

**THOMAS ECONOMETRICS**

**quantitative solutions  
for workplace issues**

**Are Your Employees Fairly  
Compensated? A 10 Point  
Inspection**

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## **Introduction**

The issue of fairness in the workplace is a dominant theme in today's employment environment. Employers and employees alike are concerned about equity in all areas of employment, from hiring decisions to promotion opportunities to compensation and benefits.

But now does an employer know whether its employees are being fairly compensated? Examining the compensation structure is best done through a comprehensive self audit. A compensation self audit is typically conducted under the auspices of legal counsel (corporate counsel and / or outside counsel). It is commonplace for legal counsel to retain the expert services of outside consultants to actually perform the self audit.

A self audit can be a lengthy – and potentially expensive – undertaking. The time and expense, however, is well spent, as it can minimize the organization's risk to compensation litigation down the road. As a first step in this process, an organization can begin by examining their compensation policies and practices using a "10-Point Inspection".

## **Are the Appropriate Compensation Structures in Place in the Appropriate Business Segments?**

The first task is to understand the compensation structures of the organization. Frequently, the compensation structures will vary within the organization by business lines, sectors, etc. For example, administrative and support staff may be paid an annual salary, while the sales team may receive commission earnings in addition to a base salary. Commissions may provide an extra motivation for the sales team, but will likely be

inappropriate for administrative staff. The idea here is to gain an understanding of how employees are paid, and whether the existing structures make sense for the different functions served by the different groups of employees.

## **Is the Compensation Policy Itself Transparent?**

Compensation decisions should be based on a set of consistent and well-articulated factors. It should be clear to anyone reviewing the policy what factors and metrics are used in the compensation decisions. If these factors and metrics cannot easily be identified, the policy itself should be revisited. Compensation decisions should be based on tangible, measurable criteria. Decisions should not be arbitrary or completely discretionary.

## **How Well is the Compensation Policy Communicated to Employees?**

An organization could have the perfect “best practice” compensation policy in the world, but employees don’t know – or don’t understand – the details of the policy, there is still an opportunity for feelings of unfairness. The compensation policy needs to be communicated to employees, and employees need to understand what is expected of them in order to achieve the next merit increase, bonus payment, etc.

## **Is the Organization's Compensation Package Competitive in the Marketplace?**

In order to attract and retain top talent, your organization's compensation package needs to be competitive with what other employers are offering in the marketplace. There are a variety of compensation and benefits surveys available that provide information on salary, bonuses and incentive pay, as well as other components of compensation. These surveys break out the information by industry, occupation, and geographic area. Examine where your compensation and benefits package stands with respect to your competitors, and consider making adjustments where necessary.

## **How Should We Group Employees For Compensation Comparisons?**

In order for the examination to generate meaningful insights, it is important that an employee's compensation is assessed against the appropriate comparison group. For example, it would be inappropriate to compare the compensation of the CEO of the organization with the compensation of the CEO's administrative assistant. The two individuals serve completely different purposes within the organization and have different levels of responsibility. Ideally, employees who have similar job functions, similar responsibility levels, and whose positions require similar skills and qualifications should be compared against one another.

## **Are Employees Compensated the Same, and If Not, Why Not?**

After deciding which employees to compare against one another, the differences in compensation amongst these employees can be examined. Two employees may serve the same function, have similar levels of responsibility, etc., and still be legitimately paid differently. These legitimate differences can be explained by “edge factors”. Examples of “edge factors” include total company seniority, time in job, education and certifications, and relevant prior experience. Differences in compensation are not necessarily indicative of “unfairness” if the differences can be explained by legitimate factors.

## **Do We Provide Compensation Extras Fairly?**

Employers are providing “compensation extras”, such as flexible schedules, telecommuting, and flex time, in efforts to help their employees manage work-life balance. These “extras” should be examined in this process to ensure that they are offered fairly and equitably to employees where appropriate.

## **Do We Set Initial Pay For New Hires Fairly?**

Fairness in initial pay setting can avoid many problems in the future. New hires with similar skills and qualifications hired for positions with similar functions and responsibility levels should be compensated similarly. Any disparities created by initial pay-setting can compound over time,

potentially leading to larger disparities in the future. A small differential in initial pay may seem innocuous, but can potentially develop into a large “fairness problem” years down the road.

## **Are We Maintaining the Appropriate Documentation Regarding Compensation Decisions?**

The old adage “an ounce of prevention is worth a pound of cure” applies when it comes to documentation of compensation decisions. It’s far easier to document the decisions on an ongoing basis than to discover at some later point this documentation is required and have to attempt to recreate it. If there special – but legitimate – circumstances governing a particular employee’s compensation (such as red-circling), these circumstances should be noted in the employee’s personnel file or other such tracking system.

## **What Improvements In Our Compensation Structure Should We Implement?**

The answers to the previous nine questions naturally lead to a better understanding of the compensation system as a whole. At the end of the day, the employer will have deeper insights into the areas of compensation in which the organization is doing well, and the areas that could be improved. A word of caution, however, is warranted – any proposed changes to the compensation structure should be carefully considered from all vantage points prior to implementation. Changes designed to remedy problems or enhance one area of compensation have the potential to

impact other areas of compensation. A thorough review of the proposed changes, and their reverberations throughout the compensation structure as a whole, should be undertaken before any modifications are instituted.

## **Conclusion**

It is important to keep in mind that this “10-Point Inspection” is not a replacement for a comprehensive self-evaluation of compensation. Rather, it is a tool for beginning a dialogue and identifying the information and data that will be necessary for modeling the compensation structure in the self audit. The “10-Point Inspection” is the first step on the path to a full assessment of the fairness of the organization’s compensation structure.