee's promotion to a higher rank signifies a win, and more lucrative compensation (higher base pay, incentives, enhanced benefits, and perks) represents the prize. The ultimate prize is promotion to CEO and a lucrative executive compensation package. The chance of winning competition decreases dramatically as employees rise through the ranks: there are fewer positions at higher levels in corporate hierarchical structure.

3. **Social Comparison Theory:** According to this theory, individuals need to evaluate their accomplishments, and they do so by comparing themselves to similar individuals. Demographic characteristics like age or race, and occupation are common comparative bases. Individuals tend to select social comparisons that are slightly better than themselves. The compensation committee members probably rely on their own compensation packages and the compensation packages of CEOs of other companies of equal or greater stature.

Approaches to Executive Compensation:

1.Economic Theory Approach: The classical economists talk largely about the determination of profits to the owners rather than compensation to the owners. These economists hold a market approach to management compensation wherein , executive ability, like any other factor of production, has a price which is determined by the interaction of the supply of and the demand for such an ability. Therefore, they view that management compensation is determined by external factors.

The **focus of the economists' approach** lies in:

- Explaining in broad - compensation overtime,
- Explaining the relative differences in compensation levels among various types of abilities or occupations,
- Forecasting trends in the demand for and supply of various types of personnel.

2. **Administrative Theory Approach:** These theorists consider executive compensation as an integral part of organizational planning and control. The compensation system is expected to support the structure and strategy of the organization. Different compensation systems (Ex-Salesmen's, Divisional manager)

are considered appropriate for different types of organization and are expected to serve specific sub-goals. The administration is thus concerned with the designing of an appropriate compensation system for a given organization, the identification of the factors determining it and the relationships of such a system with other aspects of administration.

Different philosophies of top management results in wide range of compensation practices like:

- One looks at it as cost and other as a motivational device,
- Some pay straight salary, others combine it with bonus,
- Some are generous in compensation management while other are niggardly,
- Some are committee managed and others hold the individual accountable for specific responsibilities;
- Some set high standards, others accept inadequate work without question.

3. Social Science Approach: Social Scientists have viewed the executive as an individual with needs, drives and motivations and as a person and as a member of several groups. This approach is based on the application of psychology and sociology and is more general than the economic approach and the administrative approach.

These theorists focus on:

- ➢ The factors that motivate individuals to work,
- ➢ The role of money in motivation,
- ➢ The relationship between satisfaction with pay and individual performances,
- ➢ The role of perceived equity in payment on the level of performance.

Lawler and Porter through their surveys found that when pay was held constant, there was no difference at various levels in the importance that managers attached to pay. On the other hand, when the management level was held constant higher paid managers gave less importance to pay than lower-paid managers. Money, served as a powerful motivator the executive level as per the study of Anand, who did an exploratory study of the levels and forms of executive compensation in the context of executive job satisfaction and turnover. Some Social Scientists also revealed that the nature of technology employed has an effect upon the level of compensation. The levels and patterns of executive compensation vary between industries and firm size and with the type of technology employed.

<u>Executive Compensation Planning and Administration:</u>

Executive Compensation is different from that of compensating other employees or groups of employees in several ways:

- Compensation practices at the executive and managerial level set the tone for the practices at the lower levels of management;
- Executive and managers typically have greater latitude to "make their own jobs" than personnel at lower organization levels.
- The results achieved by the company as a whole or by a profit center within the company are more likely to reflect accurately the personnel contributions of higher level executives or managers than those of employees at lower levels,
- Executive compensation different from other levels:
- The compensation of higher level executives is subject to high personnel income tax.
- The HR department often plays a more limited role, particularly in smaller companies in dealing with compensation for executives and managers than with compensation for other groups.

Key Requirements in Executive Compensation Planning and Administration:

- Compensation should be competitive with what other employers are paying for similar skills and jobs;
- Compensation paid to various individuals in an organization should reflect the comparative value of their respective contributions to that organization,
- Compensations decisions should be made and communicated in a way that is perceived as rational and fair.

Important aspects of Executive Compensation Planning and Administration:

- Position Level
- Salary Structure
- Performance Appraisal
- Incentive Bonus Plans
- Supplementary forms of compensation

MODULE-3: WAGE DETERMINATION AND WAGE ADMINISTRATION IN INDIA:

WAGE/SALARY COMPONENTS

Wage and salary administration affect levels of employee commitment to the organisation. However, fascinating the individual's job assignment is, the employee must be paid. Pay affects the way people work-how much and how well. A large part of the compensation that people receive from work is monetary. Although managers are expected to conserve money and distribute it wisely, many employees feel that they should get more of it for what they do. Wages, salaries and many employee benefits and services are form of compensation. Contemporary employment reward systems attach great prominence to wages and salaries. In the evolution of economics, the role of financial rewards has grown. The sophistication of wage and salary administration has increased as industrialized economies have become more complex. New suggestions for managing compensation systems are constantly emerging.

Meaning of Wage and Salary:

Wage and Salary administration, also known as Compensation management, remuneration management, or reward management, is concerned with designing and implementing total compensation package. The traditional concept of wage and salary administration emphasised on only determination of wage and salary structures in organisational settings. However, entered the business field which necessiated to take wage and salary administration in comprehensive way with a suitable change in its nomenclature. Beach has defined wage and salary administration as follows:
"wage and salary administration refers to the establishment and implementation of sound policies and practices of employee compensation. It includes such areas as job evaluational, surveys of wages and salaries, analysis of relevant organisational problems, development and maintenance of wage structure,

establishing rules for administering wages. wage payments, incentives, profit sharing, wage changes and adjustments, supplementary payments, control of compensation costs and other related items"

Concept of Wage and Salary

Wage and salary are the most important component of compensation and these are essential irrespective of the type of organisation. Wage is referred to as remuneration to workers particularly, hourly-rated payment. Salary refers to as remuneration paid to white-collar employees including managerial personnel. Wages and salary are paid on the basis of fixed period of time and normally not associated with productivity of an employee at a particular time.

Objectives Of Wage And Salary Administration

A sound plan of wage and salary administration seeks to achieve the following objectives:

1. To establish a fair and equitable compensation offering similar pay for similar work.
2. To attract competent and qualified personnel.
3. To retain the present employees by keeping wage levels in tune with competitive units.
4. To keep labour and administrative costs in line with the ability of the organisation to pay.
5. To improve motivation and morale of employees and to improve union management relations.
6. To project a good image of the company and to comply with legal needs relating to wages and salaries.
7. To establish job sequences and lines of promotion wherever applicable.
8. To minimize the chances of favoritisms while assigning the wage rates.

According to D.S. Beach, was and salary administration has four main purposes.

1. To recruit persons for a firm
2. To control payroll costs
3. The satisfy people, to reduce the incidence of quitting, grievances and fractions over pay and
4. To motivate people to perform better.

Principles of Wage and Salary Administration:

The following principles should be followed for an effective wage and salary administration;

1. Wage policy should be developed keeping in view the interests of all concerned parties viz., employer, employees, the consumers and the society.

2. Wage and salary plans should be sufficiently flexible or responsive to changes in internal and external conditions of the organization.

3. Efforts should be made to ensure that differences in pay for jobs are based on variations in job requirements such as skill, responsibility, efforts and mental and physical requirements.

4. Wage and salary administration plans must always be consistent with overall organizational plans and programmes.

5. Wage and Salary administration plans must always be in conformity with the social and economic objectives of the country like attainment of equality in income distribution and controlling inflation, etc.

6. These plans and programmes should be responsive to the changing local and national conditions.
7. Wage and salary plans should expedite and simplify administrative process.
8. Workers should be associated, as far as possible, in formulation and implementation of wage policy.
9. An adequate data base and a proper organizational set up should be developed for compensation determination and administration.
10. The general level of wages and salaries should be reasonably in line with that prevailing in the labour market.
11. There should be a clearly established procedure for hearing and adjusting wage complaints. This may be integrated with the regular grievance procedure, if it exists.
12. The workers should receive a guaranteed minimum wage to protect them against conditions beyond their control.
13. Prompt and correct payments to the employees should be ensured and arrears of payment should not accumulate.
14. The wage and salary payments must fulfill a wide variety of humanneeds including the need for self-actualization.
15. Wage policy and programme should be reviewed and revised periodically in conformity with changing needs. For revision of wages, wage committee should also be preferred to the individual judgment however unbiased of a manager.

<u>Wage Structure</u>

According to economic theory, wages are defined broadly as any economic compensation paid by the employer to his labourers under some contract for the services rendered by them. In its actual sense which is prevalent in the practice, wages are paid to workers which include basic wages and other allowances which are linked with the wages like dearness allowances, etc. Traditionally, in the absence of any bargaining power possessed by labourers, they did not have any say in the determination of wages paid to them. This has led to the development of several theories of wages such as subsistence theory by Ricardo, wage fund theory by Adam Smith, surplus value theory by Karl Marx, residual claimant theory by Frascis Walker, marginal productivity theory by Philip Wickstted and John Clark, bargaining theory by John Davidson. andbehaviouraI theory by James March and Herbert Simon. Each theory tries to explain how wages are determined. In the Indian context, soon after the independence, Government of India set up a Committee on Fair Wages in 1948 which has defined various concepts of wages which govern the wage structure in the country specially in those sectors which can be termed as underpaid and where workers do not have bargaining power through unions. These concepts are: i) minimum wage,
ii) Living wage, and
iii) Fair wage.
Later, the concept of need-based minimum wage was added. Let us have a brief look at these concepts.

Minimum Wage
A minimum wage is one which has to be paid by an employer to his workers irrespective of his ability to pay. According to the above committee,

"Minimum wage is the wage which must provide not only for the bare sustenance of life, but for the preservation of the efficiency of the workers. For this purpose, minimum wage must provide some measure of education, medical requirements and amenities. "

Subsequent to the committee's report, Government enacted legal provisions regarding minimum wages under the Minimum Wages Act. 1948. This Act does not define the concept of minimum wages but empowers the Central Government as well as State Governments to fix minimum wages from time to time. Wherever this Act applies, the payment of minimum wages is mandatory. In 1957, Indian Labour Conference elaborated the concept of fixation of minimum wars which were termed as need-based minimum wages.

For the calculation of wages, the Conference suggested the following guidelines:

1. The standard working class family should be taken to consist of three consumption units for the earner; the earnings of women, children and adolescents should be disregarded.
2. The minimum food requirements should be calculated on the basis of the net intake of2.700 calories per adult.
3. The clothing requirements should be estimated at a per capita consumption of 18 yards per annum per person.
4. In respect of housing. the norms should be the minimum rent charged by the Government in any area for houses provided under subsidized housing scheme for low-income groups.
5. Fuel. Lighting and other miscellaneous items of expenditure should constitute 20 per cent of the total minimum wage.

Living Wage

Along with the minimum wage the Committee on Fair Wages has given the concept of living wage which has been defined as follows:

"A living wage is one which should enable the earner to provide for himself and his family not only the bare essentials of food, clothing and shelter but a measure of frugal comfort including education for his children, protection against ill-health, requirements of essential social needs and a measure of insurance against the more important misfortunes including old age. "

Living wage is more than the concept of minimum wage. Such a wage is determined keeping in view the national income and paying capacity of industrial sector. The Committee also observed that since the national income did not support the payment of living wage. it should be implemented in three phases. In the initial stage the wages to be paid to the entire working class were to be established and stabilised. In the second phase fair wages were to be established in the community and industry. In the final phase the working class was to be paid the living wage.

Fair Wage

The concept of fair wage is linked with the capacity of the industry to pay. The Committee has defined fair wage as follows:

"Fair wage is the wage which is above the minimum wage but below the living wage. The lower limit of the fair wage is obviously the minimum wage: the upper limit is to be set by the capacity of the industry to pay. "

Thus, fair wage depends on different variables affecting wage determination. Such factors are labour productivity prevailing wage rates, the level of national income and its distribution and the capacity of industry to pay. At present, the concept of fair wages is followed by the most business organizations.

Components of Wage and Salary:

An average employee in the organized sector is entitled to several benefits-both financial as well as non-financial. To be specific, typical remuneration of an employee comprises:

Wages and Salary:

Wages represent hourly rates of pay, and salary refers to the monthly rate of pay, irrespective of the number of hours put in by an employee. Wages and salaries are subject to annual increments. They also differ from employee to employee, and depend upon nature of job, seniority, and merit.

Incentives:

Also called ―payments by results‖, incentives are paid in addition to wages and salaries.
Incentives depend upon productivity, sales, profit or cost reductionefforts.There are:

i) Individual incentive schemes and
ii) Group incentive programmes.

Individual incentives are applicable to specific employeeperformance.Where a, given task demands group effort for completion, incentives are paid to the group as a whole. The amount is later divided among group members on an equitable basis.

Fringe Benefits:

These include such motley crowd of employee benefits as provident fund, gratuity, medical care, hospitalization, accident relief, health and group insurance, canteen, uniform, recreation and the like.

Perquisites:

These are allowed to executive and include company car, club membership, paid holidays, furnished house, stock option scheme and the like. Perquisites are offered to retain competent executives.

Non-monetary Benefits:

These include challenging job, responsibilities, and recognition of merit, growth prospects, competent supervision, comfortable working conditions, and job sharing and flexi time.

Factors Influencing Wages And Salaries

A number of factors, thus, influence the remuneration payable to the employees. These factors can be categorized into

(i) External Factors and
(ii) Internal Factors.

A. External Factors

External factors influencing wages and salaries are as discussed below:

1. **Demand and Supply:** the labour market conditions or demand and supply forces operate at the national and local levels and determine organizational wage structure. When the demand of a particular type of labour is more and supply is less then the wages will be more. On the other hand, if supply of labour is more demand on the other hand, is less then persons will be available at lower wage rates also. In the words of Mescon, ‗the supply and demand compensation criterion is very closely related to the prevailing pay, comparable wage and on going wage concepts since, in essence all of these remuneration standards are determined by immediate market forces and factors.
2. **Cost of Living:** The wage rates are directly influenced by cost of living of a place. The worker swill accept a wage which may ensure them a minimum standard of living. Wages will also be adjusted according to price index number. The increase in price index will erode the purchasing power of workers and they will demand higher wages. When the prices are stable then frequent wage increases may not be undertaken.
3. **Trade Unions‘Bargaining Power: The** wage rates are also influenced by the bargaining power of trade unions. Stronger the trade union higher well be the wage rates. The strength of a trade union is judged by its membership, financial position and type of leadership. Union‘s last weapon is strike which may also be used for getting wage increases. If the workers are disorganized and disunited then employers will be successful in offering low wages.
4. **Government Legislation:** To improve the working conditions of workers, government may pass legislation for fixing minimum wages of workers. This may ensure them minimum level of living. In under developed countries bargaining power of labour is weak and employers try to exploit workers by paying them low wages. In India, Minimum Wages Act, 1948 was passed to empower government to fix minimum wages of workers.
5. **Psychological and Social Factors: Psychological** the level of compensation is perceived as a measure of success I of life. Management should take into consideration the psychological needs of the employees while fixing the wage rates so that the employees take pride in their work. Sociologically and ethically, the employees want that the wage system should be equitable, just and fair. These factors should also be taken into consideration while devising a wage programme.
6. **Economy:** Economy also has its impact on wage and salary fixation. While it may be possible for some organisations to thrive in a recession, there is no doubt that economy affects remuneration decisions. A depressed economy wills probably increase the labour supply. This, in turn, should lower the going wage rate.
7. **Technological Development:** With the rapid growth of industries, there is a shortage of skilled resources. The technological developments have been affecting skills levels at faster rates.Thus, the wage rates of skilled employees constantly change and an organization has to keep its level unto the mark to suit the market needs.

8. **Prevailing Market Rates:** No enterprise can ignore prevailing or comparative wage rates. The wage rates paid in the industry or other concerns at the same place will form a base for fixing

wage rates. If a concern pays low rates then workers leave their jobs whenever they get a job somewhere else. It will not be possible to retain good workers for long.

B. Internal Factors

The important internal factors affecting wage and salary decisions are as follows:

1. **Ability to Pay:**The ability to pay of an enterprise will influence wage rates to be paid. If the concern is running into losses then it may not be able to pay higher wage rate.A profitable concern may pay more to attract good workers. During the period of prosperity, workers are paid higher wages because management wants to share the profits with labour.
2. **Job Requirements:** Basic wages depend largely on the difficulty level, and physical and mental effort required in a particular job. The relative worth of a job can be estimated through job evaluation. Simple, routine tasks that can be done by many people with minimum skills receive relatively low pay. On the other hand, complex, challenging tasks that can be done by few people with high skill levels generally receive high pay.

3. **Management Strategy:** The overall strategy which a company pursues should determine to remuneration to its employees. Where the strategy of the organisation is to achieve rapid growth, remuneration should be higher than what competitors pay. Where the strategy is to maintain and protect current earnings, because of the declining fortunes of the company, remuneration level needs to be average or even below average.
4. **Employee:** Several employees related factors interact to determine his remuneration.
   - (i) Performance or productivity is always rewarded with a pay increase. Rewarding performance motivates the employees to do better in future.
   - (ii) Seniority. Unions view seniority as the most objective criteria for pay increases whereas management prefers performance to affect pay increases.
   - (iii) Experience. Makes an employee gain valuable insights and is generally rewarded.
   - (iv) Potential. Organizations do pay some employees based on their potential. Young managers are paid more because of their potential to perform even if they are short of experience.
   - (v) Luck. Some people are rewarded because of their sheer luck. They have the luck to be at the right place at the right time.

<u>**INCENTIVES:**</u>

Meaning of Incentive

Incentive‟ may be defined as any reward of benefit given to the employee over and above his wage or salary with a view to motivating him to excel in his work. Incentives include both monetary as well as non-monetary rewards. A scheme of incentive is a plan to motivate individual or group performance.

<u>**Definitions of Incentive**</u>

The following are some of the definitions of the term „Incentive‟:

1. Wage incentives are extra financial motivation. They are designed to stimulate human effort by rewarding the person, over and above the time rated remuneration, for improvements in the present or targeted results" – **The National Commission on Labour.**

2. "It refers to all the plans that provide extra pay for extra performance in addition to regular wages for a job" – **Hummel and Nickerson**.
3. "It is any formal and announced programme under which the income of an individual, a small group, a plant work force or all the employees of a firm are partially or wholly related to some measure of productivity output" – **Scott.**

Need for incentive

It is true that monetary compensation does constitute very important reason for the working of an employee. But this compensation alone cannot bring job satisfaction to the workers. One cannot expect effective performance from a worker who is dissatisfied with its job, even if he is well paid. Sociologists and industrial psychologists also view that the financial aspect is not the only dominant motivating force. Confidence in the management, pride in the job and in firm and concern for the overall good cannot be brought by a bonus. Hence the modern authorities on management science have recognized the need for the provision of incentives to build up good morale.

Incentives for work

Incentives can take any form. According to Z. Clark Dickinson the important incentives for work can be listed as follows:
1. Desire for livelihood and fear of want.
2. Desire for approval of master and fear of punishment.
3. Desire for praise and fear of being dismissed.
4. Impulse to activity or joy in work and dislike of inactivity.
5. The moral command and fear of conscience.

Robert E. Salton has mentioned the following nine factors as the Motives for work.
1. Doing something worthwhile (Good).
2. Trust in leadership.
3. Doing my share (Participation)
4. I count for something (Recognition).
5. A decent living (Fair Wages).
6. A chance to get somewhere (Opportunity).
7. A safe future (Security).
8. Know what's going on (Communication).
9. Conditions at work (Environment)

Classification of incentives

All forms of incentives can be broadly classified into two kinds namely,

(i) Financial Incentives, and (ii) Non-financial Incentives.

These incentives can be further sub-divided into various kinds. These kinds can be explained with the help of the figure below:

Dr. Pallabi Mund, Assistant Professor (HR)

Types of Incentives

Financial or Pecuniary Incentives

1. Wages
2. Salary
3. Premium
4. Bonus

Non-financial Incentives

1. Job Security
2. Recognition
3. Participation
4. Pride in Job
5. Delegation of Responsibility
6. Quick Promotion
7. Facilities for Development
8. Labour Welfare Amenities

Now we shall briefly discuss the various kinds of incentives.

1. Financial Incentives

Financial incentives or pecuniary incentives are the most original of all the incentives. It is given in the form of money. The financial incentives still form the most important influencing and motivating factor up to a certain limit. Because it is only by virtue of the monetary compensation that the workers can satisfy their fundamental needs such as food, clothing, shelter etc. The financial incentives may be either direct or indirect. Direct incentives include wages, bonus and other incentives directly given to the workers in the form of cash. Indirect financial incentives include subsistence allowance expenses, medical expenses etc.

2. Non-financial Incentives

Non-financial or non-pecuniary incentives include all other influences planned or unplanned, which stimulate exertion. Mere monetary incentive cannot help the management in solving all the problems of industrial unrest. Further additional cash wage may also tempt the workers to misuse the money in vices like gambling, drinking etc. Under such circumstances, the non-financial incentives have a significant role to play. Such incentives create a healthy atmosphere and change the mental outlook of the workers. They make the working class more stabilized and economically sound. Thus, in short, the workers by virtue of the non-financial incentives are enabled to enjoy a richer and fuller life. Experiences of foreign countries particularly countries like Britain, America and Japan have shown that there is a high degree of positive correlation between non-financial benefit schemes and labour productivity.

Examples of Non-Financial Incentives

Non-Financial Incentives can take a variety of forms. Some of the popular ones are given below:

1. Job Security: The management must try its best to create a sense of job security. There should be no risk of retrenchment, demotion and termination. Experiences have also shown that the productivity is less in those concerns where workers have no feeling of safe and secure. But it is high in those concerns where they have a feeling of job security.

2. Recognition: Recognition of work is the essence of securing good work. Efficient people would naturally like to get recognition for their skill and excellence in their work. Such recognition can do many things that what a cash reward can do. Of course it is not practicable for the superiors to praise everybody for everything done by them. But the technique of praise must be practiced as far as possible.

3. Participation: Workers feel more satisfied when they are given an opportunity to raise their voice in handling the affairs of the enterprise. Since they actually take part in the decision-making their co-operation is assured.

4. Sincere Interest in Subordinates as Individual Persons: The workers must be made to feel pride in their job. Various techniques can be employed to develop pride to work. Food products, dynamic leadership, fair treatment, ethical conduct etc. can effectively stimulate the workers" pride in their job and in the firm.

5. Pride in job: The workers must be made to feel pride in their job. Various techniques can be employed to develop pride to work. Food products, dynamic leadership, fair treatment, ethical conduct etc. can effectively stimulate the workers pride in their job and in the firm.

6. Delegation of Responsibility: Delegation of rights and responsibilities to execute a given task often proves to be a strong motivating factor. By delegation the superior trusts his workers and stimulates them to show better results.

7. Other Incentives: Other incentives like quick promotion, provisions of facilities for development and training, provision of labour welfare amenities etc. also have a significant role to play in motivating the employees.

<u>Merits of Incentives</u>

The following are the advantages derived by providing incentives to employees:

1. **Higher output:** By providing incentives to his employees, the employer is able to induce them to work better. This leads to higher output.

2. **Greater profits:** Needless to say, higher output results in greater profits for the business. This happens in two ways. First, the cost per unit becomes less and second, the enterprise is able to keep the selling price low and this result in greater sales.

3. **No problem of idle time:** In an organisation where no proper incentives are available for the workers, the tendency will be to while away the time. When suitable incentives are available, the workers become time conscious. They begin to see every minute in terms of money.

4. **Supervision does not pose any problem**: When suitable incentives are available, the workers become duty conscious. The need for close supervision, thus, does not arise.

5. **Efficient workers are able to earn more:** Such of those workers who are highly efficient are able to earn more by way of performance bonus, higher commission and so on.

6. **Possible to identify inefficient and dull workers:** If, in spite of the incentive schemes, some workers are able to earn only their normal wage, it should mean that they are basically dull. The employer, therefore, has to decide whether to retain them or subject them to rigorous training.

7. **Rate of labour turnover is bound to be low:**If adequate incentives are available to the workers, they may not have a feeling of dissatisfaction. Such workers are sure to have greater work commitment and therefore may not leave the organisation. The rate of labour turnover, as a result, is bound to be low.

*8***. Reduction in complaints and grievances:**As the organization makes available suitable incentives to the workers, they may not have anything to complain about. This leads to reduction in complaints and grievances.

Problems arising out of incentives

The following problems are bound to arise while implementing an incentive plan:

1. Quality of work may suffer: The workers, those in the production department in particular, may give undue importance to the quantity of output produced neglecting the quality of output. Such a problem can be overcome only if the organization has a perfect system of quality control.

2. Inter-personnel relationships may suffer: Only those employees who are really efficient will be benefited out of incentives. This may promote ill-feelings among the employees of an organization.

3. Wear and tear of machines may be more: As the employees are keen on increasing the output all the time, they may handle the machines carelessly. This increases the wear and tear of machines.

4. Health of the workers may get affected: Some workers tend to overwork in order to earn more and this may affect their health.

5. Increase in accidents: There is always a preference to step up output disregarding even safety regulations and this may increase the rate of accidents in the workplace.

6. Increase in paper work: Proper administration of any incentive scheme involves lot of paper work. It necessitates the maintenance of proper records and books.

4.2.8 Requirements of a sound incentive plan

A good incentive plan shall fulfill the following requirements:

1. Trust and confidence – The success of any incentive plan depends on the existence of an atmosphere of trust and confidence between the workers and the management. In the absence of such an atmosphere, the workers may resist any such proposal by the management.

2. Consensus required – The management should not take a unilateral decision while evolving an incentive scheme. Consensus between the workers and the management is necessary for the success of the plan.

3. Assured minimum wage – Payment to any worker should not be totally related to his performance. Every worker should be assured of a minimum wave notwithstanding performance. Only then the workers would have a sense of security.

4. No scope for bias or favoritism- The standards set under the incentive plan should be based on objective analysis. It should not expect too much out of the employee nor should it give scope for bias or favoritism.

5. Simple to operate - The incentive plan should not involve tedious calculations. It should be so simple that the worker will be in a position to work out his total earnings himself.

6. Beneficial to both the workers and the management - The incentive plan should be beneficial to both the workers and the management. From the management's point of view, it should be cost effective. From the workers' point of view, it should offer return, at a rate higher than the normal rate of wages, for the extra efforts made by them.

7. Sound system of evaluation - A perfect system of evaluating the employees performance should be created in the organisation. The results of evaluation should be made known to the employees at the earliest.

8. Redressing grievances - Grievances and complaints are bound to arise whenever any incentive plan is in vogue in the organisation. Proper machinery should be installed for the quick handling of all such complaints.

9. Review - The progress of the incentive scheme should be periodically reviewed. Only then it would be possible to notice and remove defects, if any, in the plan.

Categories of Incentive Plans

Incentive Plans are two types. These are

1) Individual Incentive Plans
2) Group Incentive Plans

Individual Incentive Plans also two types. These are:

(i) Time- based Plans

1. Hasley's Plan
2. Rowan's Plan
3. Emerson's Plan
4. Bedeaux's Plan

(ii) Output-based Plans

1. Taylor's Differential Piece Rate Plan
2. Merrick's Multiple Piece Rate Plan
3. Gnatt's Task Plan

❖ **Time-based Individual Incentive Plans**

1. Halsey's Plan

F.A.Halsey, an American engineer, introduced this plan. Under this plan, standard time is determined for each job. A worker who completes the job by taking the standard time or even exceeding it is paid normal wages calculated at the time rate. In case, he completes the job in less than the standard time, he is given bonus equal to 50% of the money value of the time saved.

The bonus payable to the worker and his total earnings, under the Halsey's plan, are calculated as follows:

Bonus = 50% (Time Saved x Time Rate)

Total Earnings = Time Rate x Time Taken + Bonus

Merits of Halsey's Plan

The following are the plus points of Halsey's plan:

1. It is simple to understand.
2 The workers are assured of a minimum wage.
3. The employer and the worker share equally the benefit resulting from savings in time.
4. The plan encourages workers to be more efficient in their work.

Demerits

Halsey's plan, however, suffers from the following limitations:

1. The efficiency of the worker is rewarded to the extent of50% only.
2. The time saved is wholly due to the efficiency of the worker but the management grabs 50% of the resulting benefit.
3. The plan does not say anything about, the quality of the work done.

2. Rowan's Plan

Under Rowan's plan, the manner of calculating bonus is slightly different from that under the Halsey's plan. Bonus, under Rowan's plan is calculated as follows:

Bonus = % of Time saved x Time Wage
Standard Time
Total Earnings of the worker = Time Wage + Bonus

Merits

The following are the positive aspects of Rowan's plan:

1. Minimum wage is guaranteed to all workers.
2. When compared with Halsey's plan, bonus under Rowan's plan is more although the basic time wage is the same under both the plans.
3. The plan provides a check against over-speeding by workers. As the worker saves more time, his bonus and total earnings only begin to decline. In the above illustration, suppose, the worker completes his task within one hour, i.e. he saves 4 hours, his bonus will only be Rs.16. He earns the same bonus of Rs.16 by completing the task in 4 hours, saving just one hour.

Demerits

The drawbacks of Rowan's plan are given below:

1. It is not as easy as Halsey's plan is.
2. The earnings of the worker become less as he saves more time. This discourages efficient workers.

3. Emerson's Efficiency Plan

Under Emerson's plan too minimum wage is guaranteed to all workers. Payment of bonus, however, is related to the efficiency of the workers. Efficiency is determined by the ratio of time taken to standard time. Usually, a worker is given bonus only when his level of efficiency, in terms of percentage, is above 66.67%.

Merits

The following are the advantages of Emerson's efficiency plan:

1. Minimum wage is guaranteed.
2. It pays bonus to workers based on their level of efficiency.
3. The 66.67% or two-third efficiency criterion is within the reach of many workers.

Demerits

The disadvantages of the plan are as follows:

1. It is not a straight-forward approach to determining bonus.
2. If the standard time allowed itself is low, it may not be possible for many workers to fulfill the efficiency criterion laid down under the plan. .

4. Bedeaux's Plan

Under this plan, the standard time and time taken for each job is reduced to minutes, and each minute is referred to as "B", i.e., one hour is the same as 60 B's. The bonus and total earnings of the worker, under the plan, are calculated as follows:

Bonus = 75% (Standard Time - Time Taken) x Time Rate
Total Earnings = Time Wage + Bonus

Merits

The benefits of Bedeaux's plan are:

1. It guarantees minimum wages to the workers.
2. It enables efficient workers to earn more.
3. The benefit of three-fourth of the time saved is given to the worker.

Demerits

The weaknesses of the plan may be stated as follows:

1. The unit name of 'B' in place of the 'minute' does not make the plan altogether different.
2. The entire benefit of time saved by the worker is not passed on to him.

- **Output-based individual incentive plans**

1. Taylor's Differential Piece Rate Plan

F. W.Taylor, who is known as the *Father of Scientific Management*, developed the differential piece rate plan. Under the plan, two piece rates are laid down –

(i) A lower rate for those workers who are not able to attain the standard output within the standard time; and

(ii) A higher rate for those who are in a position to produce the standard output within or less than the standard time.

Under the plan, minimum daily wage is not guaranteed.

Taylor's differential piece rate plan has the following components:

(i) Standard Output.

(ii) Standard Time

(iii) A Lower Piece Rate and

(iv) A higher Piece Rate

Merits

The following are the merits of Taylor's differential piece rate plan:

l. It is easy to understand and simple to operate.
2. It enables efficient workers to earn more.
3. Workers not reaching the standard are paid at a lower rate. Such people, thus, are punished for their inefficiency. This protects the interests of the organisation.

Demerits

The limitations of Taylor's plan are given below:

l. It does not guarantee minimum wage. This creates a sense of insecurity for the workers. .
2. There may be ill-feelings among workers in view of the differential piece rates.
3. The quality of the output is ignored.

2. Merrick's Multiple Piece Rate Plan

Under this plan too a standard task is set for the workers. But unlike Taylor's plan that provides for two differential rates, Merrick's plan contemplates three rates as shown below:
(i) Workers producing less than 83% of the standard output are paid at a basic rate.
(ii) Workers producing between 83 % and 100% of the standard output will be paid 110% of the basic piece rate.
(iii) Those producing more than the standard output will be paid at 120% of the basic piece rate.

Merits
The merits of the plan may u~ stated as follows:
1. It is an improvement over Taylor's plan.
2. It has greater flexibility.
3. It offers greater scope for efficient workers to earn more.

Demerits
The following are, probably, the drawbacks of the plan:
1. It is a complicated plan.
2. Even a worker achieving 83% target is branded as a poor performer.

3. Gantt's Task Plan
This plan guarantees minimum daily wage. Its special feature is that it combines time rate, piece rate and bonus. A worker who is unable to produce the standard output receives only the time wage. He becomes eligible for bonus only when he attains or exceeds the standard output within the standard time. The rate of bonus varies between 20% to 50% of his wages.

Merits
The plus points of Gantt's task plan are:
1. It has, as mentioned above, time wage, piece rate and bonus. It is, therefore, a three-in-one scheme.
2 It guarantees daily minimum wage.
3. It provides enough opportunities for efficient workers to earn more.

Demerits
The weaknesses of the plan are:
1. It is not easy to understand.
2. The fluctuations in the output levels, of different workers not attaining the standard, are ignored and they all receive the same daily minimum wage. In the illustration given above, if two workers produce 6 units and 8 units respectively (against standard output of 10), each is assured a daily wage of Rs.50.

- ❖ **Group incentive plans**

1. Profit sharing
Profit sharing is the most popular method rewarding the employees. Under it, the employees are paid in addition to the regular wage, a particular share of the net profits of the business as incentive.

Characteristics of Profit Sharing

The key features of profit sharing may be stated as follows:

1. It is based on an agreement between the employer and the employees.
2. It is a payment made after ascertaining the net profits of the business. It is not therefore, a charge on profits.
3. The amount paid to the employees is over and above their normal pay.
4. The amount to the paid is determined based on some agreed formulas.
5. The payments based on seniority and wage level of individual workers.

Merits of Profit Sharing

The advantages are profit sharing are as follows:

1. Better employer-employee relations - This is possible, as the employer is ready to share the profits of the enterprise with his employees.

2. Increase in productivity -The employees make every possible effort to increase productivity because they know very well that higher profits for the enterprise would mean higher bonus for them.

3. Better living standards - It helps to increase the living standards of the employees as the amount received is in addition to the usual wages.

4. Reduced costs of supervision - The workers themselves are duty conscious and, therefore, they need no close supervision. Thus, costs of supervision are reduced.

5. Promotion of team spirit - The employees know the importance of Teamwork, as only such an effort would result in higher output.

Limitations of Profit Sharing

The limitations of profit sharing are as follows:

1. Regular income not assured: Payment to workers, by way of profit sharing, at a particular rate depends upon the profits of the enterprise. If the enterprise makes low profits or incurs losses, it will not be in a position to pay bonus as agreed.

2. Suppression of profits: Attempts may also be made to suppress true profits so that the employees need not be paid their share. This is done by manipulating accounts.

3. No inducement: Payment under the profit sharing scheme will be made to the employees once or twice a year when accounts are closed. Such, payments at longer intervals may not really motivate employees. Daily or weekly incentive payments are far more superior to profit sharing.

4. All workers paid alike: Payment to workers under profit sharing is made without considering their relative level of efficiency. This amounts to doing injustice to those who have really made target attainment possible.

<u>JOB EVALUATION:</u>

Job evaluation is a process whereby all jobs are looked at against various criteria to give an objective assessment of the job 'size'. There are various job evaluation schemes around that use different criteria and different scoring methods. After looking at a number of different schemes, the County Council decided to use the Hay scheme for its senior managers and the National Job Evaluation scheme for other employees.

The purpose of job evaluation is to ensure that all employees are paid based on an objective and consistent assessment of the size of their job.

Evolution and Definition of Job Evaluation:

First attempts of Job Evaluation were made in 1871 by US Civil Services Commission (Patton, Little Field and Self, 1964). With the advent of scientific management and industrial engineering, it is widely used till today, for purposes of determining differentials in remuneration, particularly for manual jobs and related activities.

Job Evaluation is "A generic term covering methods of determining relative worth (equity) of jobs."**--British Standard Institution (1969)**

Features of Job Evaluation

- Job Evaluation is a systematic method for determining the relative worth of a job in comparison within and outside the organization.
- In job evaluation, various jobs are rated to determine their position in job hierarchy.
- Job Evaluation process provides a base compensation for the job.
- It helps to eliminate wage inequities and to establish a basis for sound salary and wage structure.
- Once basic pay is determined, rewards, incentives and benefits are also determined.

Contents of Job Evaluation:

- **Job Analysis:** The process of examining the content of a job, breaking it down into tasks, functions, processes, operations and elements.
- **Job Description:** Description of a job based on job analysis.
- **Job Specification:** The statement of the content of the job based on job description and job grading.
- **Job Grading:** Ranking of jobs as a result of job analysis.
- **Job Classification**: Grouping of jobs according to their worth.
- **Job Assessment/Job Pricing**: The ascription of a monetary value on the basis of job grading.

Objectives Of Job Evaluation:

- Determines place & position of a job (Ranks Job)
- Clarify responsibility & authority.
- Avoid any discrimination against wage administration.
- To ensure employee satisfaction for compensation
- To determine qualities (Job Specification) for new jobs for employee selection
- To determine criteria for merit rating and promotions
- To provide basis for classification of new or changed jobs.
- To manage internal (different jobs in organization) & external (according to market rate) consistency in compensation

- To maintain accurate data.

Process of Job Evaluation:

Preliminary Steps taken before going for Job Evaluation:

- Getting acceptance from employees and trade unions
- Creating a Job Evaluation Committee

Step 1: Identification of jobs to be evaluated:

Step 2: Determination of the factors to be evaluated like:

- Physical efforts
- Mental Efforts
- Concentration
- Communication
- Leadership skills
- Education and Experience
- Job complexity
- Job pressure

Step 3: Gathering relevant information about the jobs:

Evaluators may adopt data collection techniques like interviews, questionnaires and observation methods besides Job description statements.

Step 4: Classifying Jobs and determination of Job Ranking:

After analysing all the information related to the jobs, the evaluators assess the presence of the chosen factors in the jobs. Then the evaluator determines the rating for each job.

Step 5: Selection of Benchmark jobs:

The primary purpose of JE is the development of pay grades for each category of jobs. In this regard, it is necessary for an organization to know what the other organizations are paying for similar jobs as a comparison. However, it may not be feasible for an organization to ascertain the comparative pay scale of all jobs in the organization.

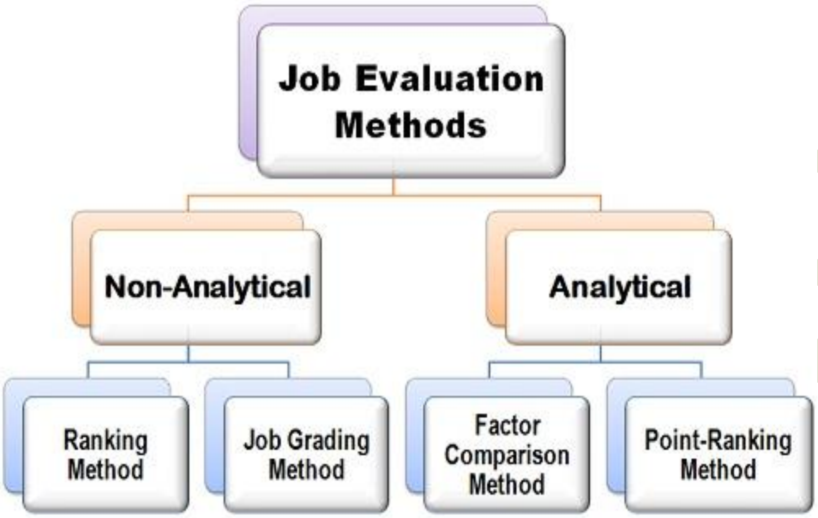
Step 6: Wage and Salary surveys:

In this stage, an organization conducts a survey of pay scales of the benchmark jobs in other organizations in the industry. Salary surveys may be conducted by an organization in a formal or informal way. Similarly, an organization may either conduct a direct survey to gather relevant information or use the published reports or professional agencies or magazines.

Step 7: Periodic review and feedback:

Any development in the external environment influences the organization continuously and also causes changes in the internal factor. For instance, technological changes influence the job characteristics and requirements profoundly. Consequently organizations are forced to review the jobs at periodic intervals to determine the worth in the changed context.

Methods of Job Evaluation:



1. Ranking Method:

This is the simplest and an inexpensive job evaluation method, wherein the jobs are ranked from the highest to the lowest on the basis of their importance in the organization.In this method, the overall job is compared with the other set of jobs and then is given a rank on the basis of its content and complexity in performing it.Jobs are also arranged according to the relative difficulty in performing them. It is a non-quantifiable and subjective method. It shows typical hierarchies in a company as jobs are ranked in the order of duties and power. This is often seen in smaller companies with fewer than 40 employees. The top of the hierarchy is considered the most important level; the person who sits at the top has the most authority and value of tat job is the highest. As we go down in the ranking method, duties become less specialized and jobs considered less valuable or expendable. Salaries are typically generated in order of job importance to the company.

Rank	Monthly salaries
1. Accountant	10000
2. Accounts clerk	7000
3. Purchase assistant	5000
4. Machine operator	4500
5. Typist	3500
6. Office boy	3000

Advantages:

- Easy to understand
- Less expensive

Disadvantages:

- Subjective in nature
- May not work out in large organizations

2. Job Grading Method:

This method is also known as Job-Classification Method. Under this method the job grades or classes are predetermined and then each job is assigned to these classes and is evaluated accordingly. For example: “Class-I” would comprise of the managerial level people under which sub-classification is done on the basis of the job roles such as office manager, department managers, departmental supervisor, etc.

Classes/ Job Grades	Jobs Assigned
Class I	**Executives/Managers** (Office Manager, Deputy office Manager, office Superintendent, Departmental Supervisor
Class II	**Skilled Workers** (Purchasing Assistant, Cashier)
Class III	**Semi-Skilled Workers** (Steno, Typist, Machine-operators, switch board operator)
Class IV	**Unskilled Workers** (Clerks, Office Boys)

Advantage	Disadvantage
1. Simple and easy to understand.	1. The jobs may differ with respect to their content and complexity. Some jobs may also appear to fit within more than one category/job grade.
2. The entire job is compared against the other jobs and is not broken into factors.	2. Placing all the jobs under one category may result in overestimation or underestimation.
3. The grade/category structure exists independent of the jobs, therefore mew jobs can be classified more easily than the Ranking method.	3. The standard used for comparison (grade/category) may have built-in biases that would affect certain groups of employees (females or minorities).

3. Factor Comparison Method:

In the ranking method we rank the jobs on the basis of their merit in the organisation. But in factor comparison method, instead of ranking complete jobs, each job is ranked according to the factors. Example of factors in a job = mental effort, physical effort, skill required, responsibility, supervisory responsibility, working condition, problem solving. The advantage of this method is that it is consistent and less subjective, thus, appreciable by all. Disadvantage: It is the most complex and an expensive method.

Steps:

1. Select the key jobs
2. Find the factors in terms of which the jobs are evaluated
3. Rank the selected jobs under each factor
4. Assign money value to each factor and determine the wage rate.

FACTORS/ KEYJOBS	Daily Wage rate	Physical Effort	Mental Effort	Skill	Respons-ibility	Working Condition
Electrician	60	11 (3)	14 (1)	15 (1)	12 (1)	8 (2)
Fitter	50	14 (1)	10 (2)	9 (2)	8 (2)	9 (1)
Welder	40	12 (2)	7 (3)	8 (3)	7 (3)	6 (3)
Cleaner	30	9 (4)	6 (4)	4 (5)	6 (4)	5 (4)
Labourer	25	8 (5)	4 (5)	6 (4)	3 (5)	4 (5)

4. Point Ranking Method

This method uses a point scheme based on the compensable job factors of skill, effort, responsibility and working conditions. In this method, each job's key factor is identified and then the sub factors are determined. These sub-factors are then assigned the points by its importance. For example, the key factor to perform a job is skills, and then it can be further classified into sub-factors such as training required, communication skills, social skills, persuasion skills, etc. The more compensable factors a job possesses, the more points are assigned to it. Jobs with higher accumulated points are considered more valuable to the organization.

❖ **Process of Point Ranking Method:**

1) Select the key jobs
2) Identify the factors of all identified jobs such as skill, effort, responsibility, etc.
3) Divide each major factor into a number of sub-factors. Each sub factor is defined and expressed in order of importance and is assigned points.
4) Find the maximum number of points assigned to each job.
5) Once the worth of a job in terms of total points is known, the points are covered into money values, keeping the wage rates in mind.

<u>Difference between Point Ranking Method and Factor Comparison Method</u>

Point ranking method is like factor comparison method.Here the factors of the job prioritise according to its importance. Then points are summed up to determine the wage rate for the job.The only difference between factors comparison and point method is, in first one, the factors are ranked and in the second one the factors are being allocated points.

MAJOR FACTORS	SUB-FACTORS
SKILL	**Education** and training required, experience, social skills required, problem-solving, use of judgement, creative thinking, etc
REPONSIBILITIES/ ACCOUNTABILITIES	Breadth of responsibility, composite of work, degree of freedom, accountability of product, etc.
EFFORT	Mental demands of a job, physical demands of a job, stress, etc.

Degree	Defines
1	Able to carry out simple calculation, **High School educated.**
2	Does all the clerical operations, computer literate, **Graduate**
3	Handle mail, develop contacts, takes initiative and does work independently **Post Graduate.**
4	Handling team, **Post Graduate, Higher Degree**
5	Taking part in strategic decision making, **post graduate, specialised course**

Factors	Point values for degrees					Total
	1(HS)	2(GR)	3(PG)	4(HG)	5(HG+SC)	
Skill	10	20	30	40	50	150
Physical effort	8	16	24	32	40	120
Mental effort	5	10	15	20	25	75
Responsibility	7	14	21	28	35	105
Work. cond.	6	12	18	24	30	90
Maximum total points of all factors depending on their importance to job =						540

Point range	Daily wage/salary rate	Job grade by key bank officials
500 - 600	300-400	1. Officer
600-700	400-500	2. Accountant
700-800	500-600	3. Manager I scale
800-900	600-700	4. Manager II scale
900-1000	700-800	5. Manager III scale

Advantage	Disadvantage
It is less subjective and is error free as the rater sees the job from all the perspectives.	It is a complex method and is time-consuming since the points and wage scale has to be decided for each factor and the sub factors.

<u>Merit Based Pay:</u>
Merit based pay is also known as Pay for Performance. This type of pay rewards the higher performing employees with additional pay or incentive pay. It is defined as a raise in pay based on a set of criteria set by the employer. This usually involves the employer conducting a review meeting with the employee to discuss the employee's work performance during a certain time period.

Importance of Merit Based Pay:

- It sends a powerful message about what you want to see from employee performance and contribution.
- It is used to recognize and reward employee efforts and contributions and confirms what you most value from employees.
- It reinforces the actions and behaviours of employees when the merit pay range is made public and the employee is allowed to see where his/her performance increase falls in the range defined already by the employer.
- During the review meeting, when employees hold conversations with their respective supervisors, they learn a lot about their actions and contributions most valued.
- It also helps those low performers too in understanding where they are lagging behind and identify the areas wherein more actions and contributions is required.

Advantages:

- Merit pay helps an employer differentiate between the performance of high and low performing employees and reward the performance of the higher performers.

- Merit pay, unlike profit sharing or similar bonus pay schemes, allows an employer to differentiate between the performance of the company as a whole and the performance and contributions of an individual.

- While many merit pay programs also provide an overall reward that is distributed to all employees, to promote such values as teamwork, co-worker positive relationships, and effective customer service, a portion of the available compensation is reserved for their strongest performers.
- Merit pay also provides a vehicle for an employer to recognize individual performance on a one-time basis. This is useful for rewarding employees who may have participated in a one-time project such as implementing a new HRIS or opening up a new sales territory.

Disadvantages:

- Problem in the basis of measurement of employees eligible for merit pay: The most desirable accomplishments and contributions are almost never measurable so the manager's or supervisor's opinion remains a constant in determining merit pay. If you use only items that you can measure, you're not considering the most important aspects of your employees' jobs.
- Large scale investment: The amount of time and energy that organizations invest in an attempt to make performance measurable for merit pay, including developing competencies, measurements, baselines for performance, and so forth, is better spent on delivering service for customers. Organizations have generated documents with several hundred pages that lay out what merit means in various jobs.
- Inability to communicate: Another challenge of merit pay is the ability of the supervisor to communicate to each employee the value of his or her contribution, and what superior performance entails that makes it worthy of merit pay consideration. Some supervisors communicate better than others.
- Also communication about what entails superior performance is easier in some jobs than in others.
- In spite of the limitations that exist in the awarding of merit pay, it can still be the best opportunity to ensure that the outstanding performers remain with the company and continue to make their astonishing contributions.
- Training your managers and supervisors in how to document performance, how to communicate a pay increase, and in how to set clear expectations is the best place to start to create a fair merit pay system.

Wage Differentials

A wage differential refers to the difference in wages between people with similar skills within differing localities or industries. It can also refer to the difference in wages between employees who have dissimilar skills within the same industry. It is generally referred when discussing the given risk of a certain job. For example, if a certain line of work requires someone to work around hazardous chemicals, then that job may be due a higher wage when compared to other jobs in that industry that do not necessitate coming into contact with dangerous chemicals.

The importance of proper wage differential has been stressed by **Harry Ober in his book "Occupational Wage Differentials in Industry",** thus: "Occupational differentials in wage rates are generally recognized as vital to the existing system of wages. Not only do they make possible compensation in accordance with skill, effort, and working conditions, but they are necessary to ensure a sufficient supply of skilled and trained worker…....To the worker in a particular occupation, wage differentials mean additional income for more difficult/tiresome or more skilled performance. Differentials also indicate differences in craft or trade prestige."

Principles or Rationalism of a sound wage differential:

- Wages should be commensurate with work
- Equal wages should be paid for equal work
- It should provide a sufficient incentive for acquiring skill and improving productivity
- It should be sufficient enough to attract workers to jobs in industries in which there is a shortage of labour.

The committee on fair wages recommended that wage differentials should be established on the basis of certain considerations like:

- The degree of skill
- The strain of work
- The experience involved
- The training required
- The responsibility undertaken
- The mental and physical requirements
- The hazard attendant on the work
- The fatigue involved

Factors affecting nature and extent of wage differentials are:

- The conditions prevailing in the market
- The extent of unionisation
- The relative bargaining power of the employers and workers
- The rate of growth of productivity
- The extent of authoritarian regulations and the centralization of decision-making.

<u>Types of Wage Differentials:</u>

1. **Occupational Wage Differentials:** This implies differentials in pay for different occupations in an organisation that widely differ from one another in terms of skill requirement (skilled, semi-skilled and unskilled) and the extent of requirement and the extent of responsibility taken. Such differences in occupations induce people/workers to undertake more challenging jobs, encourage workers to develop their skills by way of education and training. Wage differentials in occupations are due to : differences in work in different industries/firms/localities; differences in personal capabilities, age, gender, etc.

2. **Inter-Firm Wage Differentials:** This implies differentials in pay for the same or similar jobs/ occupations between different firms of the same industry in the same labour market (in the same area). Factors that influence inter-firm wage rates are differences in technological advancement, financial capacity, availability of raw materials, transport facilities, etc

3. **Inter-Area/Regional Wage Differentials:** This implies differentials in pay for the workers working in the same occupation at different geographical regions. These differences are the result of working conditions prevalent in different regions of the country. For example- the Central Government employees serving in the remote and disturbed areas like the North Eastern States of India are paid additional remuneration in the form of the Remote Area Allowance. Sometimes, such wage differentials are used to attract people to serve in particular regions. Several other factors that result in such geographical/regional wage differentials are : differences in - cost of living, rate of capital formation, extent of unionization, the urban or rural character of the surroundings, etc.

4. **Inter-Industry Wage Differentials**: These differences in wages surface in case of workers working in the same occupation and the same area but in different industries. The industries paying higher wages have mostly been industries with a large number of skilled workers while those paying less have large proportion of semi-skilled or unskilled workers. These differences are the result of varying skill requirements, level of unionisation, nature of product market, ability to pay, the stage of development of an industry, etc.

5. **Gender Differentials:** Certain personal wage differences also arise because of the differences in the personal characteristics (sex) of workers working in the same unit and occupation. Though provision of 'equal pay for equal work' is certainly there, but it is still not the reality. Instances are there when woman worker is paid less than her male counterpart for doing the same job because of lack of organization among women employees, less mobility among them, their weak body constitution as compared to their male counterparts. The reports on Royal Commission on Labour (1931) and The Labour Investigation Committee (1944) had found considerable differences in the earnings of men and women on the same job on an extensive scale. But it has reduced to a considerable extent in the recent world today due to the various Government regulatory laws and enactments and change in outlook of the employers.

6. **Sector Differentials:** This implies differences in wage rates due to differences in sectors. For example, wage differentials between agricultural and industrial sectors. Factors influencing sector differentials are - nature of the workers group (organized and unorganized worker groups), level of economic development of a sector and overall economic development of the country as a whole. Agricultural labour in India belongs to the unorganized sector of the economy as organized effort is lacking among them whereas workers in the industrial sectors have their own unions to fight for them. Rural area workers are dominated by traditional outlook, lower literacy and widespread underemployment compared to urban workers who are more organized, and have a benefit of firm employer-employee relationship which is lacking in rural folks.

<u>Socio-Economic Objectives of Wage Policy:</u>

1. To eliminate malpractices in the payment of wages.
2. To set minimum wages for workers, whose bargaining position is weak due to the fact that they are either un-organised or inefficiently organised. In other words, to reduce wage differential between the organised and unorganised sectors.
3. To rationalise inter-occupational, inter-industrial and inter-regional wage differentials in such a way that disparities are reduced in a phased manner.

To ensure reduction of disparities of wages and salaries between the private sector and public sector in a phased manner.

5. To compensate workers for the raise in the cost of living in such a manner that in the process, the ratio of disparity between the highest paid and the lowest paid worker is reduced.
6. To provide for the promotion and growth of trade unions and collective bargaining.
7. To obtain the workers a just share in the fruits of economic development.
8. To avoid following a policy of high wages to such an extent that it results in substitution of capital for labour thereby reducing employment.
9. To prevent high profitability units with better capacity to pay a level of wages far in excess of the prevailing level of wages in other sectors.
10. To permit bilateral collective bargaining within national framework so that high wage islands are not created.

In order to achieve the above objectives under the national wage policy, the following regulations have been adopted by the government:
1. Prescribing minimum rates of wages: The Minimum Wages Act, 1948 was passed for this. The Act empowers the government to fix minimum rates of wages in respect of certain sweated and unorganised employments. It also provides for the review of these wages at intervals not exceeding 5 years.
2. Compulsory conciliation and arbitration: the Industrial Disputes Act 1947 was passed for this. It provides for the appointment of Industrial Tribunals and National Industrial Tribunals for settlement of industrial disputes including those relating to wages.
3. Wage boards: A wage board is a tripartite body with representatives of management and workers, presided over by a government nominated chairman who can act as an umpire in the event of disagreement among the parties.
Technically, a wage board can make only recommendations, since there is no legal sanction for it, but for all practical purposes, they are awards which if made unanimously, are considered binding upon employers.

MODULE - 4: INSTITUTIONAL MECHANISM

Fixation of wages is a recent phenomenon in India. There was no effective machinery until , World War II for settlement of disputes for fixation of wages. After independence of India, industrial relations become a major issue and there was a phenomenal increase in industrial dispute mostly over wages leading to substantial loss of production. Realizing that industrial peace is essential for progress on industrial as welt as economic front, the Central Government convened in 1947, a tripartite conference consisting of representatives of employers, labor and government. Government of India formulated industrial policy resolution in 1948 where the government has mentioned items which have bearing on Wages:

1) **Statutory fixation of minimum wages,**
2) **Promotion of fair wages.**

To achieve the 1st objective, the minimum wages act, 1948 was passed to lay down certain norms and procedures for determination and fixation of wages by central and state government. To achieve the 2"d objective government of India appointed in 1949, a tripartite committee on fair wages to determine the principles on which fair wages should be fixed.

The legal framework for the payment of wages/salaries is governed mainly by four legislations that include:

- The Payment of Wages Act, 1936
- The Minimum Wages Act, 1948

- The Payment of Bonus Act, 1965
- The Equal Remuneration Act, 1972

Wages and salary incomes in India and fixed through several institutions. **Those are explained as below:**

1. Unilateral pay fixation:

In India, 92% of the labour force is unorganized. Though a significant portion of the unorganized labour force is covered by the minimum wage legislation, given the high unemployment and underemployment, there are little incentives for employers to comply with the legislation (for every person who does not work below minimum wage there could be many more who are willing to work for less than the minimum wage) and many other practical difficulties in effective enforcement.

Majority of the unorganized sector workforce is not unionized and hence the possibility for determining wages and working conditions through collective bargaining is virtually ruled out. In few cases, collective bargaining in the unorganized and sick industries in the private sector has actually led to agreeing for less than the benefits and protection afforded by legislation. Due to all the above reasons, in respect of a vast majority of the workforce in the unorganized sector, wages are unilaterally determined.

This often results in not only workers getting less than the minimum wages and benefits stipulated under law, but also discrimination in wages and benefits between one (set of) workers with another. This type of wage fixation by employer can be unfair to the individual employees because the latter will have lesser bargaining power vis-à-vis their employers, often tend to encourage arbitrariness and raise questions about fairness and equity.

2. Collective Bargaining:

The word 'collective' means group and 'bargaining' means negotiation and therefore, it may be considered as a negotiation of a dispute between the labour union and the management. In simple words, it is a process whereby management and labour try to explore each others difficulties with the object of reaching an agreement regarding working conditions and terms of employment.

- **Prerequisites of Collective Bargaining:**

I. Both parties (employer and employees) should realize the need of collective bargaining.
II. Both parties should try to solve the problems through negotiations sincerely and honestly.
III. A single plant bargaining is considered better than a multiple plant bargaining. In single plant bargaining, there is a bargain between a single employer and single union.
IV. Both parties should present facts and figures on the discussion table. Their approach should be constructive in order to resolve the problems.
The management should pay reasonable wages and any unfair labour practice should be avoided.
V. If any agreement is reached, it must be a written document.
VI. Both parties should ensure that agreement reached is respected and implemented and industrial peace is established.
VII. There should be a provision for arbitration if there is any dispute regarding interpretation of agreement and its implementation.

Collective bargaining relates to those arrangements under which wages and conditions of employments are generally decided by agreements negotiated between the parties. Broadly speaking the following factors affect the wage determination by collective bargaining process:

- Alternate choices and demands,
- Institutional necessities,
- The right and capacity to strike.

a) In a modern democratic society wages are determined by collective bargaining in contrast to individual bargaining by working.

b) In the matter of wage bargaining, unions are primarily concerned with:

- General level of wages rates.
- Bonus, incentives and fringe benefits, Administration of wages.

❖ **<u>Collective bargaining takes place at the following levels:</u>**

(i) At Unit Level:

- Such a bargaining is limited to a particular unit or undertaking enterprise only.
- This is a decentralized approach to bargaining. Unit level means individual level bargaining.
- In companies like MNCs belonging to IT industry, where there are educated and well aware workforce, there are no unions in this type of industry. So whenever negotiation has to take place, it happens at individual level.

(ii) Plant Level bargaining:

- This type of bargaining takes place between an employer and a union.
- If there are multiple unions, the bargaining can take place between an employer and multiple unions.
- The basis of bargaining are the parameters set by a particular plant/company.

(iii) At the Industry Level:

- At this level, the bargaining generally takes place in a tripartite form involving the union/unions, employer and government officer/officers.
- The parameters for this kind of bargaining varies from industry to industry. For example, bargaining takes place in different forms in Jute/Textile industry than Steel industry.
- In India, collective bargaining of this type is very popular in textile industry where agreements are reached between labour unions and the various management bodies.

(iv) At Territorial / Geographical level:

- The employment provisions and say pension schemes made by state/ territorial government changes depending upon area.
- Companies set up in varies geographical locations cannot use same grounds or parameters for bargaining.

(V) At the National Level:

- At the national level the bargaining is mutual and agreements usually take the form of 'tripartite agreements' entered into between labour union and managements in the presence of the government representatives.
- The agreement entered into between Indian Tea Association, Indian Tea Planters Association and Hind Mazdoor Sabha (HMS) and INTUC is an **example** of collective bargaining at the national level.
- National level bargaining is **common in public sector** where wages, compensation and various other employees benefit schemes are decided at national level.
- If **we compare internationally, Norway is ranked highly** in collective Bargaining in national level bargaining.

3. Industrial Wage Boards

a) Concept of wage board was first enunciated by committee on fair wages.

b) It was commended by first five year plan and second five year plan also considered wage board as an acceptable machinery for setting wage disputes.

c) Wage boards in India are of two types:

- **Statutory Wage Board:** It means a body set up by law or with legal authority to establish minimum wages and other standards of employment which are then legally enforceable in particular trade or industry to which board's decision relate.
- **Tripartite Wage Board:** It means a voluntary negotiating body set up by discussions between organized employers, workers and government to regulate wages, working hours and related conditions of employment.

d) Wage board decisions are not final and are subjected to either executive or judicious review or reconsideration by other authority or tribunals.

e) The powers and procedure of wage boards are same as those industrial tribunals unsaturated under ID Act 1947.

4. Pay Commissions

The pay structure of the Central Government employees is based on the recommendations of Pay Commissions set up by the Central Government. While some State Governments also broadly follow the recommendations of the Central Pay Commissions for their employees, also a few other State Governments set up their own pay commissions. During the past 50 years, Govt. of India has set up six pay commissions. The recommendations of the 5th Pay Commission, which submitted its report in 1997, as accepted by the Government was in force for about 10 years until the 6th Pay commission was established in 2006.

a) First pay commission was appointed by Government of India in 1946 under chairmanship of justice Vardachariar to enquire in to conditions of service of central government employees.

b) The Vardachariar Commission in its report said that in no case should a man'spay less than living wage.

c) The 3rd pay commission was appointed in august 1957 and commission submits its report 'in 1959, examined the norms for fixing a need based minimum wage set up 15th session of ILC.

d) Government of India appointed third pay commissions in 1970s which submit its report in April 1973. In this report commission express its support for a system in which pay adjustments will occurs automatically upon an upward movement in consumer price index.

e) After thirteen years, government appointed fourth central pay commissions under chairmanship of justice P.N. Singhal on July 26, 1983 to examine structure of all central government employees, including those of union territories. Officers belong to all India service and armed forces. Commission submits its report on July 30, 1986 and recommended drastic changes in play scale.

f) The 5th pay commission (1952-1996) made certain recommendation regarding restricting of pay scales.

g) The 6th pay commission was established on 2006 and committee submitted its report on March 2008.

5. Adjudication by Courts and Tribunal:

Since independence adjudication has been one of the main instruments for settlement of disputes, improvement in wage scales and standardization of wages and allowances. Though courts and tribunals were primarily intended to deal with settlement of industrial disputes, in practice, wage fixation has become an important element in their work and functioning. This is because of large of disputes concerning of Wages and allowances. Numerous wage disputes in many industries have been referred for adjudication to labor courts and tribunals during past ten decades. The high courts and Supreme Court have also adjudicated upon such disputes. The awards given by these authorities not only helped in formulation of a body of principles governing wage fixation but laid foundation for present wage structure in many of major industries. Some major legislation which governs the principles of wage fixation — Minimum Wages Act 1948, Payment of Wages Act 1936, Equal Remuneration Act 1976, Industrial Disputes Act 1947, add Companies Act 1956.

SIGNIFICANT COMPENSATION ISSUES

As with other FIR activities, compensation management operates in a dynamic environment. **For example,** *as* managers strive to reward employees in a fair manner, they must consider controls over labor costs, legal issues regarding male and female wage payments, and internal pay equity concerns. Each of these concerns is highlight the following important compensation issues:

1) **Issue of Equal Pay for Comparable Worth:** Comparable worth is concerned with the fact that women receive less pay than men for jobs that may be different but are of comparable worth. **For example,** nurses make less than sanitation workers; however, it is argued that the job of nurse is worth more than the job of sanitation worker. This issue goes far beyond that of providing equal pay to men and women performing similar to equal jobs.

2) **Problem of Measuring Comparability:** If jobs should be paid according to their worth to the organization, there must be some means of measuring the relative worth of jobs. Unfortunately, compensation specialists have not agreed on a comparable worth standard by which to evaluate jobs. Furthermore, most agree that the traditional job evaluation techniques fall short of providing a needed standard. Congress and the courts have largely refused to deal with the comparable worth issue. This issue is a complex one, and few seem to know how to deal effectively with it.

3) **Issue of Low Salary Budgets:** Low salary budgets reflect a general trend toward tight compensation cost controls caused by global competition for jobs, the reduction in workforce because of technology, and the growing use of temporary and part-time employees who receive low wages and few benefits. Unfortunately, low wages could portend unfavorable effects for employers and society, including increased turnover as employees change jobs for higher wages and diminished employee output *as* employees perceive a low pay-for-performance relationship.

4) **Issue of Wage-Rate Compression:** Wage-rate compression occurs when the pay difference between successive wage grades narrows. This compression is frequently found between highly paid hourly employees and their immediate supervisors.

COMPENSATION AS RETENTION STRATEGY

Compensation can be critical in motivating employees. They are more likely to be motivated when they feel their contributions are being fairly and equitably rewarded. Compensation is a reward system. It reflects the employee's value to the firm and in turn impacts his or her sense of self.

An effective compensation plan helps the organisation attract, and retain, skilled employees. Compensation can also be used to encourage workers to learn new skills and to exhibit appropriate behavior. Employees who are rewarded for performing well will, in turn, provide good role models for others.

If, in an ideal organization, individual goals are aligned with organizational goals, then the organization will meet its goals when all the employees meet their goals. Rewarding employees (by providing equitable compensation) for meeting their own goals, therefore, brings the organization closer to achieving its overall goals.

Compensation constitutes the largest part of the employee retention process. The employees always have high expectations regarding their compensation packages. Compensation packages vary from industry-to industry. So, an attractive compensation package plays a critical role in retaining the employees.

Compensation packages should include the following components for employee retention:

1) **Salary and Monthly Wage:** It is the biggest component of the compensation;package. It is also the most common factor of comparison among employees. It includes:
   - Basic wage,
   - House rent allowance,
   - Dearness allowance, and
   - City compensatory allowance

   Salary and wages represent the level of skill and experience an individual has. Time to time increase in the salaries- and wages of employees is necessary. And this increase should be based on the employee's performance and his contribution to the organization.

2) **Bonus:** Bonuses are usually given to the employees at the end of the year or on a festival.

3) **Economic-Benefits:** Economic benefits include paid holidays, leave, travel concession, etc.

4) **Long-Term Incentives:** Long-term incentives include stock options or stock grants. These incentives help retain employees in the organization's start-up stage.

5) **Health Insurance:** Health insurance is of great benefit to the employees. It saves employees money as well *as* gives them a peace of mind that they have somebody to take care of them in bad times. It also shows the employees that the organization cares about the employee and their families.

6) **After Retirement:** It includes payments that employees get after their retirement like EPF (Employee Provident Fund), etc.

7) **Miscellaneous Compensation:** It may include employee assistance programs (like psychological counseling, legal assistance, etc.), discounts on company products, and use of company.

IMPACT OF COMPENSATION EMPLOYEE RETENTION

Compensation can have **a** direct impact on employee retention. While employers may use employee incentives and monetary rewards to retain employees, there are ways to complement compensation that have a much greater impact. Based on the type of compensation, along with the terms and conditions of an employee compensation package, an employer can boost employee retention.

Employees' looking voluntarily to make a change want to continue their career with a company that offers promotion and development opportunities, a collegial work environment and a leadership team that is openly appreciative of its human capital. Compensation and benefits may be important factors in the decision to look for employment elsewhere; however, many reports indicate compensation is low on the list of priorities in looking for another position. Employees have an intrinsic need for respect, motivation and challenging work, which are compelling reasons for seeking employment elsewhere. Employers who consider compensation as part of the strategy for employee retention are headed in the right direction, but are looking at just one half of the equation. Compensation coupled with better opportunities to develop employee skills is a more complete way of formulating an effective retention strategy.

One of the most effective ways compensation can have a positive impact on employee retention is to construct an employee development plan that promises employees career track opportunities with the company. Being on an upward career track should come with corresponding salary and merit increases. In addition, performance-based bonuses motivate employees in terms of aligning their individual goals with company goals. Implementing incentives such as stock options, profit sharing, and spot rewards are other ways compensation affects retention. These forms of compensation demonstrate how critical employee performance is to the organization's overall profitability. Spot rewards are usually not as lucrative; however, they provide immediate recognition, reward and compensation when company leadership observes an employee performing superior work. Appreciation is key to employee retention, and if compensation is a part of recognition, then compensation is likely to increase employee retention.

As with most strategic initiatives, retention strategy development starts with an assessment of the organization, including an assessment of the values, vision and principles that drive behavior in the organization. This should drive whom to hire, whom to keep and whom to reward. The people who share the organization's values are likely to be the right choice for the business in the long-run. By developing a retention strategy around the right employees, the organization will be much more effective in retaining its employees during any economic period. Implementing compensation and benefits programs that reward .the right behavior and performance will help attract the right people to the organization, and it will also help the best people become more productive. In addition to a retention strategy, a communications plan built on a strong foundation of trust enables effective implementation of the new retention and compensation strategies. A combination of an effective retention strategy has several components that must be addressed order to retain top employees.