



TOPIC 2

Keeping qualified employees

The compensation of employees, including health and safety at work, has become one of the important issues in organisations. After the organisation has attracted and hired a certain calibre of employee, it is critical that the compensation and health management practices not hinder efforts to retain productive and talented employees.

TOPIC AIM

The aim of this topic is to familiarise you with the activities and complexities involved in managing compensation and benefits, including the health and safety of employees in the organisation.

LEARNING OUTCOMES FOR TOPIC 2

After completing this topic, you should be able to

- examine, compare and comment on compensation and benefits of employees (**Workbook 04**)
- discuss the influence of the health and safety of employees in the organisation (**Workbook 05**)

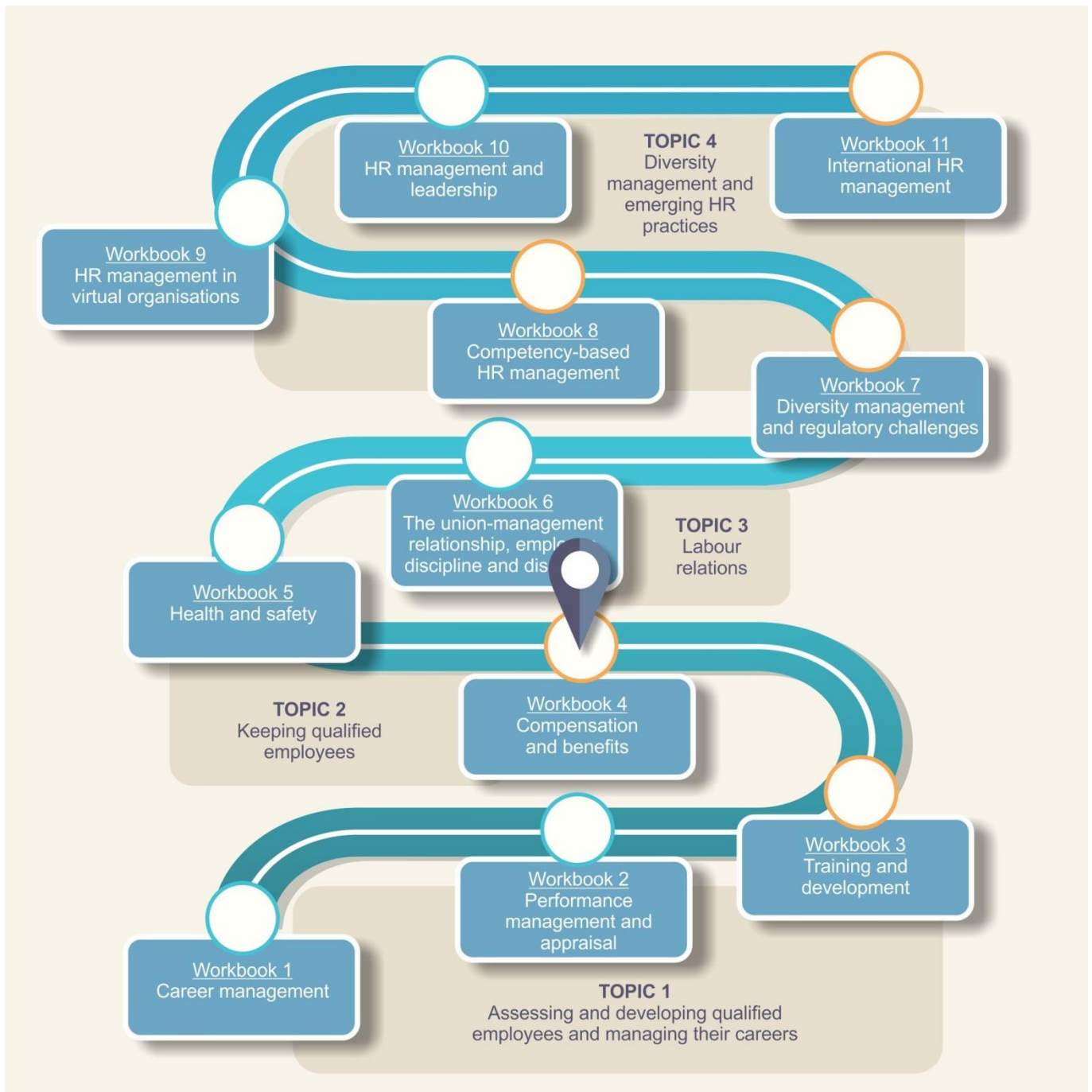
WORKBOOK 04

Compensation and benefits

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Have a look at the mind map to see where you are in the process of working through the study material.



4.1 LEARNING OUTCOMES



Read through the outcomes before you continue. This will give you an overall picture of what we will discuss in this workbook.

After studying this workbook, you should be able to

- explain the link between pay, motivation and performance
- define job evaluation and discuss four popular methods of performing it
- differentiate between three types of individual incentives
- discuss why gain-sharing or profit-sharing and employee stock ownership plans (ESOPs) have grown as organisational incentive plans

- discuss the different executive compensation methods
- explain the importance of employee benefits and their organisational objectives

4.2 KEY CONCEPTS



A number of key concepts are listed at the end of chapter 11 of your prescribed book. Please read through them before you continue. Then you will be familiar with the different concepts that we will refer to in this workbook.

Some of the important key concepts in this workbook are:

- Compensation
- Job evaluation
- Merit pay
- Piecework
- Gain-sharing plans
- Golden parachute contract
- Stock option plan
- Skill-based pay

4.3 INTRODUCTION

One of the most significant tasks confronting HR managers is the design and implementation of compensation systems. These systems are designed to serve many purposes, but the main goal is to provide fair and equitable remuneration for all employees. The HR manager therefore has to ensure that all employees feel that they are being paid what they are worth and that their salaries compare favourably with those of others doing similar work, inside and outside the organisation. In addition, the compensation programme must provide equity to the employees while allowing the organisation to remain competitive in the marketplace.

The key question therefore is:

How does the HR manager ensure that the organisation's compensation strategy benefits both the organisation and employees?

Compensation is what employees receive in exchange for their contribution to the organisation. The purpose of compensation is to attract, retain and motivate employees in order to achieve the employer's business objectives. The employer's compensation package should be good enough to attract competent employees from the marketplace. It must be reviewed in such a way and kept in line with accepted market norms so that it motivates employees to perform and remain with the company. Without adequate compensation, current employees are likely to leave and replacements will be difficult to recruit. Compensation, however, goes far beyond just wages and salaries. It may also include incentives that help relate labour costs to productivity. A wide range of benefits and services is almost always part of the total compensation package each employee receives. Taking all of this into account, you should now begin to realise what a complicated task the HR manager faces in determining the compensation and benefits applicable to the different positions in the organisation.



Activity 4.1: Future Leaders University

Read the case study at the end of chapter 11 in the prescribed book (Future Leaders University) and then answer these questions:

- a. Fiona has been working for Future Leaders University for 23 years. Identify and discuss the method the university can use to research her salary on the local labour market.
- b. Discuss communication as an important element in compensation.
- c. Do you think that money is the only motivator for Professor Clever to stay at the university? Give reasons for your answer.
- d. What is the goal of a compensation system?



It should be obvious to you that keeping employees happy in the work environment (especially when it comes to their money) is a very important issue to employees and needs to be attended to by management with the utmost care and attention. When answering the questions in activity 4.1, you should have noted the following:

- a. Future Leaders University can do a salary survey to conduct research into similar competitors' salaries (pay rates) for Fiona. A survey is the systematic process of collecting data on, in this case, compensation paid by other organisations to their employees. Future Leaders University can use surveys conducted by compensation consultancies.
- b. Communication in all aspects of HR is important, and especially in compensation. Employees need to understand the company's pay system. Their understanding is indirectly shaped through the pay they receive and directly through formal communication about their pay, their performance and the markets in which the organisation competes. Employees need to be advised of the company's pay policies and how these policies affect them individually. They therefore need information on issues such as how the performance appraisal and incentive system works, if there is a job rating system, how it works and how it affects them. Evidence suggests that the goodwill created by being open about pay may also affect the perception of pay equity. Employees in companies with open pay policies tend to express higher satisfaction with their pay and with the pay system.
- c. There is more to motivation (and keeping employees in an organisation) than just money. Different things motivate people in different ways under different circumstances, which makes it difficult to answer the question. For instance, a sabbatical may motivate Professor Clever to embark on professional development, whereas family responsibility time to attend to her special needs child may motivate Fiona. There are, however, certain principles which managers can apply to use money as a motivator. For money to motivate, it must be substantial enough to encourage the employee to perform and must also be directly related to work performance. Organisations use intrinsic and extrinsic rewards to compensate employees for their time and effort. Extrinsic rewards relate to being stimulated by external sources, such as salary and benefits. Intrinsic rewards have to do with being stimulated internally and performing because of the challenges, satisfaction and fulfilment when making a contribution.
- d. The compensation system is one of the most important HR tools. With its compensation system, a company aims to
 - attract employees with the required personalities, skills, competencies and values
 - retain good performers (in the case of Future Leaders University to keep valued employees such as Fiona)
 - encourage and reward employees who believe in the importance of quality
 - promote performance, productivity and outputs

It is obvious why employees would feel upset about their salary increases (or no increases). Obviously they view salary increases as important. Misunderstanding of salary increases (or no increases) is bound to occur in organisations if the policy on compensation, benefits and incentives is not communicated

properly or properly understood by all employees. The HR manager therefore plays a vital and difficult role in determining the policy of the organisation and ensuring that it is implemented correctly at all levels in the organisation. To enable you to better understand compensation systems and benefits, we will answer the following questions in this unit:

- What are the objectives of compensation?
- What role does job evaluation play in the compensation process?
- What types of pay systems can be found?
- Why have benefits become so important and what types of benefits exist?
- What is executive compensation and what does it entail?

4.4 COMPENSATION OBJECTIVES

You will agree that employees should be compensated in some way for the contributions they make in the company employing them. Once employees have been paid for their effort, a fair exchange has taken place between them and the organisation. This is one of the many objectives of compensation.



Study section 11.1 in chapter 11 of the prescribed book.



Activity 4.2

Read the introductory part to chapter 11 in the prescribed book, then study "Compensation objectives". Keeping the case study in activity 4.1 in mind, answer these questions:

- Which of the compensation objectives (summarised in figure 11.2) are applicable to Future Leaders University? Why?
- Identify and explain other compensation objectives in designing a compensation system.



Feedback

You should have realised by now that the primary objective of any compensation programme (as with all the other HR management functions that you know) is to utilise and manage human resources effectively in pursuing the organisation's wider objectives. This is why it is always important for the HR manager to ensure that compensation goals are formalised. This ensures that wage and benefit policies realise their goals. You should have referred to section 11.1 and table 11.1 (10 Cs to assess the effectiveness of pay and rewards) in chapter 11 of the prescribed book for the following additional goals of compensation:

- to reward contribution and performance
- to remain competitive in the labour market
- to maintain salary equity among employees
- to motivate employees to perform to the maximum of their capabilities
- to control wage and salary costs
- to attract and retain good staff
- to reduce unnecessary staff turnover
- to comply with government legislation
- to ensure internal and external equity

Competitive, equitable salaries will therefore ensure that good employees are attracted to the organisation, that these employees are motivated to improve their performance (because they know that their past performance will be rewarded) and that they remain with the organisation. Table 11.1 shows the criteria an organisation can select from to assess the effectiveness of its reward arrangements. It is, however, a difficult task to get to the point where the HR manager can say that the salaries offered by the organisation are competitive and equitable. How can this be achieved? This is where proper job evaluation comes in.

4.5 JOB EVALUATION

How do you determine how much to pay someone? Remember that employees not only differ in terms of their qualifications and experience, but they also have different types of jobs at different hierarchical levels. The HR manager therefore has to use another tool to determine what the employees' compensation should be.

Job evaluation is used by organisations to determine the value of jobs and therefore to determine the relativity of pay between jobs. Job evaluation implies that a job's worth can be measured and that employees in higher-level jobs will earn higher salaries than those in lower-level jobs.



Study section 11.2 in chapter 11 of the prescribed book.



Activity 4.3

Read the following paragraph and answer the questions:

Robert had been working for his twin brother Tshepo for 6 months. He then told Tshepo that he wanted a steady monthly salary, and he refused to continue working until Tshepo had indicated how much he would pay him. Tshepo then asked a few friends to help him out. Unfortunately they soon joined Robert in demanding compensation for their efforts. Tshepo suddenly realised that he had a serious problem. He had no idea what to pay his employees. And even worse, he didn't know how to determine their salaries! Should they all be paid the same salary or should people doing similar work be paid a similar salary? Was it really necessary to pay them steady salaries each month? Would it not be better to negotiate each month's salary with them after all expenses had been covered?

- How can job evaluation solve Tshepo's problems?
- Compare internal and external equity in considering Robert's salary.
- What job evaluation methods are most suited to Tshepo's business? Why?
- Explain whether Tshepo should use a job evaluation committee or outside assistance.
- Briefly summarise the advantages and disadvantages of the different job evaluation methods. Use a table similar to this one here as a framework.

JE method	Advantages	Disadvantages
Job ranking	<ul style="list-style-type: none"> Fast and easy to complete 	<ul style="list-style-type: none">
Job classification		
Point		
Factor comparison		



Feedback

Our discussion clearly shows the importance of proper job evaluation when determining compensation. During job evaluation, jobs are analysed and assessed to determine (in a reliable way) what they are worth to the company. This assessment then forms the basis of a balanced **pay structure**. Internal equity (fair comparison of pay with other jobs within the organisation) and external equity (fair comparison of what an employee would earn doing a similar job in other organisations) help to recruit productive employees and maintain internal perceptions of pay equity in the organisation. Note that the most popular job evaluation methods found in South Africa include job ranking, the factor comparison method, the classification method and the point method (see table 11.2 in section 11.2 of chapter 11 of the prescribed book). You could also have referred to table 11.3 in section 11.2.1 of chapter 11 of the prescribed book to discuss the advantages and disadvantages of different job evaluation methods.

There is also no absolute means of measuring the value of work and this value is relative when determining compensation. Job evaluation therefore fills a significant assessment gap. For the job evaluation process to be successful, there must be total commitment from management and complete agreement from the trade unions, staff committees and other consultative bodies. All interested parties must be unanimous in their belief that the exercise is necessary and worthwhile. Tshepo can benefit from a job evaluation committee that has adequate knowledge of all the jobs in his organisation (see section 11.2.2 in chapter 11 of the prescribed book). This committee can then decide whether to formulate a job evaluation system or hire outside consultants.

Once the HR manager knows how to determine what to pay the different employees, he/she has to solve the problem of how to pay employees for performing their jobs. The answer to this question lies in the utilisation of the different pay systems available.

4.6 PAY SYSTEMS AND GUIDELINES FOR INCENTIVE PLANS

Compensation systems differ in organisations as well as among employees. The HR manager usually has to determine whether employees will be compensated for the time they took to do the job or for the amount of effort they put into it. In this section, we will look at different pay systems.



Study sections 11.3 and 11.4 in chapter 11 of the prescribed book.



Activity 4.4

Read this paragraph and answer the questions that follow.

A medium-sized business specialising in the manufacturing and distribution of corrugated cardboard gift boxes and storage containers has just completed wage negotiations with the union representatives of their staff. The following are agreed:

- a basic salary of R30 000 per annum
- a pension fund – 8% of annual salary, half to be contributed by the employee and half by the employer
- a hospital insurance fund – 10% of annual salary, half to be contributed by the employee and half

by the employer

- an across-the-board increase of 8.36%, effective from the following month; in addition to this, a 2% salary increase for staff who have worked at the company for longer than three years
- a gain-sharing plan for all employees in the company
- the individual performance incentive will be changed to team-based incentives from the following month
- the company will implement the broad-banding system

However, the employees are dissatisfied with the across-the-board increase and the implementation of team-based incentives.

- Identify the different forms of pay that the company offers in the paragraph.
- Critically discuss why employees are dissatisfied with the across-the-board increases.
- Draft a checklist to assess whether the guidelines for incentive plans in the organisation are adhered to.



Feedback

Employees should be compensated for their efforts and motivated (by means of various incentives) to keep up their good work. Generally employees do not perform the same across the board. You will agree that the type of job should determine the type of pay system to be used. The HR manager can use the following three types of approaches:

- Time-based approach – employees are paid for the time on the job
- Performance- and productivity-based approach – employees are rewarded for performance or productivity
- Tasks/skills-based approach – employees are paid for skills or competencies they possess rather than for specific tasks performed
- Organisations also want employees to realise the link between a portion of their compensation and the performance of their group or the entire organisation. Incentives such as profit-sharing plans or gain-sharing plans and employee stock ownership plans are often provided for by organisations (**see section 11.3.3 for a further explanation of these incentive plans**)

You could have referred to section 11.4 in chapter 11 in the prescribed book to compile a relevant checklist of guidelines for incentive plans. Here is an example:

Guideline for incentive plans	YES/NO
Bold incentives	No
Emphasis on team performance	Yes
Quick feedback	Yes

Adapted from Wörnich et al (2015)

Besides taking the above pay systems into account, the HR manager also has to remember that top management (or executives) are paid differently from mid-level and lower-level management (see "Executive compensation" in the prescribed book).

4.7 EXECUTIVE COMPENSATION

Executive compensation can be defined as the total remuneration or financial compensation a top executive receives within a company. This includes a basic salary, any and all bonuses, share options and any other company benefit. Executive compensation is an important part of corporate governance and is often determined by a company's board of directors.

Executives in any organisation (CEO, top management, etc) receive "special treatment" either in the form of add-on packages not received by other employees or in the form of compensation components entirely unique to the organisation. Milkovich and Newman (2008) identify two characteristics of this group:

- These employees tend to be strategically important to the company. If they do not succeed at their job, success for the entire organisation is in jeopardy.
- Their positions have built-in conflict. Conflict may arise because different factions place incompatible demands on members of the group.

This explains why executive compensation is different from the rest of the organisation's compensation.

Executive compensation has become a controversial issue in recent years. Cases of CEOs leaving office with large sums of money while the companies they led are in financial difficulties are regularly covered by the media and presented as proof that there is a problem. More recently, the economic crisis and government rescue of failing firms with public funds have justified imposing caps to executive pay (Kelly-Gagnon & Gu nette 2010). Adding to this, with the implementation of the King III report, the focus will be more on executive compensation than ever before.



Study section 11.5 in chapter 11 of the prescribed book and then answer the questions in activity 4.5.



Activity 4.5

- Distinguish between a golden parachute contract and a stock option plan.
- What are the most common determinants of CEO and executive pay?



Feedback

You should have referred to sections 11.5.1 and 11.5.2 in chapter 11 of the prescribed book to explain the difference between these two options. A golden parachute contract protects executives should another company buy their company. The stock option plan allows managers to buy a specific amount of stock in the company. By now you should understand the reasons for the difference in pay for top management and the rest of the organisation. A number of different factors determine the pay of top management, namely organisation size, organisation performance, executive-specific factors, organisation structure, job- or position-specific factors and job complexity.

Executive compensation has become a complex issue and requires proper planning and implementation, not only from HR, but at board level as well.

Once the HR manager knows why employees should be compensated, what to pay whom and how, you would think the compensation issue would be finalised. This is not the case. Most organisations do not just pay their employees a basic salary, but also provide something "extra". This "extra" is referred to as benefits.

4.8 BENEFITS

Organisations differ in how they allocate employee benefits or compensation. However, through

legislation (Compensation for Occupational Injuries and Diseases Act, Basic Conditions of Employment Act or the Unemployment Insurance Act), government influences employee benefits by means of regulations concerning safety, retirement or unemployment compensation. It is also interesting to note that a substantial amount of an organisation's compensation costs are made up of employee benefits. But is the payment or provision of these benefits really all that important?



Study section 11.6 in chapter 11 of the prescribed book.



Activity 4.6: Benefits

Watch the following video. Reflect and share your thoughts on compensation and benefits.

Compensation and benefits in animation

<https://www.youtube.com/watch?v=pqtYQb9nbRk>

Learning outcomes:

1. To differentiate between employee total compensation and reward systems offered by organisations
2. To be able to define job evaluation and discuss popular job evaluation methods
3. To identify and explain legislation that influences and regulates employee benefits
4. To be able to differentiate between individual and group incentives

Share your thoughts and understanding of compensation and benefits – do this online. If you are not employed, ask your parents or family members which benefits or types of compensation are offered by their organisation.

Refer to the [Discussion Forums](#) tool on the HRM2602 myUnisa module site and select [Forums 07: Workbook 04 Activities](#).

Answer the following questions:

- a. Which benefits mentioned in the video are provided by your organisation?
- b. Which of the benefits mentioned in the video are influenced by the government legislation concerning safety or loss of employment?
- c. Which of the reward pie benefits mentioned in the video are linked to business results and are also considered as voluntarily offered by the organisation?
- d. Explain the impact of benefits on the productivity and performance of employees.



Feedback

You now probably agree that it is really necessary to provide benefits. Originally, benefits were introduced to promote and reward employee loyalty and, in some instances, to discourage unionisation. There may also have been an element of paternalism – believing employees to be incapable of fully providing for their personal welfare. However, this has changed. Nowadays, benefits play an important role in encouraging employees to work for the organisation and to remain with it.

Organisations offer rewards based on business results, that is, the productivity or performance of employees (individuals or teams). Business results are an outcome of the strategic planning and

objectives of the organisation. Therefore rewards, pay systems or benefits will vary among organisations and will be linked to the performance of the organisation. You should have noticed that benefits can be classified into three basic groups, according to the type of benefit provided. These groups are the following:

- Economic benefits which include items such as life assurance, low-cost loans, profit-sharing, allowances and share purchase schemes. These benefits are also called non-cash deferred benefits.
- Employee services which include subsidised canteens, use of company vehicles, product or service discounts, medical services and education assistance. These types of benefits are also known as non-cash current benefits.
- Recreational benefits which include provision of leisure areas, sports facilities and social clubs.

In South Africa, organisations are legally required to provide the following employee benefits:

- unemployment insurance
- compensation for occupational injuries and diseases

All other employee benefits (e.g. pension, medical aid, housing subsidy) are provided at the discretion of the employer. Employers are not obligated to provide any voluntary benefit if they do not wish to do so.

Organisations offer benefits for a variety of reasons. The most important is the tax advantages received. Organisations are taxed on the size of their compensation payroll. By providing employee benefits, the size of the payroll is reduced. However, employee benefits are advantageous not only to the organisation, but also to the employee. Regardless of all the issues to consider when planning for compensation, the HR manager also has to be aware of the additional compensation issues when operating internationally. We will cover these in Workbook 11.

4.9 SUMMARY

By now you have probably realised that the compensation and benefits an organisation provides is one of the most powerful tools that HR managers have at their disposal. Competitive and equitable compensation, incentives and benefits will ensure that good employees are attracted to the organisation, that they are motivated to do their best and that they will remain with the organisation. Because of the importance of compensation and benefits, the HR manager will have to put extra effort into developing a proper compensation strategy.

Rewarding employees financially improves their level of motivation and thus improves productivity. This ultimately shows up in the "bottom line", and part of the increased profits must be circulated back to the workforce responsible for it.

4.10 SELF-ASSESSMENT



The self-assessment questions consist of multiple-choice and written questions. To access the multiple-choice questions, visit the self-assessment workbook 04 tab on [Additional Resources](#) and begin your assessment.

Question 1

How can an organisation safeguard the relationship of performance and motivation (where the employee is motivated to perform at high levels because there is a distinct link between performance and reward)?

Question 2

Define job evaluation and briefly discuss the purpose of job evaluation in employee compensation.

Question 3

What is a pay system? Differentiate between the three kinds of pay systems described in the prescribed book.

Question 4

Outline at least four reasons why an organisation needs a compensation system.



Question 1

You will find the answer to this question in "Compensation objectives" in the prescribed book and in section 4.4 of this workbook.

One of the objectives of compensation is to motivate employees by rewarding good performance and offering incentives. Explain how an organisation can do this by using performance appraisal, rewards for performance and feedback on performance.

Question 2

Find the answer to this question in "Job evaluation" in the prescribed book and in section 4.5 of this workbook.

When you answer this question, explain how job evaluation is used in compensation. Start by defining job evaluation and then explain what it is used for. Do not describe the job evaluation process or methods of job evaluation.

Question 3

You will find the answer to this question in "Pay systems" in the prescribed book and in section 4.6 and activity 4.4 of this workbook.

Describe the concept "pay system" and then use a table to describe and differentiate between time-based, person-based and performance-based systems.

Question 4

You will find the answer to this question in "Compensation objectives" in the prescribed book and in section 4.4 of this workbook. You should discuss the four objectives of a compensation system.



Reflect on your learning while working through this unit. Complete the following self-assessment checklist to determine your understanding of this unit and whether you have mastered the learning outcomes:

Learning outcomes	Yes	No
Am I able to explain the link between pay, motivation and performance?		
Will I be able to define job evaluation and discuss four popular methods of performing it?		
Am I able to differentiate between three types of individual incentives?		

Can I discuss why gain-sharing or profit-sharing and ESOPs have grown as organisational incentive plans?		
Can I discuss executive compensation methods?		
Am I able to explain the importance of employee benefits and their organisational objectives?		



GUIDELINES FOR COMPLETING THE REFLECTION ACTIVITY

- If you answered yes to all of the questions in the checklist, you are now ready to move on to the next workbook.
- If you answered no to any of the questions in the checklist, work through the specific sections again.

It is very important that you achieve all the learning outcomes of this module, as they guide your learning process in this module.



CARRY ON

Now that you have successfully completed Workbook 04 and all the activities, you can go on to Workbook 05.

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