Code: 0413-4102

Compensation Management

Demonstrate Understanding of the Pay Model and Apply Compensation Techniques and Policies

A company wants to recruit a Marketing Manager. Three candidates apply.

Candidate	Experience	Expected Salary
A	2 years	$40,000/year
B	5 years	$55,000/year
C	10 years	$75,000/year

Should the company pay all candidates the same salary? Why or why not?

HR managers use a Pay Model to determine fair, competitive, and strategic compensation.

Pay Model

The Pay Model is a framework that organizations use to design compensation systems that align employee rewards with organizational goals.

The Pay Model is a framework that helps organizations make compensation decisions consistent with business strategy.

–Milkovich, Newman & Gerhart

Importance of the Pay Model

A good pay model helps organizations

- ❑ Attract talented employees
- ❑ Retain skilled workers
- ❑ Improve motivation
- ❑ Increase productivity
- ❑ Promote fairness
- ❑ Control labor costs
- ❑ Achieve strategic goals

The Pay Model Framework

PAY MODEL

Compensation Objectives

↓

Compensation Policies

↓

Compensation Techniques

↓

Employee Performance

↓

Organizational Success

Four Policy Objectives of the Pay Model

The Pay Model is built around four policy objectives.

PAY MODEL

Internal Alignment

+

External Competitiveness

+

Employee Contributions

+

Management

Objective 1: Internal Alignment

Meaning

Internal alignment means

Employees are paid fairly according to the value of their jobs within the organization.

Position	Monthly Salary
Office Assistant	$600
Accountant	$1,000
HR Manager	$1,800
General Manager	$3,500

Higher responsibility receives higher compensation.

Techniques Used

- Job Analysis
- Job Evaluation
- Job Classification
- Pay Grades

Example

University employees

Vice Chancellor

↓

Dean

↓

Professor

↓

Associate Professor

↓

Assistant Professor

↓

Lecturer

Different responsibilities lead to different salary levels.

Objective 2: External Competitiveness

Meaning

Organizations compare their salaries with competitors.

Purpose

To Attract employees; Retain talent and Remain competitive

Example

Suppose three banks offer different salaries.

Bank	Salary
Bank A	$900
Bank B	$950
Bank C	$1,100

Most qualified applicants may choose Bank C.

Objective 3: Employee Contributions

Meaning

Employees receive rewards according to

- ✓ Performance
- ✓ Skills
- ✓ Knowledge
- ✓ Competencies

Common Compensation Methods

Merit Pay

Incentive Pay

Commission

Bonus

Profit Sharing

Gain Sharing

Example

Sales Employee

Basic Salary

$25,000/year

Sales Target Achieved

Performance Bonus

$5,000

Higher contribution receives higher reward.

Objective 4: Management

Meaning

Management refers to how compensation policies are designed, communicated, implemented, and evaluated.

Good compensation management includes

Fair administration

Transparency

Legal compliance

Employee communication

Budget control

Example

A company reviews salaries annually.

- ❑ Employees understand
- ❑ Performance criteria
- ❑ Promotion rules
- ❑ Bonus calculations

This increases trust.

Four Policy Objectives

Objective	Main Focus
Internal Alignment	Fairness inside the organization
External Competitiveness	Market competitiveness
Employee Contributions	Reward performance
Management	Effective administration

Compensation Techniques

Technique 1: Job-Based Pay

Employees are paid according to job value.

Example

Manager earns more than Assistant Manager because of greater responsibility.

Technique 2: Skill-Based Pay

Employees are paid according to skills.

Example

A technician who learns AI programming receives higher pay.

Compensation Techniques

Technique 3: Competency-Based Pay

Employees receive higher pay for demonstrating valuable competencies such as leadership, teamwork, or problem-solving.

Technique 4: Performance-Based Pay

Rewards depend on employee performance.

Examples

Sales incentives

Productivity bonuses

Annual merit increases

Compensation Techniques

Technique 5: Team-Based Pay

Teams receive rewards for achieving organizational goals.

Example

A hospital rewards the emergency department after achieving excellent patient satisfaction.

Technique 6: Profit Sharing

Employees receive part of the company's annual profit.

Example

If company profit increases by 20%, employees receive an additional annual bonus.

Compensation Techniques

Technique 7: Gain Sharing

Employees receive rewards when productivity improvements reduce costs or increase efficiency

Compensation Policies

Policy 1: Equal Pay for Equal Work

Employees performing similar work with similar qualifications should receive equal pay.

Policy 2: Performance-Based Compensation

Outstanding performance receives additional rewards.

Policy 3: Market-Based Compensation

Organizations compare salaries with competitors.

Policy 4: Flexible Benefits

Employees choose benefits according to their needs.

Examples

Health insurance

Childcare assistance

Education support

Retirement plans

Compensation Policies

Policy 5: Legal Compliance

Compensation must comply with

Minimum wage laws

Overtime regulations

Anti-discrimination laws

Tax regulations

Advantages of an Effective Pay Model

For Employees

- ✓ Fair compensation
- ✓ Higher motivation
- ✓ Career growth
- ✓ Job satisfaction
- ✓ Better quality of life

For Organizations

- ❑ Improved productivity
- ❑ Lower turnover
- ❑ Better recruitment
- ❑ Higher employee commitment
- ❑ Competitive advantage

Common Challenges

- ✓ Budget constraints
- ✓ Pay inequity
- ✓ Inflation
- ✓ Labor shortages
- ✓ Legal compliance
- ✓ Changing employee expectations
- ✓ Managing remote and hybrid workforces