CHAPTER 8

Total Rewards

WHAT DO I NEED TO KNOW?

After reading this chapter, you should be able to:

LO1	Discuss how organizations implement a "total rewards" approach to compensating and rewarding employees.
LO2	Identify the kinds of decisions and influences involved in providing base pay to employees.
LO3	Describe how organizations recognize individual, team, and organizational performance with incentives.
LO4	Summarize the role of employee benefits and the types of benefits offered by employers.
LO5	Review the importance of effectively communicating the organization's approach to total rewards.
LO6	Examine issues related to compensating and rewarding executives.

Ovais Iqbal/ Cisco.

Cisco's Time2Give provides full-time employees with five days of paid leave each year to volunteer with a non-profit or charity organization.

Cisco Provides Time2Give

Time2Give is the formal volunteering policy of the global IT and networking firm Cisco. The policy provides all full-time employees with five days of paid time each year to volunteer at a non-profit organization or charity of their choice. David Heather, vice-president of HR for Canada explains, "Employees were volunteering on their own time and taking some time off personally. We wanted to make the commitment to our employees that they could have five days of paid leave that wouldn't affect their benefits."

Cisco employees can schedule the time in increments such as two hours twice a month or take the five days as a block of time. Employees let their managers know and book their time in the company tracking system, similar to how they book vacation time. The volunteer projects vary from judging a local science fair, to scuba diving to clear debris, to building schools in Africa. "We leave it open to our employees," says Heather. "It's their passion; it's their choice."

With his time from "Time2Give," Toronto-based Ovais Iqbal, director of systems engineering, recently travelled to Turkey for one week to volunteer with the Canadian charity Minhaj Welfare Foundation. The Foundation provides aid and distributes food to people displaced by the violence in Syria and was exploring the feasibility of building an orphan care home in Reyhanli, a town near the Syrian border. Iqbal shared his experience on a Cisco blog: "There is no doubt that this trip has changed me. I feel grateful to live in Canada and to work for a company that believes we have a responsibility to be our better selves and help those in need, no matter where they are in the world."[1]

Introduction

Many organizations are recognizing the strategic value of adopting a comprehensive approach to compensating and rewarding employees, frequently referred to as **total rewards**. Figure 8.1 shows how a total rewards strategy reflecting the organization's culture, business strategy, and HR strategy is a powerful tool to attract, motivate, engage, and retain employees while achieving organizational performance and results.

total rewards A comprehensive approach to compensating and rewarding employees.

RBC defines its approach to employee compensation and benefits to take into account the "overall work experience provided to employees."[2] Organizations with this total rewards approach create a *value proposition* for current and prospective employees that considers the total value they receive for contributing their time and energy to the company. Because compensation, benefits, and the work experience have a major impact on employee attitudes and behaviours, total rewards influence what kinds of employees are attracted to (and remain with) the organization. A survey on strategic rewards and pay practices reported that Canadian companies cited the primary reason for developing a total rewards strategy was to align rewards with the business strategy.[3] As shown in Figure 8.2, the Conference Board of Canada's Compensation Planning Outlook 2018 identified the top rewards activities and priorities for the next 12 to 18 months as maintaining competitive position; reviewing strategy and ensuring alignment with business objectives; retaining talent, attracting talent; and connecting pay and performance.[4]

FIGURE 8.1

Total Rewards Model

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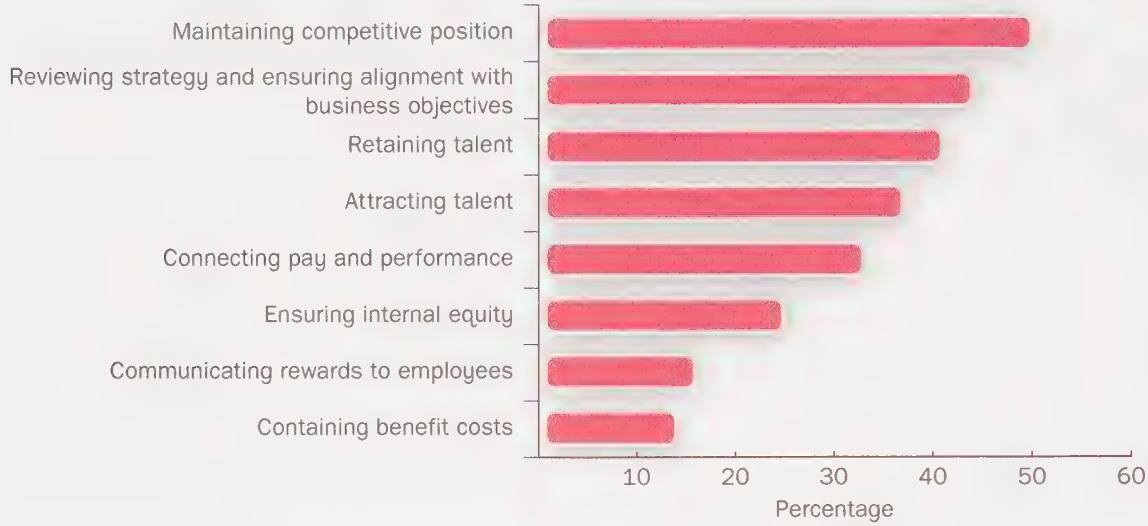
FIGURE 8.2

Top Rewards Activities and Priorities



Source: Heather McAteer, "Compensation Planning Outlook 2018" (Ottawa: Conference Board of Canada, October 2017), p. 19. Reprinted with permission by the Conference Board of Canada.

Employees care about policies affecting their compensation, benefits, and the work experience itself because these policies affect not only their income but also their overall well-being and security. Also, employees consider these elements a sign of status and success. They attach great importance to compensation and rewards when they evaluate their relationship and satisfaction with their employers. As the workforce becomes increasingly diverse, the definition of what employees expect in exchange for their work will become increasingly complex. For example, Table 8.1 provides some generational total rewards preferences for consideration. This chapter addresses total rewards; however, the primary emphasis will be on forms of **total compensation**, that is, direct and indirect compensation including base pay, incentives, and benefits received in exchange for the employee's contribution of time, talent, effort, and results.[5] In addition, Chapter 1 discussed (and Chapter 11 will discuss) attributes of work environments where employees are more likely to experience satisfaction and engagement, Chapter 6 explored training, learning, and development opportunities provided to employees, and Chapter 7 examined performance processes. A comprehensive "Total Rewards Inventory" checklist outlining elements that could be included in an organization's value proposition is provided in Figure 8.3.

total compensation All types of financial rewards and tangible benefits and services employees receive as part of their employment.

direct compensation Financial rewards employees receive in exchange for their work.

This chapter opens by describing the role of **direct compensation**—all types of financial rewards employees

TABLE 8.1

Generational Emphasis within Total Rewards

Baby Boomers	High-visibility projects, promotions, support around work/life issues, personal learning and development, onsite facilities, industry recognition
Gen X	Training, learning, and development; challenging tasks/stretch assignments; independent work environment; project variety; work/life balance; flexible work arrangements; variable pay
Millennials (Gen Y)	Meaningfulness of work/projects, manager feedback, casual work environment, daily work/life balance, access to senior leaders, mentoring, social activities, community involvement, flextime

Source: Adapted from Adwoa K. Buahene and Giselle Kovary, "The Great Divide," *HR Professional*, October/November 2007, p. 27.

FIGURE 8.3

Total Rewards Inventory

Compensation

Base Wages
- ☐ Salary Pay
- ☐ Hourly Pay
- ☐ Piece Rate Pay

Premium Pay
- ☐ Shift Differential Pay
- ☐ Weekend/Holiday Pay
- ☐ On-Call Pay
- ☐ Call-In Pay
- ☐ Hazard Pay
- ☐ Bilingual Pay
- ☐ Skill-Based Pay

Variable Pay
- ☐ Commissions
- ☐ Team-Based Pay
- ☐ Bonus Programs
  - ☐ Referral Bonus
  - ☐ Hiring Bonus
  - ☐ Retention Bonus
  - ☐ Project Completion Bonus
- ☐ Incentive Pay
  - Short-Term:
    - ☐ Profit Sharing
    - ☐ Individual Performance–Based Incentives
    - ☐ Performance-Sharing Incentives
  - Long-Term:
    - ☐ Restricted Stock
    - ☐ Performance Shares
    - ☐ Performance Units
    - ☐ Stock Options/Grants

Benefits

Legally Required/Mandated
- ☐ Employment Insurance
- ☐ Workers' Compensation Insurance
- ☐ Canada Pension Plan/Quebec Pension Plan

Health & Welfare
- ☐ Medical Plan
- ☐ Dental Plan
- ☐ Vision Plan
- ☐ Prescription Drug Plan
- ☐ Flexible Spending Accounts (FSAs)
- ☐ Health Reimbursement Accounts (HRAs)
- ☐ Health Savings Accounts (HSAs)
- ☐ Life Insurance
- ☐ Spouse/Dependent Life Insurance
- ☐ AD&D Insurance
- ☐ Short-Term/Long-Term Disability Insurance

Retirement
- ☐ Defined Benefit Plan
- ☐ Defined Contribution Plan
- ☐ Profit-Sharing Plan
- ☐ Hybrid Plan

Pay for Time Not Worked
- ☐ Vacation
- ☐ Holiday
- ☐ Sick Leave
- ☐ Bereavement Leave
- ☐ Leaves of Absence (personal, medical, family)

Work/Life

Workplace Flexibility/Alternative Work Arrangements
- ☐ Flextime
- ☐ Flexible Schedules
- ☐ Telecommuting
- ☐ Alternative Work Sites
- ☐ Compressed Workweek
- ☐ Job Sharing
- ☐ Part-Time Employment
- ☐ Seasonal Schedules

Paid and Unpaid Time Off
- ☐ Maternity/Family Leave
- ☐ Sabbaticals

Health and Wellness
- ☐ Employee Assistance Programs
- ☐ On-Site Fitness Facilities
- ☐ Discounted Fitness Club Rates
- ☐ Preventive Care Programs
- ☐ Weight Management Programs
- ☐ Smoking Cessation Assistance
- ☐ On-Site Massages
- ☐ Stress Management Programs
- ☐ Voluntary Immunization Clinics
- ☐ Wellness Initiatives
- ☐ Health Screenings
- ☐ Nutritional Counselling
- ☐ On-Site Nurse
- ☐ Business Travel Health Services
- ☐ Occupational Health Programs
- ☐ Disability Management
- ☐ Return-to-Work Programs
- ☐ Reproductive Health/Pregnancy Programs

Community Involvement
- ☐ Community Volunteer Programs
- ☐ Matching Gift Programs
- ☐ Shared Leave Programs
- ☐ Disaster Relief Funds
- ☐ Sponsorships/Grants
- ☐ In-Kind Donations

Caring for Dependants
- ☐ Dependant Care Reimbursement Accounts
- ☐ Dependant Care Travel-Related Expense Reimbursement
- ☐ Dependant Care Referral and Resource Services
- ☐ Dependant Care Discount Programs or Vouchers
- ☐ Emergency Dependant Care Services
- ☐ Childcare Subsidies
- ☐ On-Site Caregiver Support Groups
- ☐ On-Site Dependant Care
- ☐ Adoption Assistance Services
- ☐ After-School Care Programs
- ☐ University and college/Scholarship Information
- ☐ Scholarships
- ☐ Mother's Privacy Rooms
- ☐ Summer Camps and Activities

Financial Support
- ☐ Financial Planning Services and Education
- ☐ Adoption Reimbursement
- ☐ Transit Subsidies
- ☐ Savings Bonds

Voluntary Benefits
- ☐ Long-Term Care
- ☐ Auto/Home Insurance
- ☐ Pet Insurance
- ☐ Legal Insurance
- ☐ Identity Theft Insurance
- ☐ Employee Discounts
- ☐ Concierge Services
- ☐ Transit Passes
- ☐ Parking

Culture Change Initiatives
- ☐ Work Redesign
- ☐ Team Effectiveness
- ☐ Diversity/Inclusion Initiatives
- ☐ Work Environment Initiatives

Performance & Recognition

Performance
- ☐ Manager/Employee 1:1 Meetings
- ☐ Performance Reviews
- ☐ Project Completion/Team Evaluations
- ☐ Performance Planning/Goal-Setting Sessions

Recognition
- ☐ Service Awards
- ☐ Retirement Awards
- ☐ Peer Recognition Awards
- ☐ Spot Awards
- ☐ Managerial Recognition Programs
- ☐ Organization-Wide Recognition Programs
- ☐ Exceeding Performance Awards
- ☐ Employee of the Month/Year Awards
- ☐ Appreciation Luncheons, Outings, Formal Events
- ☐ Goal-Specific Awards (quality, efficiency, cost savings, productivity, safety)
- ☐ Employee Suggestion Programs

Development & Career Opportunities

Learning Opportunities
- ☐ Tuition Reimbursement
- ☐ Tuition Discounts
- ☐ Corporate Universities
- ☐ New Technology Training
- ☐ On-the-Job Learning
- ☐ Attendance at Outside Seminars and Conferences
- ☐ Access to Virtual Learning, Podcasts, Webinars
- ☐ Self-Development Tools

Coaching/Mentoring
- ☐ Leadership Training
- ☐ Exposure to Resident Experts
- ☐ Access to Information Networks
- ☐ Formal or Informal Mentoring Programs

Advancement Opportunities
- ☐ Internships
- ☐ Apprenticeships
- ☐ Overseas Assignments
- ☐ Internal Job Postings
- ☐ Job Advancement/Promotion
- ☐ Career Ladders and Pathways
- ☐ Succession Planning
- ☐ On/Off Ramps Through Career Lifecycle
- ☐ Job Rotations

Source: Based on WorldatWork "Your Total Rewards Inventory," p. 4, retrieved May 5, 2008. WorldatWork website: www.worldatwork.org

receive as part of their employment—and defines the kinds of influences on those making pay-level decisions. We describe methods of evaluating jobs and market data to develop effective pay structures. Next, we look at the elements of incentive pay systems. The many kinds of incentive pay fall into three broad categories: incentives linked to individual, team, or organizational performance. Choices from these categories should consider not only their strengths and weaknesses, but also their fit with the organization's goals. This chapter also looks at **indirect**

compensation—the benefits and services employees receive in exchange for their work—including the important role benefits play. The chapter also covers why and how organizations should effectively communicate with employees about their total rewards. Finally, this chapter looks at an issue also linked to organizational performance—executive compensation.

indirect compensation The benefits and services employees receive in exchange for their work.

Decisions about Base Pay

Because pay is important both in its effect on employees and its cost, organizations need to plan what they will pay employees in each job. An unplanned approach, in which each employee's pay is independently negotiated, will likely result in unfairness, dissatisfaction, and rates that are either overly expensive or so low that positions are hard to fill. Organizations make decisions about two aspects of pay structure: job structure and pay level. **Job structure** consists of the relative pay for different jobs within the organization. It establishes relative pay among different functions and different levels of responsibility. For example, job structure defines the difference in pay between an entry-level accountant and an entry-level assembler, as well as the difference between an entry-level accountant, a senior accountant, and a director of accounting. **Pay level** is the average amount (including wages, salaries, and incentives) the organization pays for a particular job. Together, job structure and pay levels establish a **pay structure** that helps the organization achieve goals related to employee motivation, cost control, and the ability to attract and retain talented people.

job structure The relative pay for different jobs within the organization.

pay level The average amount (including wages, salaries, and incentives) the organization pays for a particular job.

pay structure The pay policy resulting from job structure and pay-level decisions.

The organization's job structure and pay levels are policies of the organization. Establishing a pay structure simplifies the process of making decisions about individual employees' pay by grouping together employees with similar jobs. As shown, in Figure 8.4, human resource professionals develop this pay structure based on legal requirements, market forces, and the organization's goals, such as attracting a high-quality workforce and meeting principles of fairness.

What Are the Legal Requirements?

All of an organization's decisions about compensation and rewards need to at least *comply* with the applicable laws. As discussed in Chapter 2, although these laws differ

FIGURE 8.4

Considerations in Developing a Pay Structure

across federal, provincial, and territorial jurisdictions, a common core of legal requirements including human rights legislation, employment labour standards acts, and pay equity legislation exists. Ontario's pay transparency legislation is also provided as an illustrative example of an emerging attention.

- **Human rights legislation**—Employers may not base differences in rewards on an employee's age, sex, race, or other prohibited ground of discrimination. Any differences in pay must instead be tied to business-related considerations such as job responsibilities or performance.
- **Employment/labour standards acts**—The Canada Labour Code and the relevant provincial and territorial laws include minimum requirements for wages, hours of work, overtime pay, vacation, and statutory holidays, as well as other specific provisions. Adopting a $15 per hour minimum wage has stimulated controversy as described later in the chapter in HR Oops. Alberta's minimum hourly wage increased to $15 on October 1, 2018, and British Columbia has announced a $15.20 minimum hourly wage effective June 1, 2021.[6] Executives, professionals, administrative, and outside sales employees are usually considered "exempt" employees and are not eligible for certain provisions such as overtime pay that "non-exempt" employees receive.
- **Pay equity legislation**—In addition to the Federal Government of Canada, pay equity legislation is in place in several provinces, and attempts to address the wage gap between female- and male-dominated jobs to ensure that jobs of equal value within the organization receive similar rates of pay. Organizations use job evaluation (described later in the chapter) to establish the worth of an organization's jobs in terms of criteria such as their difficulty and their importance to the organization. The employer then compares the evaluation points awarded to each job with the pay for each job. If jobs have the same number of evaluation points, they should be paid equally. As discussed in Chapter 2, pay equity remains a highly relevant issue driven through public, political, and organizational awareness and efforts to disrupt gender-based pay gaps.
- **Pay transparency legislation (Ontario)**—Ontario's Pay Transparency Act, 2018, effective January 1, 2019, disrupts the stigma (and fear of potential retaliation) of discussing salary with co-workers and others and reducing the wage gap between female and male employees. Requirements on provincially regulated employers in Ontario include:[7]
    - all publicly advertised job openings must include a salary rate or range.
    - job candidates cannot be asked about past compensation received.
    - employees who discuss their compensation cannot be disciplined or face reprisals.
    - some employers are required to monitor and report "compensation gaps based on gender and/or other diversity characteristics."

Economic Influences on Pay

An organization cannot make spending decisions independent of the economy. Organizations must keep costs low enough that they can sell their products profitably, yet they must be able to attract workers in a competitive labour market. Decisions about how to respond to the economic forces of product markets and labour markets limit an organization's choices about pay structure.

Product and Labour Markets

The organization's *product market* includes organizations that offer competing goods and services—competing to serve the same customers. Organizations under pressure to cut labour costs may respond by reducing staff levels, freezing pay levels, postponing hiring decisions, or requiring employees to bear more of the cost of benefits such as insurance premiums. However, organizations also compete to obtain human resources in *labour markets*—competing with other firms to hire the same skilled employees.

Pay Level: Deciding What to Pay

Although legal requirements and economic influences limit organizations' choices about pay levels, there is a range within which organizations can make decisions.[8] The size of this range depends on the details of the organization's competitive environment. If many workers are competing

Ron Levine/Getty Images

Two employees who do the same job cannot be paid differently because of gender, race, age, or other prohibited grounds of discrimination. Only if there are differences in their experience, skills, seniority, or job performance are there legal reasons their pay might be different.

for a few jobs, employers will have more choice; however, in tight labour markets workers will have more employment options.

When organizations have a broad range in which to make decisions about pay, they can choose to pay *at, above,* or *below* the rate set by market forces. Economic theory holds that the most profitable level, all things being equal, would be at the market rate. Often, however, all things are *not* equal from one employer to another. For instance, an organization may gain an advantage by paying above the market rate if it uses the higher pay as one means to attract top talent and then uses these excellent employees' knowledge to be more innovative, produce higher quality, or work more efficiently.

This approach is based on the view of employees as resources. Higher pay may be an investment in superior human resources. Having higher labour costs than your competitors is not necessarily bad if you also have the best and most effective workforce, which produces more products of better quality. Pay policies are one of the most important human resource tools for encouraging desired employee behaviours. Therefore, organizations must evaluate pay as more than a cost—but rather as an *investment* that can generate returns in attracting, retaining, and motivating a high-quality workforce. Of course, employers do not always have this much flexibility. Some companies are under intense pressure to charge low prices for their products, and some companies are trying to draw workers from a pool that is too small to satisfy all employers' needs.

Gathering Information about Market Pay

To compete for talent, organizations use **benchmarking**, a procedure in which an organization compares its own practices against those of successful competitors. In terms of compensation, benchmarking involves the use of pay surveys that provide information about the going rates of pay at competitors in the organization's product and labour markets. An organization can conduct its own surveys, but the federal government and other organizations make a great deal of data readily available.

benchmarking
A procedure in which an organization compares its own practices against those of successful competitors.

For example, the federal government's Job Bank site provides earnings data by city or postal code for occupations listed in the National Occupational Classification (NOC). Many industry, trade, and professional groups also collect wage and salary data. Employers should check with the relevant groups to see what surveys are available. Consulting firms also will provide data, including the results of international surveys, and can tailor data to an organization's particular needs. Human resource professionals need to determine whether to gather data focusing on particular industries, regions, or job categories.

How Do Employees Judge Pay Fairness?

In developing a pay structure, it is important to keep in mind employees' perceptions about fairness. If employees perceive their pay as unfair, they may experience pay dissatisfaction and be less motivated to achieve organizational goals. Employees evaluate their pay relative to the pay of other employees. Social scientists have studied this kind of comparison and developed *equity theory* to describe how people make judgments about fairness.[9] According to equity theory, people measure outcomes such as pay in terms of their inputs. For example, an employee might think of her pay in terms of her degree, her three years of experience, and her 45+ hour workweeks. To decide whether a certain level of pay is equitable, the person compares her ratio of outcomes and inputs with other people's outcome/input ratios. The person in this example might notice that an employee with less education or experience is earning more than she is (unfair) or that an employee who works 55 hours a week is earning more (fair). In general, employees compare their pay and contributions using several considerations:

- What they think employees in other organizations earn for doing the same job.
- What they think other employees holding different jobs within the organization earn for doing work at the same or different levels.
- What they think other employees in the organization earn for doing the same job.

How employees respond to their impressions about equity can have a great impact on the organization. Typically, if employees see their pay as equitable, their attitudes and behaviour continue unchanged. If employees see themselves as receiving an advantage, they usually rethink the situation to see it as equitable. But if employees conclude that they are under-rewarded, they are likely to make up the difference in one of three ways—putting forth less effort (reducing their inputs), finding a way to increase their outcomes (e.g., asking for a raise), or withdrawing by leaving the organization or withholding their best ideas.

As work becomes more collaborative and the emphasis on knowledge-sharing increases, it becomes more likely that information about pay will also be shared. Social media and sites such as Glassdoor are contributing to this trend.

Job Structure: Relative Value of Jobs

Along with market forces and principles of fairness, organizations consider the relative contribution each job should make to the organization's overall performance. One typical way of doing this is with a **job evaluation**, an administrative procedure for measuring the relative internal worth of the organization's jobs. Usually, the organization does this by assembling and training a job evaluation committee, consisting of people familiar with the jobs to be evaluated. The committee often includes a human resource specialist and, if its budget permits, may hire an outside consultant.

job evaluation An administrative procedure for measuring the relative internal worth of the organization's jobs.

To conduct a job evaluation, the committee identifies each job's *compensable factors,* meaning the characteristics of a job that the organization values and chooses to pay for. As shown in Table 8.2, an organization might consider the effort required and skill requirements of people performing information technology-related jobs. Other compensable factors might include working conditions and responsibility. Based on the job attributes defined by job analysis (discussed in Chapter 3), the jobs are rated for each factor. The rater assigns each factor a certain number of points, giving more points to factors when they are considered more important and when the job requires a high level of that factor. Often the number of points comes from one of the *point manuals* published by trade groups and management consultants. If necessary, the organization can adapt the scores in the point manual to the organization's situation or even develop its own point manual. As in the example in Table 8.2, the scores for each factor are totalled to arrive at an overall evaluation for each job.

Job evaluations provide the basis for decisions about *relative internal worth*—the value of the job within the organization necessary to meet pay equity requirements as discussed in Chapter 2. According to the sample assessments in Table 8.2, the job of business systems analyst is worth more to this organization than the job of database administrator. Therefore, the organization would be willing to pay significantly more for the work of a business systems analyst than it would for the work of a database administrator.

The organization may limit its pay survey to jobs evaluated as *key jobs.* These are jobs that have relatively stable content and are common among many organizations, so it is possible to obtain survey data about what people earn in these jobs. Organizations can make the process of creating a pay structure more practical by defining key jobs. Research for creating the pay structure is limited to the key jobs that play a significant role in the organization. Pay for the key jobs can be based on survey data, and pay for the organization's other jobs can be based on the organization's job structure. A job with a higher evaluation score than a particular key job would receive higher pay than that key job.

Pay Structure: Putting It All Together

The pay structure reflects decisions about how much to pay (pay level) and the relative value of each job (job structure). The organization's pay structure should reflect what the organization knows about market forces, as well as its own unique goals and the relative contribution of each job to achieving the goals. By balancing this external and internal information, the organization's goal is to set levels of pay that employees will consider fair and motivating. Organizations typically apply the information by establishing some combination of pay rates, pay grades, and pay ranges. Within this structure, they may state the pay in terms of a rate per hour, commonly called an **hourly wage**; a rate of pay for each unit produced, known as a **piecework rate**, or a rate of pay per week, month, or year worked, called a **salary**.

hourly wage Rate of pay per hour worked.

piecework rate Rate of pay for each unit produced.

salary Rate of pay for each week, month, or year worked.

Pay Rates

If the organization's main concern is to match what people are earning in comparable jobs, the organization can base pay directly on market research into as many of its key jobs as possible. To do this, the organization looks for survey data for each job title. If it finds data from more

TABLE 8.2

Job Evaluation of Three Jobs with Four Compensable Factors

	Compensable Factors				
Job Title	Skill	Effort	Responsibility	Working Conditions	Total
Database administrator	60	40	30	30	130
Software developer	80	60	50	20	210
Business systems analyst	110	70	70	20	270

than one survey, it must weight the results according to their quality and relevance. In light of that knowledge, the organization decides what it will pay for the job.

The next step is to determine salaries for the non-key jobs, for which the organization has no survey data. Instead, the person developing the pay structure creates a graph like the one in Figure 8.5. The vertical axis shows a range of possible pay rates, and the horizontal axis measures the points from the job evaluation. The analyst plots points according to the job evaluation and pay rate for each key job. Finally, the analyst fits a line, called a **pay policy line**, to the points plotted. (This can be done statistically, using a procedure called regression analysis.) Mathematically, this line shows the relationship between job evaluation and rate of pay. Using this line, the analyst can estimate the market pay level for a given job evaluation. Looking at the graph gives approximate numbers, or the regression analysis will provide an equation for calculating the rate of pay. For example, using the pay policy line in Figure 8.5, a job with 315 evaluation points would have a predicted salary of $7,783 per month.

pay policy line
A graphed line showing the mathematical relationship between job evaluation points and pay rate.

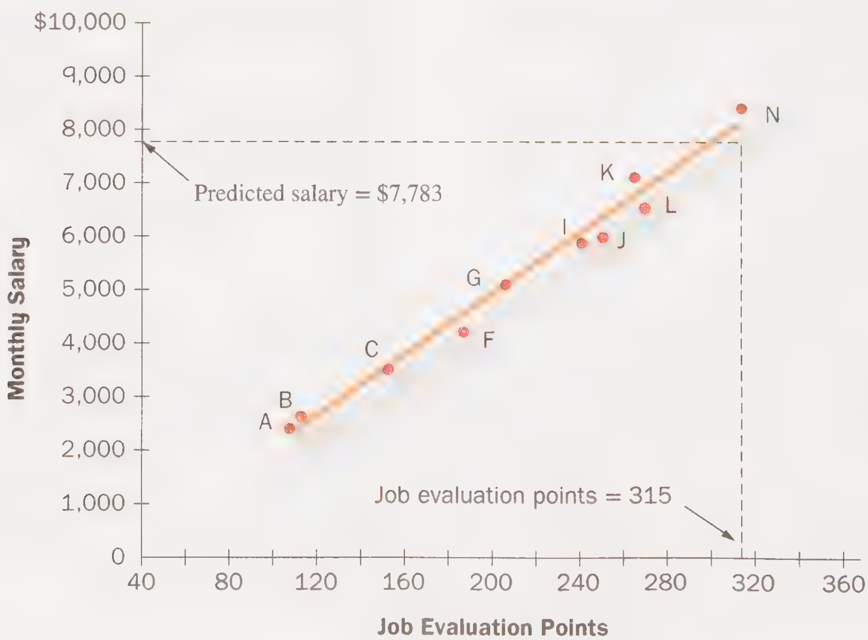
The pay policy line reflects the pay structure in the market, which does not always match rates in the organization (see key job F in Figure 8.5). Survey data may show that people in certain jobs are actually earning significantly more or less than the amount shown on the pay policy line. For example, some kinds of expertise are in short supply. People with that expertise can command higher pay, because they can easily leave one employer to get higher pay somewhere else. Suppose, in contrast, that local businesses have laid off many warehouse employees. Because so many of these workers are looking for jobs, organizations may be able to pay them less than the rate that job evaluation points would suggest.

When job structure and market data conflict in these ways, organizations have to decide on a way to resolve the two. One approach is to stick to the job evaluations and pay according to the employees' worth to the organization. Organizations that do so will be paying more or less than they have to, so they will likely have more difficulty competing for customers or employees. A way to moderate this approach is to consider the importance of each position to the organization's goals.[10] If a position is critical for meeting the organization's goals, paying more than competitors pay may be worthwhile.

At the other extreme, the organization could base pay entirely on market forces. However, this approach also has some practical drawbacks. One is that employees may conclude that pay rates are unfair. Two vice-presidents or two supervisors will expect to receive similar pay because their responsibilities are similar. If the differences between their pay are large, because of different market rates, the lower-paid employee will likely be dissatisfied. Also, if the organization's development plans include rotating managers through different assignments, the managers will be reluctant to participate if managers in some departments receive lower pay. Organizations therefore must weigh all the objectives of their pay structure to arrive at suitable rates.

FIGURE 8.5

Pay Policy Lines



Pay Grades

pay grades Sets of jobs having similar worth or content, grouped together to establish rates of pay.

A large organization could have hundreds or even thousands of different jobs. Setting a pay rate for each job would be extremely complex. Therefore, many organizations group jobs into **pay grades**—sets of jobs having similar worth or content, grouped together to establish rates of pay. For example, the organization could establish five pay grades, with the same pay available to employees holding any job within the same grade.

A drawback of pay grades is that grouping jobs will result in rates of pay for individual jobs that do not precisely match the levels specified by the market and the organization's job structure. Suppose, for example, that the organization groups together its accountants (with a job evaluation of 255 points) and its business systems analysts (with a job evaluation of 270 points). Surveys might show that the market rate of pay for business systems analysts is higher than that for accountants. In addition, the job evaluations give more points to business systems analysts. Even so, for simplicity's sake, the organization pays the same rate for the two jobs, because they are in the same pay grade. The organization would have to pay more than the market requires for accountants or pay less than the market rate for business systems analysts (so it would probably have difficulty recruiting and retaining them).

Pay Ranges

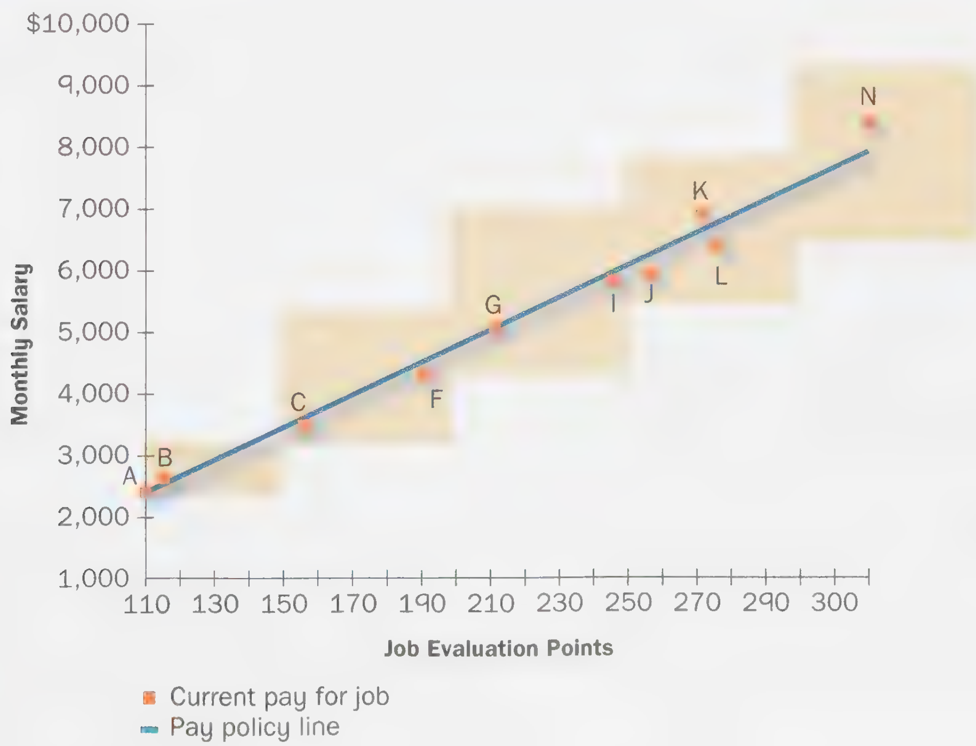
Usually, organizations want some flexibility in setting pay for individual jobs. They want to be able to pay the most valuable employees the highest amounts and to give rewards for performance. Flexibility also helps the organization balance conflicting information from market surveys and job evaluations. Therefore, pay structure usually includes a **pay range** for each job or pay grade. In other words, the organization establishes a *minimum, maximum,* and *midpoint* of pay for employees holding a particular job or a job within a particular pay grade or band. Employees holding the same job may receive somewhat different pay, depending on where their pay falls within the range.

pay range A set of possible pay rates defined by a minimum, maximum, and midpoint of pay for employees holding a particular job or a job within a particular pay grade or band.

A typical approach is to use the market rate or the pay policy line as the midpoint of a range for the job or pay grade. The minimum and maximum values for the range may also be based on market surveys of those amounts. Pay ranges are most common for professional and administrative jobs and for jobs not covered by union contracts. Figure 8.6 shows an example of pay ranges based on the pay policy line in Figure 8.5. Notice that the jobs are grouped into five pay grades, each with its own pay range.

FIGURE 8.6

Sample Pay Grade Structure



In this example, the range is widest for employees who are at higher levels in terms of their job evaluation points. That is because the performance of these higher-level employees will likely have more effect on the organization's performance, so the organization needs more latitude to reward them. For instance, as discussed earlier, the organization may want to select a higher point in the range to attract an employee who is more critical to achieving the organization's goals.

Usually pay ranges overlap somewhat, so that the highest pay in one grade is somewhat higher than the lowest pay in the next grade. Overlapping ranges gives the organization more flexibility in transferring employees among jobs, because transfers need not always involve a change in pay. On the other hand, the less overlap, the more important it is to earn promotions in order to keep getting raises. Assuming the organization wants to motivate employees through promotions (and assuming enough opportunities for promotion are available), the organization will want to limit the overlap from one level to the next.

Alternatives to Job-based Pay

The traditional and most widely used approach to developing a pay structure focuses on setting pay for jobs or groups of jobs.[11] This emphasis on jobs has some limitations. The precise definition of a job's responsibilities can contribute to a mindset that some activities "are not in my job description," at the expense of flexibility, innovation, quality, and customer service. Organizations may avoid change because it requires repeating the time-consuming process of creating job descriptions and related paperwork. Another change-related problem is that when the organization needs a new set of competencies, the existing pay structure may be rewarding the wrong behaviours. Finally, a pay structure that rewards employees for winning promotions may discourage them from gaining valuable experience through lateral career moves.

Organizations have responded to these problems with a number of alternatives to job-based pay structures. Some organizations have found greater flexibility by **broadbanding**, a pay structure that consolidates pay grades into a few "broad bands," thereby reducing the number of pay ranges in the organization's pay structure. For example, back in the 1990s IBM changed from a pay structure with 5,000 job titles and 24 salary grades to one with 1,200 jobs and 10 bands. Broadbanding reduces the opportunities for promoting employees, but this type of pay structure tends to encourage and provide flexibility for employees to make lateral career moves.

broadbanding A pay structure that consolidates pay grades into a few "broad bands."

Another way organizations have responded to the limitations of job-based pay has been to move away from the link to jobs and toward pay structures that reward employees based on their knowledge and skills (competencies).[12] **Competency-based pay systems** (also known as *skill-based pay systems*) are pay structures that set pay according to the employees' level of skill or knowledge and what they are capable of doing. Paying for competencies makes sense at organizations where changing technology requires employees to continually widen and deepen their knowledge. Competency-based pay also supports efforts to involve employees and enrich jobs because it encourages employees to add to their knowledge so they can make decisions in many areas. In this way, competency-based pay helps organizations become more flexible and innovative. More generally, competency-based pay can encourage a climate of learning and adaptability and give employees a broader view of how the organization functions.

competency-based pay systems Pay structures that set pay according to the employees' levels of skill or knowledge and what they are capable of doing.

A disadvantage associated with this type of pay system is that it rewards employees for acquiring skills but does not provide a way to ensure that employees actually *use* their new skills.[13] The result may be that the organization is paying employees more for learning skills that the employer is not benefiting from. The challenge for HRM is to design work so that the work design and pay structure support one another.

Pay Structure and Actual Pay

Usually the human resource department is responsible for establishing the organization's pay structure. But building the structure is not the end of the organization's decisions about pay structure. The structure represents the organization's policy, but what the organization actually does may be different. As part of its management responsibility, the HR department therefore should compare actual pay to the pay structure, ensuring that policies and practices match.

A common way to do this is to measure a *compa-ratio,* the ratio of average pay to the midpoint of the pay range. Figure 8.7 shows an example. Assuming the organization has pay grades, the organization would find a compa-ratio for each pay grade: the average paid to all employees in the pay grade divided by the midpoint for the pay grade. If the average equals the midpoint, the compa-ratio is 1. More often the compa-ratio is somewhat above 1 (meaning the average pay is above the midpoint for the pay grade) or below 1 (meaning the average pay is below the midpoint).

Assuming that the pay structure is well planned to support the organization's goals, the compa-ratios should be close to 1. A compa-ratio greater than 1 suggests that the organization is paying employees more than planned

FIGURE 8.7

Finding a Compa-Ratio

Pay Grade: 1
Midpoint of Range: $4,675 per month

Salaries of Employees in Pay Grade	
Employee 1	$5,306
Employee 2	$4,426
Employee 3	$5,223
Employee 4	$5,114

Compa-Ratio

$$\frac{\text{Average}}{\text{Midpoint}} = \frac{\$5{,}017.25}{\$4{,}675.00} = 1.07$$

Average Salary of Employees
$5,306 + $4,426 + $5,223 + $5,114 = $20,069
$20,069 ÷ 4 = $5,017.25

and may have difficulty keeping costs under control. A compa-ratio less than 1 suggests that the organization may be underpaying employees and may have difficulty attracting and retaining qualified employees.

Incentive Pay

The first part of this chapter discussed the framework for total rewards and setting pay for jobs. Now we focus on using pay to recognize and reward employees' contributions to the organization's success.

In contrast to decisions about pay structure, organizations have wide discretion in setting performance-related pay, called **incentive pay** or *pay for performance*. Organizations can tie incentive pay to individual performance, profits, or many other measures of success. They select incentives based on their costs, expected influence on performance, and fit with the organization's broader HR and company policies and goals.

incentive pay Forms of pay linked to an employee's performance as an individual, group member, or organization member.

Many organizations offer incentive pay in the effort to energize, direct, or influence employees' behaviour. According to the Conference Board of Canada, 82 percent of Canadian organizations have at least one short-term incentive plan. These plans are particularly popular in the private sector—91 percent of companies reported having one or more short-term incentive plans and 53 percent of public-sector organizations also have one or more short-term incentive plans.[14] Incentive pay is influential because the amount paid is linked to certain predefined behaviours or outcomes. For example, an organization can pay a salesperson a *commission* for closing a sale, or the members of a production department can earn a *bonus* for meeting a monthly production goal. Knowing they can earn extra money for closing sales or meeting departmental goals, the employees often try harder or get more creative than they might without the incentive pay. In addition, the policy of offering higher pay for higher performance may make an organization attractive to high performers.[15]

For incentive pay to motivate employees to contribute to the organization's success, the plans must be well designed. In particular, effective plans meet the following requirements:

- Performance measures are linked to the organization's goals.
- Employees believe they can meet performance standards.
- The organization gives employees the resources they need to meet their goals.

Adam121/Dreamstime.com/GetStock.com

Many sales associates in the auto industry earn a straight commission, meaning that 100 percent of their pay comes from commission instead of a salary. What type of individual might enjoy a job like this?

- Employees value the rewards given.
- Employees believe the reward system is fair.
- The plan takes into account that employees may ignore any goals that are not rewarded.

Because incentive pay is linked to particular outcomes or behaviours, the organization is encouraging them to demonstrate those desired outcomes and behaviours. As obvious as that may sound, the implications are more complicated. If incentive pay is extremely rewarding, employees may focus on only the performance measures rewarded under the plan and ignore measures that are not rewarded. Many call centres pay employees based on how many calls they handle, as an incentive to work quickly and efficiently. However, speedy call handling does not necessarily foster good customer relationships. Organizations may combine a number of incentives so employees do not focus on one measure to the exclusion of others.

Although most, if not all, employees value pay, it is important to remember that earning money is not the only reason people try to do a good job. As discussed in other chapters (see Chapters 1, 6, and 11), people also want interesting work, appreciation for their efforts, flexibility, and a sense of belonging to the work group—not to mention the inner satisfaction of work well done. Therefore, a complete plan for compensating and rewarding employees has many components, from pay to work design to developing managers so they can provide effective leadership.

We will now identify elements of incentive pay systems. We consider each option's strengths and limitations with regard to these principles. The many kinds of incentive pay fall into three broad categories: incentives linked to individual, team, or organizational performance. Choices from these categories should consider not only their strengths and weaknesses, but also their fit with the organization's goals. The choice of incentive pay may affect not only the level of motivation but also the kinds of employees who are attracted to and stay with the organization. For example, there is some evidence that organizations with team-based rewards will tend to attract employees who are more team oriented.[16]

Pay for Individual Performance

Although individual pay for performance can "foster an individualistic culture or a culture of entitlement,"[17] organizations reward individual performance with a variety of incentives.

- **Piecework rates**—As an incentive to work efficiently, some organizations pay production workers a piecework rate, a wage based on the amount they produce. The amount paid per unit is set at a level that rewards employees for above-average production volume. A clear advantage of piece rates is the direct link between how much work the employee does and the amount the employee earns. However, for complex jobs or jobs with hard-to-measure outputs, piecework plans do not apply very well. Also, unless a plan is well designed to include performance standards, it may not reward employees for focusing on quality or customer satisfaction if it interferes with the day's output. In Figure 8.8, the employees quickly realize they can earn huge bonuses by writing software "bugs" and then fixing them, while writing bug-free software affords no chance to earn bonuses.
- **Standard hour plans**—Another quantity-oriented incentive for production workers is the **standard hour plan**, an incentive plan that pays workers extra for work done in less than a preset "standard time." The organization determines a standard time to complete a task, such as tuning up a car engine. If the mechanic completes the work in less than the standard time, the mechanic receives an amount of pay equal to the wage for the full standard time. Suppose the standard time for tuning up an engine is 2 hours. If the

FIGURE 8.8

How Incentives Sometimes "Work"

Source: DILBERT, reprinted by permission of United Features Syndicate, Inc.

mechanic finishes the tune-up in 1.5 hours, the mechanic receives 2 hours of pay for 1.5 hours worked. Working that fast over the course of a week could add significantly to the mechanic's pay. In terms of pros and cons, standard hour plans are much like piecework plans. They encourage employees to work as fast as they can, but not necessarily to care about quality or customer service.

- **Merit pay**—Almost all organizations have established some program of **merit pay**—a system of linking pay increases to ratings on performance appraisals. An advantage of merit pay is that it provides a method for rewarding performance in all of the dimensions measured in the organization's performance management system. If that system is appropriately designed to measure all the important job behaviours, then the merit pay is linked to the behaviours the organization desires. This link seems logical, although so far there is little research showing the effectiveness of merit pay.[18] A drawback of merit pay, from the employer's standpoint, is that it can quickly become expensive. Managers at a majority of organizations rate most employees' performance in the top two categories (out of four or five).[19] Therefore, the majority of employees are eligible for the biggest merit increases, and their pay rises rapidly. Another drawback of merit pay is that it assumes that performance is based on employees' ability and motivation; however, performance may be enhanced or reduced by factors beyond the employees' control (e.g., economic conditions or a manager's rating bias).

standard hour plan An incentive plan that pays workers extra for work done in less than a preset "standard time."

- **Performance bonuses**—Like merit pay, performance bonuses reward individual performance, but bonuses are not rolled into base pay. The employee must re-earn them during each performance period. In some cases, the bonus is a one-time reward. For example, the nearby Did You Know? discusses the use of "spot" bonuses. Bonuses may also be linked to objective performance measures rather

merit pay A system of linking pay increases to ratings on performance appraisals.

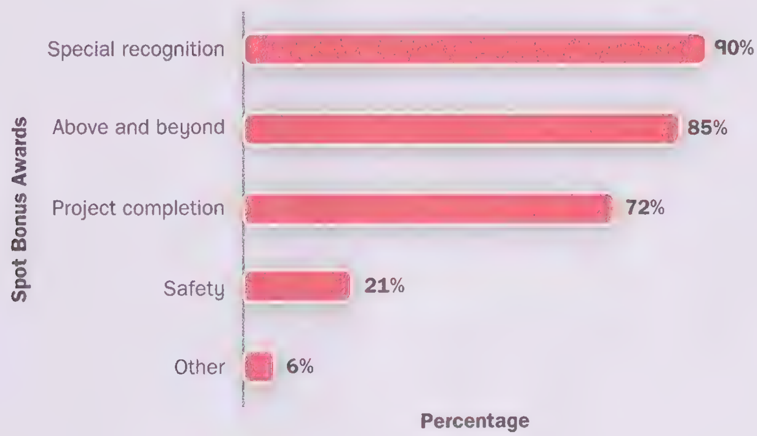
Did You KNOW?

Awarding Spot Bonuses

A majority of companies (60 percent) paid *spot bonuses*—bonuses delivered on the spot for special recognition—most frequently to reward performance above and beyond expectations or upon the completion of a project. In organizations that award these bonuses, maximum payouts to managers, supervisors, and professionals are typically in the range of $2,500 to $5,000.

Questions

1. From the perspective of an employer, how could you determine whether the increase in the use of spot bonuses makes good business sense?



Source: "Bonus Programs and Practices," June 2014, pp. 6, 9, and 19. Contents © 2018. Reprinted with permission from WorldatWork. Content is licensed for use by purchaser only. No part of this article may be reproduced, excerpted or redistributed in any form without express written permission from WorldatWork. WorldatWork website: www.worldatwork.org than potentially subjective ratings. Bonuses for individual performance can be extremely effective and give the organization great flexibility in deciding what kinds of behaviour to reward. All this flexibility makes it essential to be sure that bonuses are tied to behaviour that makes a difference for the organization's overall performance and to ensure that employees have some control over achieving the bonus requirements.

- **Commissions**—A variation on piece rates and bonuses is the payment of **commissions**, or pay calculated as a percentage of sales. For instance, a flooring sales consultant might earn commissions equalling 6 percent of the price of the flooring the person sells during the period. In a growth-oriented organization, sales commissions need not be limited to salespeople.

commissions Incentive pay calculated as a percentage of sales.

Pay for Team Performance

Employers may address the drawbacks of individual incentives by including team incentives in the organization's compensation plan. To earn team incentives, employees must cooperate and share knowledge so that the entire team can meet its performance targets. Widely used team incentives include gainsharing, bonuses, and team awards.

Gainsharing

Organizations that want employees to focus on efficiency may adopt a **gainsharing** program, which measures increases in productivity and effectiveness and distributes a portion of each gain to employees. For example, if a factory enjoys a productivity gain worth $30,000, half the gain might be the company's share. The other $15,000 would be distributed among the employees in the factory. Knowing that they can enjoy a financial benefit from helping the company be more productive, employees supposedly will look for ways to work more efficiently and improve the way the factory operates.

gainsharing Team incentive program that measures improvements in productivity and effectiveness and distributes a portion of each gain to employees.

Gainsharing addresses the challenge of identifying appropriate performance measures for complex jobs. Even for simpler jobs, setting acceptable standards and measuring performance can be complicated. Gainsharing frees employees to determine how to improve their own and their team's performance. It also broadens employees' focus beyond their individual interests. But in contrast to profit sharing, discussed later, it keeps the performance measures within a range of activity that most employees believe they can influence. Organizations can enhance the likelihood of a gain by providing a means for employees to share knowledge and make suggestions, as we will discuss later in this chapter.

Gainsharing is most likely to succeed when organizations provide the right conditions. Among the conditions identified, the following are among the most common:[20]

- management commitment
- need for change or strong commitment to continuous improvement
- management acceptance and encouragement of employee input
- high levels of cooperation and interaction
- employment security
- information sharing on productivity and costs
- goal setting
- commitment of all involved parties to the process of change and improvement
- performance standards and calculations that employees understand and consider fair and that are closely related to managerial objectives
- employees who value working in teams

Team Bonuses and Awards

In contrast to gainsharing plans, which typically reward the performance of all employees at a facility, bonuses for team performance tend to be for smaller work groups.[21] These bonuses reward the members of a group for attaining a specific goal, usually measured in terms of physical output. Team awards are similar to team bonuses, but they are more likely to use a broad range of performance measures, such as cost savings, successful completion of a project, or even meeting deadlines.

Robert Churchill/Getty Images

Team members who meet a sales goal or a product development team that meets a deadline or successfully launches a product may be rewarded with a bonus for team performance. What are some advantages and disadvantages of team bonuses?

Both types of incentives have the advantage that they encourage group or team members to cooperate and collaborate so that they can achieve their goal. However, depending on the reward system, competition among individuals may be replaced by competition among teams. Competition may be healthy in some situations, as when teams try to outdo one another in satisfying customers. On the downside, competition may also prevent necessary cooperation among teams. To avoid this, the organization should carefully set the performance goals for these incentives so that concern for costs or sales does not obscure other objectives, such as quality, customer service, and ethical behaviour.

Pay for Organizational Performance

Two important ways organizations measure their performance are in terms of their profits and their stock price. In a competitive marketplace, profits result when an organization is efficiently providing products that customers want at a price they are willing to pay. Stock is the owners' investment in a corporation; when the stock price is rising, the value of that investment is growing. Rather than trying to figure out what performance measures will motivate employees to do the things that generate high profits and a rising stock price, many organizations offer incentive pay tied to those organizational performance measures. The expectation is that employees will focus on what is best for the organization.

These organization-level incentives can motivate employees to align their activities with the organization's goals. At the same time, linking incentives to the organization's profits or stock price exposes employees to a high degree of risk. Profits and stock price can soar very high very fast, but they can also fall. The result is a great deal of uncertainty about the amount of incentive pay each employee will receive in each period. Therefore, these kinds of incentive pay are likely to be most effective in organizations that emphasize growth and innovation, which tend to need employees who thrive in a risk-taking environment.[22]

Profit Sharing

With **profit sharing**, payments are a percentage of the organization's profits and do not become part of the employees' base salary. Organizations use profit sharing for a number of reasons. It may encourage employees to think more like owners, taking a broad view of what they need to do in order to make the organization more effective. Employees are more likely to cooperate and less likely to focus on narrow self-interest. Also, profit sharing has the practical advantage of costing less when the organization is experiencing financial difficulties. If the organization has little or no profit, this incentive pay is small or nonexistent, so employers may not need to rely as much on layoffs to reduce costs.[23]

profit sharing Incentive pay in which payments are a percentage of the organization's profits and do not become part of the employees' base salary.

An organization setting up a profit-sharing plan should consider what to do if profits fall. If the economy slows and profit-sharing payments disappear along with profits, employees may become discouraged or dissatisfied. If profit sharing is offered to all employees but most employees think only management decisions about products, price, and marketing have much impact on profits, they will conclude that there is little connection between their actions and their rewards. In that case, profit sharing will have little impact on employee behaviours. This problem is even greater when employees have to wait months before profits are distributed. The time lag between high performance, behaviour, and financial rewards is sometimes simply too long to be motivating.

Given the limitations of profit-sharing plans, one strategy is to use them as a component of a pay system that includes other kinds of pay more directly linked to individual behaviour. This increases employees' commitment to organizational goals while addressing concerns about fairness.

Stock Ownership

While profit-sharing plans are intended to encourage employees to "think like owners," a stock ownership plan actually makes employees part owners of the organization. Like profit sharing, employee ownership is intended as a way to encourage employees to focus on the success of the organization as a whole. The drawbacks of stock ownership as a form of incentive pay are similar to those of profit sharing. Specifically, it may not have a strong effect on individuals' motivation. Employees may not see a strong link between their actions and the company's stock price, especially in larger organizations. The link between pay and performance is even harder to appreciate because the financial benefits mostly come when the stock is sold—typically when the employee leaves the organization. Ownership programs usually take the form of *stock options* or *employee stock ownership plans*. These are illustrated in Figure 8.9.

Stock Options

One way to distribute stock to employees is to grant **stock options**—the right to buy a certain number of shares of stock at a specified price. (Purchasing the stock is called *exercising* the option.) Suppose that in 2019 a company's employees received options to purchase the company's stock at $10 per share. The employees will benefit if the stock price rises above $10 per share, because they can pay $10 for something

stock options Rights to buy a certain number of shares of stock at a specified price.

FIGURE 8.9

Types of Pay for Organizational Performance

(a share of stock) that is worth more than $10. If in 2024 the stock is worth $18, they can exercise their options and buy stock for $10 a share. If they want to, they can sell their stock for the market price of $18, receiving a gain of $8 for each share of stock. Of course, stock prices can also fall. If the 2024 stock price is only $8, the employees would not exercise the options.

Traditionally, organizations have granted stock options to their executives. In recent years, many organizations pushed eligibility for options further down in the organization's structure. Some studies suggest that organizations perform better when a large percentage of top and middle managers are eligible for long-term incentives such as stock options.[24]

Recent scandals have drawn attention to another challenge of using stock options as incentive pay. As with other performance measures, employees may focus so much on stock price that they lose sight of other goals, including ethical behaviour. Ideally, managers would bring about an increase in stock price by adding value in terms of efficiency, innovation, and customer satisfaction. But there are other, unethical ways to increase stock price by tricking investors into thinking the organization is more valuable and more profitable than it actually is. Hiding losses and inflating the recorded value of revenues are just two ways some companies have boosted stock prices, enriching managers until these misdeeds come to light.

Employee Stock Ownership Plans

While stock options are most often used with top management, a broader arrangement is the **employee stock ownership plan (ESOP)**. In an ESOP, the organization distributes shares of stock to its employees by placing the stock into a trust managed on the employees' behalf. Employees receive regular reports on the value of their stock, and when they leave the organization, they may sell the stock to the organization or (if it is a publicly traded company) on the open market. For example, WestJet's Share Purchase Program enables WestJetters to receive up to 20 percent of their salaries in WestJet shares. Shares can be purchased as common shares or can be directed into RRSPs with WestJet matching the employee's contributions.[25]

employee stock ownership plan (ESOP) An arrangement in which the organization distributes shares of stock to all its employees by placing it in a trust.

Although ESOPs are the most common form of employee ownership, they raise a number of issues. On the negative side, they carry a significant risk for employees. Problems with the company's performance therefore can take away significant value from the ESOP. Many companies set up ESOPs to hold retirement funds, so these risks directly affect employees' retirement income.

Still, ESOPs can be attractive to employers. Along with tax and financing advantages, ESOPs give employers a way to build pride in and commitment to the organization. Employees have a right to participate in votes by shareholders (if the stock is registered on a national exchange, such as the TSX).[26] This means employees participate somewhat in corporate-level decision making.

What Is the Role of Employee Benefits?

Employees at almost every organization receive more than cash in exchange for their efforts. They also receive a package of **employee benefits**—compensation in forms other than cash (indirect compensation). Examples include paid vacation time, tuition reimbursement, and pension plans, among a wide range of possibilities.

As part of the total rewards provided to employees, benefits serve functions similar to pay. Benefits contribute to attracting, retaining, and motivating employees. The variety of possible benefits also helps employers tailor their offerings to the kinds of employees they need. Employers

employee benefits Compensation in forms other than cash.

HR How-To

Rewarding Workers When Raises Are Not an Option

You want to reward good performance, but there's hardly any money in the budget for raises and bonuses. That's the situation facing many HR managers in today's business climate. Here are some suggestions for making the most of whatever you can spend:

- Make sure that merit pay is truly related to performance gains. Raises are expensive and widely used, so high-performing employees expect to earn significantly more than average. Therefore, it is essential to be sure that performance measures used as the basis for raises are tied to business success and that the organization measures performance accurately.
- Offer modest but frequent incentives as quick rewards for accomplishments. An unexpected $100 one-time award for delighting a customer can have more impact, at a lower cost, than a $100 per month raise.
- Implement other strategies to reward performance that can also serve as employee incentives, such as flexible schedules, interesting and unique projects, and formal recognition. These are particularly useful for companies that don't have large budgets to provide meaningful year-end or spot bonuses.
- If the organization cannot afford to give everyone—or even all the above-average performers—a raise, it should target pay increases to the top performers. Explain that merit pay is for doing something exceptional, not just performing one's job. When expressed clearly, this message actually can strengthen employees' understanding of the connection between performance and incentive pay.
- Set and communicate clear, measurable targets for earning incentive pay. Employees want to understand what they have to do to earn a raise or bonus. They also appreciate knowing the size of the incentive they are eligible to earn.
- Accept that employees who do not achieve the requirements for earning incentive pay may leave. If the system is working properly, the employees who leave will be the ones who contribute the least. If good performers also are leaving, make sure the organization is providing employees with the resources they need—including training and empowerment—for meeting performance targets.

Sources: Stephen Miller, "Flat Salary Increase Budgets Spur Promotions for Pay Raises," *Society for Human Resource Management,* November 19, 2015, https://www.shrm.org; Yian Q. Mui, "Companies Have Found Something to Give Their Workers Instead of Raises," *Washington Post,* July 28, 2015, https://www.washingtonpost.com; "28 Ways to Reward and Recognize Your Employees," *Titan HR,* February 28, 2015, http://titanhr.com; Juan Pablo Gonzalez, Kate Richardson, and Hemali Desai, "Get More Bang for Your Comp Program Buck Despite Stagnant Salary Budget Increases," *Compensation Focus* (WorldatWork), October 2013, http://www.worldatwork.org.

need to examine their benefits package regularly to see whether they still meet employees' needs and expectations. Even if employers spend large sums on benefits, if employees do not understand how to use them or why they are valuable, the cost of the benefits will be largely wasted.[27] Employers need to communicate effectively so that the benefits are understood and appreciated by employees.

Employees have come to expect that benefits will help them maintain economic security. Canada Pension Plan/Quebec Pension Plan, company pension plans, and retirement savings plans help employees prepare for their retirement. Insurance plans help to protect employees from costs such as unexpected medical expenses. The important role that benefits serves is a reason that some benefits are required by law, e.g., Employment Insurance.

Even though many kinds of benefits are not required by law, they have become so common that today's employees expect them. Many employers find that attracting qualified workers requires them to provide health and retirement benefits of some sort. A large employer without such benefits would be highly unusual and would have difficulty competing in the labour market. A national survey conducted by Ipsos-Reid found that Canadian employees value their health benefits. As reported by Benefits Canada, 91 percent of survey respondents said that other than salary, a "good job" was defined as having a good benefits package—"benefits are serving as a proxy or a marker for a good workplace."[28] And a Sanofi Canada Healthcare Survey reveals that Millennial employees are more likely than their older co-workers to see benefits as a right—63 percent of Baby Boomers see health benefits as a perk or privilege, whereas only 50 percent of Millennial employees see health benefits as a perk or privilege.[29]

Like other forms of compensation and rewards, benefits impose significant costs. On average, out of every dollar spent on compensation, more than 31 cents go to benefits and this share has been steadily rising.[30] An organization managing its labour costs must pay careful attention to the cost of its employee benefits.

Overall, employers are concerned about balancing various issues related to benefits provided to employees. Several forces have made benefits a significant part of compensation packages. One is that laws require employers to provide certain benefits, such as contributions to Canada Pension Plan and Employment Insurance. Also, tax laws can make benefits favourable. For example, employees do not pay income taxes on most benefits they receive, but they pay income taxes on cash compensation. Therefore, an employee who receives a $1,000 raise "takes home" less than the full $1,000, but an employee who receives an additional $1,000 worth of non-taxable benefits receives the full benefits. Another cost advantage of paying benefits is that employers, especially large ones, often can get a better deal on insurance or other programs than employees can obtain on their own.

Finally, some employers assemble creative benefits packages to set them apart in the competition for talent. For example, Netflix offers unlimited vacation time (within reason). This policy is in keeping with its HR strategy of "hiring adults"—experts who already have a history of success, love movies, and can manage their time. Since the company's success comes from people driven by a passion for what they do and what they can accomplish, offering freedom as a benefit contributes to attracting and keeping the right talent.[31] Apple and Facebook attracted media attention when they offered female employees $20,000 toward "egg freezing" as part of their comprehensive benefits package (the same benefit is offered to men by covering the cost of sperm freezing).[32]

What Benefits Are Required by Law?

Governments require various forms of security to protect workers from financial hardships. Because these benefits are required by law, employers cannot gain an advantage in the labour market by offering them, nor can they design the nature of these benefits.

Canada Pension Plan (CPP)/Quebec Pension Plan (QPP) A contributory, mandatory plan that provides retirement pensions, disability benefits, and survivor benefits.

- **Canada Pension Plan (CPP)/Quebec Pension Plan (QPP).** These plans cover all workers in Canada who are age 18 and older and have annual income exceeding $3,500. CPP/QPP is a mandatory **contributory plan** that provides retirement pensions, disability benefits, and survivor benefits. Workers who meet eligibility requirements receive benefits according to their age and earnings history.[33]

contributory plan All costs of the plan are funded by employees, employers, and the plan's own investments.

Employment Insurance (EI) A federally mandated program to provide temporary financial assistance to non-working Canadians.

- **Employment Insurance (EI).** This federally mandated program provides temporary financial assistance to non-working eligible people who have lost their jobs through no fault of their own, while they look for another job or upgrade their skills. Coverage is also extended to include a variety of situations; for example, to those who are ill; are providing compassionate care to a gravely ill family member; are pregnant, are parents caring for a newborn or adopted child, or are parents caring for a critically ill child.[34]

Workers' Compensation Acts Provincial programs that provide benefits to workers who suffer work-related injuries or illnesses.

- **Workers' Compensation Acts.** These provincial programs provide benefits to workers who suffer work-related injuries or illnesses. Workers' compensation operates under a principle of *no-fault liability,* meaning that an employee does not need to show that the employer was grossly negligent in order to receive compensation, and the employer is protected from lawsuits. The benefits fall into three major categories: wage-loss benefits, medical services, and rehabilitative services. Workers' compensation is entirely funded by employers—neither workers nor the government contribute. The amount employers pay depends on the industry and kinds of occupations involved as well as the size of the employer's payroll. Organizations can minimize the cost of this benefit by keeping workplaces safe and making employees and their managers conscious of safety issues, as discussed in Chapter 2.

What Optional Benefits Do Some Employers Provide?

Other types of benefits are optional. These include various kinds of insurance, retirement plans, and paid leave. Part-time workers often receive fewer benefits than full-time employees. The most widely offered benefits are paid leave for vacations and holidays (that exceed the legally required minimums specified in employment/labour standards legislation), life and medical insurance, and retirement plans. The extent to which the employer pays for the benefit varies widely among organizations. Some organizations require employees to pay a significant percentage of the premiums for insurance plans such as dental coverage. Other organizations pick up 100 percent of the premiums.

Benefits such as health insurance usually extend to employees' spouses and dependants. To ensure an employer does not face a charge of discrimination related to sexual orientation and/or marital status as a protected ground of discrimination, employers cover different-sex as well as same-sex partners.

Paid Leave

Employment/labour standards legislation outlines minimum entitlements (e.g., bereavement leave and paid holidays); however, many employers provide vacation and holidays in addition to the minimum legislated requirements. Some organizations also offer additional days off for personal reasons or to contribute their time to a charitable organization. For example, Cisco Systems' Time2Give formal volunteering policy, which provides all full-time employees with five days of paid time each year to volunteer at a nonprofit organization or charity of their choice was discussed in the chapter opening.

Sick leave programs pay employees for time not worked because of health issues. The amount of sick leave is often based on length of service, so that it accumulates over time; for example, one day added to sick leave for each month of service. Employers have to decide how many paid leave days to grant and whether to let them continue accumulating year after year. As reported by the Conference Board of Canada, the overall absenteeism rate has increased from an average of 6.0 days per employee in 2006–2007 to 6.6 days in 2016–2017. Absenteeism in the public sector averages 8.8 days per employee in contrast to 5.4 days in the private sector.[35]

An organization's policies for time off may include other forms of paid and unpaid leave. For a workforce that values flexibility, the organization may offer paid *personal days,* days off employees may schedule according to their personal needs, with the supervisor's approval. Typically, organizations offer a few personal days in addition to sick leave. *Floating holidays* are paid holidays that vary from year to year. The organization may schedule floating holidays so that they extend a Tuesday or Thursday holiday into a long weekend. Organizations may also give employees discretion over the scheduling of floating holidays.

Employers should establish policies for leaves without pay; for example, leaves of absence to pursue nonwork goals or to meet family needs. Unpaid leave is also considered an employee benefit because the employee usually retains seniority and benefits during the leave.

Group Insurance and Benefits

As we noted earlier, rates for group insurance are typically lower than for individual policies. Also, insurance benefits are not subject to income tax, as wages and salaries are. When employees receive insurance as a benefit, rather than higher pay so they can buy their own insurance, employees can get more for their money. Because of this, most employees value group insurance. The most common types of insurance and benefits offered as employee benefits are medical, life insurance, and disability insurance.

- **Medical insurance.** The policies typically cover medical expenses that are incurred over and above provincially funded medical coverage. Some employers offer additional coverage, such as dental care, vision care, and prescription drug programs. Employers must also make choices about coverage of so-called "lifestyle drugs," that is, drugs considered "cosmetic" or "discretionary." Examples are medical treatments for obesity, infertility, erectile dysfunction, male pattern baldness, and smoking cessation.[36] With legalization of recreational cannabis, more companies are covering medical cannabis as part of their benefits coverage. For example, Sun Life Financial includes medical marijuana in its group benefits plan.[37]

  An alternative (or in addition) to traditional employer-provided medical insurance is a **health spending account**, in which an employer puts aside a specific amount of money per employee to cover health-related costs. Employees decide what health care services they will purchase with their allocation.

health spending account A specific amount of money set aside per employee by the employer to cover health-related costs.

- **Employee health and wellness programs.** As discussed in Chapter 2, an employee wellness program is a set of communications, activities, and facilities designed to change health-related behaviours in ways that reduce risks. *Passive* programs provide information and services, but no formal support or motivation to use the program (e.g., health education and fitness facilities). *Active* wellness programs assume that behaviour change requires support and reinforcement along with awareness and opportunity (e.g., counsellors who tailor programs or coach individual employees). The Canadian Automobile Association's (CAA) health and wellness program has been recognized at the Benefits Canada Workplace Benefits Awards for its multi-faceted approach to engage all employees including remote workers. For example, its step challenge—offering a Fitbit subsidy as well as organizing learn-to-run clinics and running groups—has seen 63 percent of employees achieve a daily recommended amount of physical activity, up from 28 percent before the step challenge.[38]

Many organizations are adopting an integrated strategic approach to wellness that promotes a corporate culture to support employees in taking responsibility for their health and overall wellness including *financial wellness.*

Shutterstock / Daxiao Productions

Companies that value employee health and wellness may provide fitness equipment or even fully functional gym facilities.

For example, Microsoft offers employees one-on-one financial coaching sessions and uses a web-based app called FiTage, which uses data about each employee's income and assets to identify the age at which the person will become financially independent. Two months after rolling out the FiTage app, more than one-fifth of the company's employees had used it. Among the initial results, employees lowered their average FiT age by more than a year. Microsoft added incentives for using the app, and participation increased to half the workforce.[39]

- **Employee assistance program (EAP).** As discussed in Chapter 2, an employee assistance program (EAP) provides confidential counselling services to employees experiencing personal problems. Many organizations also extend these services to family members. Left untreated, personal problems may cause employees to lose their ability to cope and work performance will suffer. Employees must be able to feel confident the program respects their confidentiality. Other considerations include the range of offerings provided (some EAP providers offer a very broad range of services that may overlap with health, wellness, and lifestyle-related services); proximity to counsellors; client references; and availability of effectiveness reporting measures.[40]
- **Life insurance.** Employers may provide life insurance to employees or offer the opportunity to buy coverage at low group rates. With a *term life insurance* policy, if the employee dies during the term of the policy, the employee's beneficiaries receive a payment called a death benefit. In policies purchased as an employee benefit, the usual death benefit is a multiple of the employee's yearly pay. The policies may provide additional benefits for accidental death. Along with a basic policy, the employer may give employees the option of purchasing additional coverage, usually at a nominal cost.
- **Disability insurance.** Employees risk losing their income if a disability makes them unable to work. Disability insurance provides protection against this loss of income. Typically, **short-term disability insurance** provides benefits for six months or less. **Long-term disability insurance** provides benefits after that initial period, potentially for the rest of the disabled employee's life. Disability payments are a percentage of the employee's salary—typically 50 to 70 percent. Payments under short-term plans may be higher. Often the policy sets a maximum amount that may be paid each month. Because its limits make it more affordable, short-term disability coverage is offered by more employers.

short-term disability insurance Insurance that pays a percentage of a disabled employee's salary as benefits to the employee for six months or less.

long-term disability insurance Insurance that pays a percentage of a disabled employee's salary after an initial period and potentially for the rest of the employee's life.

Retirement Plans

Employers have no obligation to offer retirement plans beyond the protection of CPP/QPP security, but many offer some form of pension or retirement savings plan. As depicted in Figure 8.10, almost 6.2 million employees in Canada have registered pension plans (RPPs). A breakdown of registered pension plans and members by type of plan is provided.

An additional issue facing employers' approaches to retirement plans is a growing interest in **phased retirement**, a gradual transition into full retirement by reducing hours or job responsibility.[41] Employers are facing an increasing demand for phased retirement programs from employees who are healthier, living longer, and have personal or financial reasons to continue working in some capacity. Employers also benefit from retaining older workers with valued skills and experience who wish to retire gradually. Phased retirement also provides the employer with more time to transfer knowledge and skills to younger employees;[42] however, many employers are worried about the implications and costs of providing benefits coverage to older employees.

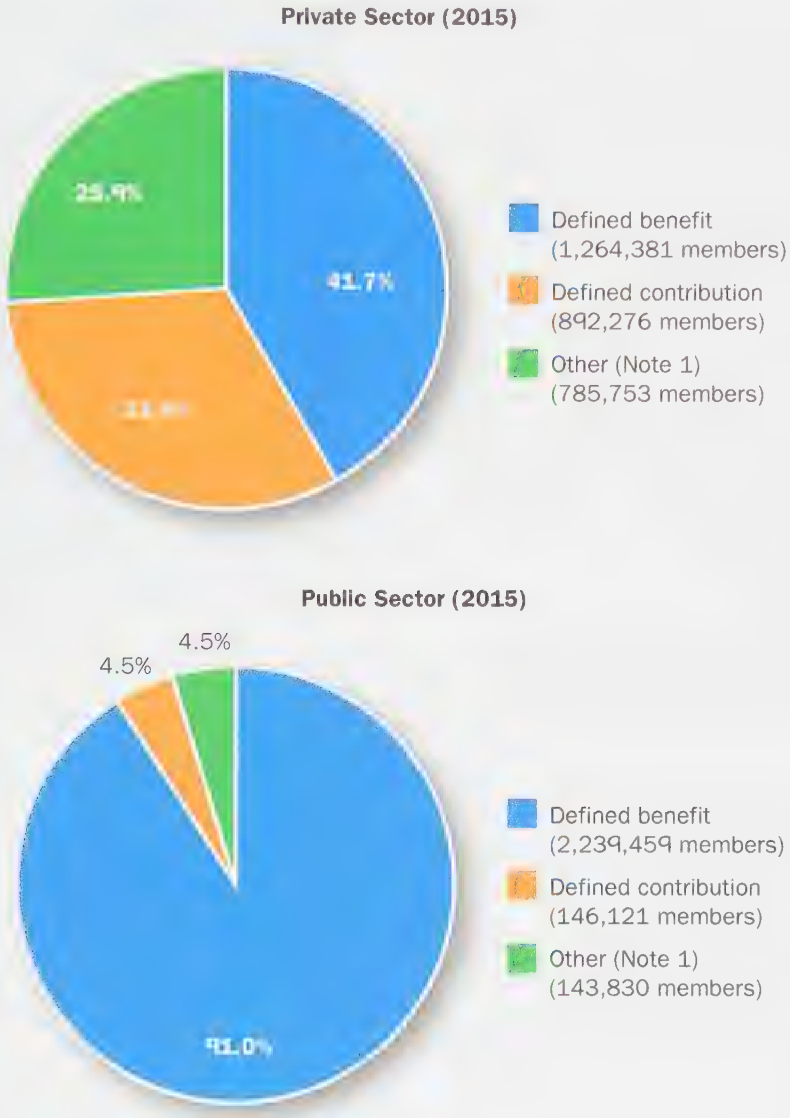
phased retirement A gradual transition into full retirement by reducing hours or job responsibility.

Most pension plans are either a defined benefit plan or a defined contribution plan.

- **Defined benefit plans.** Employers have a choice of using registered retirement plans (RPPs) that define the amount to be paid out after retirement or plans that define the amount the employer will invest each year.

FIGURE 8.10

Membership in Registered Pension Plans by Type of Plan and Sector



Note 1: Other plans include having a hybrid, composite, defined benefit/defined contribution, and other component.

Source: Statistics Canada, "Table 1: Registered pension plan membership, by sector and type of plan," *The Daily*, July 21, 2017, CANSIM Table 280–116, www.statcan.gc.ca/daily-quotidien/170721/t001d.htm, retrieved May 19, 2018.

defined benefit plan A pension plan that defines the benefits to be paid according to a formula stipulated in the plan.

A **defined benefit plan** defines the benefits to be paid according to a formula stipulated in the plan.[43] Usually the amount of this defined benefit is calculated for each employee based on the employee's years of service, age, and earnings (e.g., a percentage of the average of the employee's five highest-earnings years). These calculations typically result in pension payments that may provide 70 percent of pre-retirement income for a long-service employee. Using years of service as part of the basis for calculating benefits gives employees an incentive to stay with the organization so it can help to reduce voluntary turnover. Overall, 67.1 percent of employees in Canada with an RPP (in 2015) were in a defined benefit pension plan; however, this represents a decline from more than 85 percent in 2001,[44] largely due to the migration of new and existing private-sector employees to defined contribution plans. For example, in 2012, RBC stopped offering new Canadian hires access to its defined benefit plan. Existing employees can remain in RBC's defined benefits plan or switch to the defined contribution plan, which was made attractive through features such as higher employer contributions.[45]

- **Defined contribution plans.** An alternative to defined benefits is a **defined contribution plan**, which specifies the contributions made by the employer, as well as the employee. Pension benefits are based upon the accumulated contributions and investment returns achieved.[46] These plans free employers from the risks that investments will not perform as well as expected. They put the responsibility for wise investing squarely on the shoulders of each employee. A defined contribution plan is also easier to administer. Considering the advantages to employers, it is not surprising that a growing share of retirement plans in the private sector are defined contribution plans. Defined contribution plans do not penalize employees for changing jobs; however, these plans provide less assurance of financial security in retirement.

defined contribution plan A retirement plan that specifies the contributions made by the employer as well as the employee; pension benefits are based upon the accumulated contributions and investment returns achieved.

Denisismagilov/Dreamstime.com/GetStock.com

Companies including Netflix and Virgin America have implemented "unlimited vacation" policies described as "Take what you want, take what you need." What type of organizational culture and employees are likely to be the best fit to adopt this approach? Do you think this will be a successful "HR experiment" for these organizations?"

Family-friendly Benefits and Services

As employers have recognized the importance of employees' need to balance their work and outside commitments including the care of family members, pursuit of education, personal development, and volunteer activities, many have implemented "family-friendly" HR practices. Options such as flextime and telework were discussed in Chapter 1. In addition, some organizations provide benefits and services including child and/or elder care, parental leave top-up, and adoption assistance. For example, Simon Fraser University provides maternity and parental leave top-up payments (up to 100 percent of salary for 35 weeks) and the National Energy Board provides new mothers a full year of maternity top-up payments (to 93 percent of salary) and adoptive parents and new fathers parental leave top-up to 93 percent of salary for 35 weeks.[47]

According to Statistics Canada, approximately 2.7 million Canadians provide unpaid care to people 65 years and older. Many of these people have been referred to as the *sandwich generation*—with dual responsibility of raising children and providing care for aging parents or relatives. Due to the aging of the Baby Boomers this segment is expected to grow, resulting in increased stress and demands on employees.[48] Some employers have responded by providing benefits and services including access to counselling, flexible schedules, referral services, and access to information and other resources available in the community or region.

Some companies even recognize that pets are "family" and provide employees with paid time off when they get a pet or are coping with the death of a pet. For example, at Shopper's Drug Mart employees can take paid days off if they have a loss in the family, and that includes a pet.[49] The value of family-friendly benefits accrues to not only employees but also employers in the form of increased productivity, enhanced commitment, and reduced stress.[50]

Other Benefits

The scope of possible employee benefits is limited only by the imagination of the organization's decision makers. Organizations have developed a wide variety of benefits to meet the needs of employees and to attract and keep the kinds of workers who will be of value to the organization.

To encourage learning and attract the kinds of employees who wish to develop their knowledge and skills, many organizations offer *tuition reimbursement* programs. A typical program covers tuition and related expenses for courses that are relevant to the employee's current job or future career at the organization. Employees are reimbursed for these expenses after they demonstrate they have completed an approved course. Tuition reimbursement is an important benefit at many organizations on top employer lists.

Selecting Employee Benefits

Although the government requires certain benefits, employers have wide latitude in creating the total benefits package they offer employees.[51] Decisions about which benefits to include should take into account the organization's goals, its budget, and the expectations of the organization's current employees and those it wishes to recruit in the future. Employees have come to expect certain things from employers. An organization that does not offer the expected benefits will have more difficulty attracting and keeping talented workers. Also, if employees believe their employer feels no commitment to their well-being and security, they are less likely to feel committed to their employer.

An Organization's Objectives

A logical place to begin selecting employee benefits is to establish objectives for the benefits package. This helps an organization select the most effective benefits and monitor whether the benefits are doing what they should. Unfortunately, research suggests that most organizations do not have written objectives for benefits.

Among companies that do set goals, the most common objectives include controlling the cost of health care benefits and retaining employees.[52] The first goal explains the growing use of wellness programs and employee-directed health plans. For the second goal, employers need to learn what employees care about. In some cases, the approach may be indirect, helping the company distinguish itself as an employer that certain kinds of employees will be attracted and committed to. A company that establishes itself as committed to the environment could offer benefits in line with that goal—say bicycle storage and vouchers for taking the bus to work.[53] For example, Sparkrock, a software development firm, encourages employees to commute via

HR Oops!

Protests at Tim Hortons after Cuts to Employee Benefits

Employees at a Cobourg, Ontario Tim Hortons, owned by the son and daughter of the chain's co-founders, say were told to "sign a document acknowledging they are losing paid breaks, paid benefits, and other incentives as a result of the province's minimum wage hike." "Breaks will no longer be paid. A 9 hour shift will be paid for 8 hours and 20 minutes." The document also stated that employees with six months to five years of service would have to pay 75 percent of the cost of their benefits. Employees with more than five years of service would have to pay 50 percent of the cost of benefits. An employee said that benefits had previously been "covered 100 percent by the company."

Public backlash was swift and included a social media boycott campaign, #NoTimmysTuesday, with rallies in 15 cities and towns organized by the Ontario Federation of Labour. Former Ontario Premier Kathleen Wynne called the franchisees' actions "a clear act of bullying." An official statement from Tim Hortons' corporate office stated, "These recent actions by a few restaurant owners. . . . do not reflect the values of our brand, the views of our company, or the views of the overwhelming majority of our hardworking restaurant owners."

Questions

1. Is it any surprise that employee benefits are important and highly valued by Tim Hortons employees? Explain your answer.
2. Suggest what the franchise owners could have done differently to provide an approach to employee total rewards that would be viewed as fair and reasonable for employees and other Tim Hortons franchise owners.

Source: Josie Kao, "Protests hit local Tim Hortons as franchises cut workers' benefits," *The Varsity,* January 15, 2018; "Demonstrators picket Time Hortons after cuts to employee benefits," *CBC News,* January 10, 2018, www.cbc.ca; Tara Deschamps and Shawn Jeffords, "'Reckless': Tim Hortons blasts franchisees' cuts to paid breaks and benefits," *Financial Post,* January 8, 2018, http://business.financialpost.com; Martha Porado and Ryan Murphy, "Benefits cuts by Tim Hortons franchises premature: NDP critic," *Benefits Canada,* January 5, 2018, www.benefitscanada.com; Aaron Saltzman, "Tim Hortons heirs cut paid breaks and worker benefits after minimum wage hike, employees say," *CBC News,* January 3, 2018, www.cbc.ca.

bicycle to its Toronto office by providing bike parking and a $5 per day incentive, as well as hosting seasonal tune-up clinics.[54]

Employees' Expectations and Values

Employees expect to receive benefits that are legally required and widely available, and they value benefits they are likely to use. To meet employee expectations about benefits, it can be helpful to see what other organizations offer. Employers should also consider that the value employees place on various benefits is likely to differ from one employee to another. As outlined earlier in the chapter, a basic demographic factor such as age can influence the kinds of benefits employees want. However, these are only general observations; organizations should check which considerations apply to their own employees and identify more specific needs and differences.

The choice of benefits may influence current employees' satisfaction and may also affect the organization's recruiting, in terms of both the ease of recruiting and the kinds of employees attracted to the organization. The HR Oops! box discusses the public relations fiasco faced by Tim Hortons when some franchisees cut valued employee benefits.

Flexible Benefits

Organizations can address differences in employees' needs and engage their employees by offering **flexible benefits plans** in place of a single benefits package for all employees. These plans, often called flexible benefits or *flex benefits,* offer employees a set of alternatives from which they can choose the types and amounts of benefits they want. The plans vary. Some impose minimum levels for certain benefits, such as health care coverage; some allow employees to receive money in exchange for choosing a "light" package; and some let employees pay extra for the privilege of receiving more benefits. For example, some plans let employees give up vacation days for more pay or to purchase extra vacation days in exchange for a reduction in pay.

flexible benefits plans Benefits plans that offer employees a set of alternatives from which they can choose the types and amounts of benefits they want.

Flexible benefits plans have a number of advantages.[55] The selection process can make employees more aware of the value of the benefits, particularly when the plan assigns each employee a sum of money to allocate to benefits. Also, the individual choice in a flexible benefits plan enables each employee to match their needs to the company's benefits, increasing the plan's actual value to the employee.

A drawback of flexible benefits plans is that they have a higher administrative cost, especially in the design and startup stages. Organizations can avoid some of the higher cost, however, by using software packages and standardized plans that have been developed for employers wishing to offer flexible benefits. Another possible drawback is that employee selection of benefits will increase rather than decrease costs, because employees will select the kinds of benefits they expect to need the most. For example, an employee expecting to need a lot of dental work is more likely to sign up for a dental plan. The heavy use of the dental coverage would then drive up the employer's premiums for that coverage. Costs can also be difficult to estimate when employees select their benefits. Organizations frequently respond by requiring employees to share in the costs of benefits.

LO5 Communicating Total Rewards to Employees

"Communication is often a weak link. An average program well-communicated will do better than an outstanding program poorly communicated."[56] A comprehensive communications strategy is required to help employees understand the total value the organization is investing in its approach to compensating and rewarding employees. This is essential so that total rewards can achieve their objectives including focusing employees on organizational goals, attracting and retaining employees, and creating a motivating environment.

Because they interact with their employees each day, managers play a significant role in communication. The HR department should prepare managers to explain to employees why the organization's approach to compensating and rewarding is designed as it is, and to determine whether employee concerns indicate a need for change. Employees are interested in their compensation and rewards and they need a great deal of detailed information. It follows that technology and supporting databases can play a significant role. More employers are using technology to provide employees with tools and information related to both communication and administration of employee compensation and rewards. Employees and job applicants often lack a clear sense of the market value of total rewards that an organization offers. For example, research asking employees about their benefits has shown that employees significantly underestimate the cost and value of their benefits.[57]

Employers have many options for communicating information about their total rewards. Research from Sun Life showed that different generational groups have different preferences for receiving information from their employers about rewards—Baby Boomers are most likely to prefer paper-based communications, Gen X appreciates online communication, and Millennials prefer online

Did You KNOW?

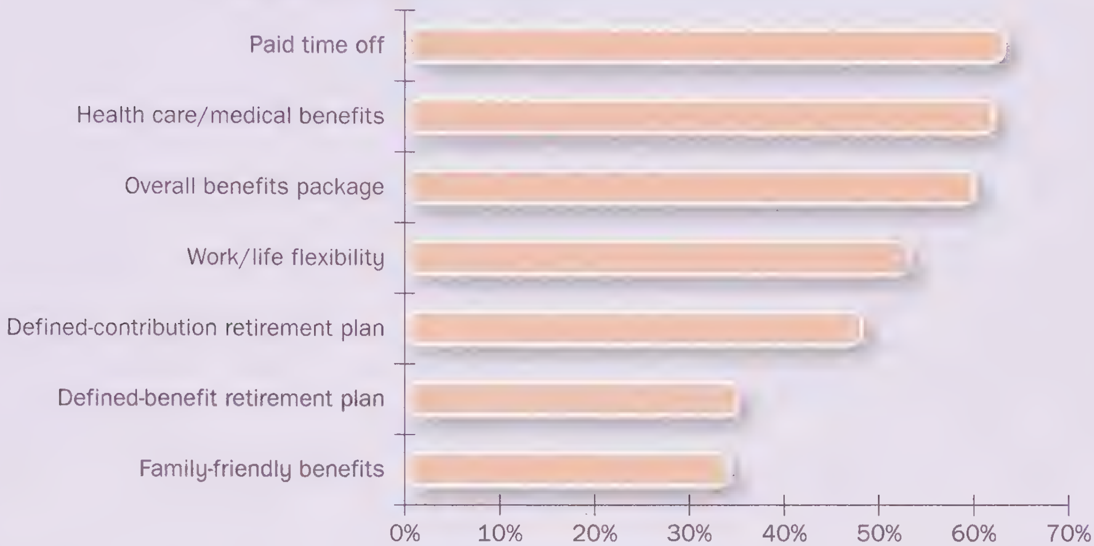
Benefits Are Important to Employees

The Society for Human Resource Management has found that benefits consistently ranked in the top five contributors to employees' job satisfaction.

Question

How does the data shown here support the view that HR managers should actively communicate with employees about their benefits?

Employees Rating Benefit Important or Very Important



Sources: Society for Human Resource Management, *Employee Job Satisfaction and Engagement: Revitalizing a Changing Workforce,* April 2016, http://www.shrm.org; Debra Cohen, "Employee Engagement," *People and Strategy* 36, no. 4 (2014): 13–14; Frank Giancola, "How Important Are Benefit Plans to Your Employees and How Satisfied Are They with Your Offerings?" *Employee Benefit Plan Review,* July 2013, pp. 27–30.

communication to anything else.[58] To increase the likelihood that employees will receive and understand the messages, employers can combine several media, such as videos, brochures, question-and-answer meetings, intranet site, memos, presentations, email and messaging applications.

Communication efforts are also moving beyond ensuring employees receive and understand the messages to "driving action, enabling employees to make the best possible use of the programs available to them," according to Diane McElroy, a senior vice-president with Aon Hewitt in Toronto. McElroy adds that some employers provide *total rewards statements* for prospective employees as part of the job offer. "Some organizations are providing these statements when they make offers to job candidates. That way, if the potential new hire receives another offer—especially one with a higher base salary—he or she can make an informed comparison and determine whether a bigger paycheque really does mean great compensation."[59] In summary, an investment of creativity in employee communication can reap great returns in the form of committed, satisfied employees, and the achievement of organizational objectives including employee attraction and retention.

Executive Compensation and Rewards

Pay for Executives

The media have drawn public attention to the issue of executive compensation and rewards. The issue attracts notice because of the very high pay that the top executives of major North American companies have received in recent years; see Table 8.3 for Canada's highest-paid executives. In 2016, the average CEO total compensation of Canada's top 100 highest paid executives was $10.4 million.[60]

Notice also that as shown in Figure 8.11, only a small share of the average compensation paid to CEOs is in the form of a salary. Most CEO compensation takes the form of performance-related pay, such as bonuses and stock. This variable pay causes the pay of executives to vary much more widely than other employees earnings.

Although these high amounts apply to only a small proportion of the total workforce, the issue of executive pay is relevant to pay structure in terms of equity theory. As we discussed earlier in the chapter, employees draw conclusions about the fairness of pay by making comparisons among employees' inputs and outcomes. By many comparisons, Canadian CEOs' pay is high. The Canadian Centre for Policy Alternatives, a public policy think tank, reported that in 2016, Canada's 100 highest-paid CEOs received 209 times the annual earnings of an average Canadian, up from 105 times the average Canadian worker's wage in 1998. In 2016, Canadian workers earned an average wage of $49,738.[61] For example, by 10.57 a.m. on January 2, 2016, the first working day of the year, the average top CEO had already earned as much as the average Canadian worker made in the entire year.[62]

However, to assess the overall fairness of this ratio, equity theory would consider not only the size of executive pay relative to other employees but also the amount the CEOs contribute. CEOs likely have a much greater effect on the organization's performance than the average employee. But if they do not seem to contribute 209 times more, employees may see the compensation as unfair. However, according to Carleton University professor Ian Lee, CEO "compensation is justified and shouldn't be compared to an average worker's salary." Lee explains that top players in sports, entertainment, and business always make more than the average person because "they offer rare and sought-after talent."[63]

Executive Incentives and Benefits

Assuming that incentives influence performance, decisions about incentives for executives should have a great impact on how well the executives and the organization perform. Along with overall pay levels for executives, organizations need to create incentive plans for this small but important group of employees. CEO pay is increasingly moving away from a salary to total compensation based primarily on incentives. For example, in 2008, the average top Canadian CEO received 14 percent of total compensation in salary. However, in 2016, as shown in Figure 8.11 salary represented only 11 percent of total compensation.[64]

To encourage executives to develop a commitment to the organization's long-term success, executive compensation often combines short-term and long-term

TABLE 8.3

Canada's Highest Paid CEOs (2016)

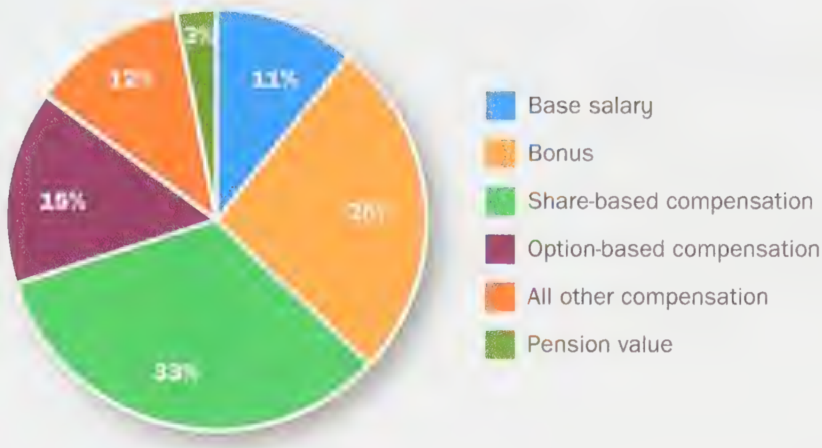
Rank	Company	Title	Name	Base Salary	Other Compensation†	Total Compensation
1	Valeant Pharmaceuticals International Inc	CEO	Joseph Papa*	$1,299,990	$81,831,262	$83,131,252
2	Magna International Inc	CEO	Donald Walker*	$430,781	$28,183,681	$28,614,462
3	Rogers Communications Inc	Former President & CEO	Guy Laurence	$1,029,711	$23,573,282	$24,602,993
4	Macdonald Dettwiler & Associates Ltd	Former President & CEO	Daniel Friedmann	$266,831	$21,160,422	$21,427,253
5	Canadian Pacific Railway Ltd	CEO	Hunter Harrison	$2,904,595	$15,925,199	$18,829,794

† Other Compensation includes: cash bonuses, stock-based bonuses, options-based bonuses, pension value, and any other payments other than base salary.

Sources: David Macdonald, "Climbing Up and Kicking Down: Executive Pay in Canada," *Canadian Centre for Policy Alternatives,* January 1, 2018, p 17; and CB Staff, "Canada's Top 100 highest-paid CEOs," Canadian Business, January 2, 2018, www.canadianbusiness.com.

FIGURE 8.11

Breakdown of CEO Pay



Source: David Macdonald, "Climbing Up and Kicking Down: Executive Pay in Canada," Figure 2, *Canadian Centre for Policy Alternatives,* January 1, 2018, p 10. Copied under licence from Access Copyright. Further reproduction, distribution or transmission is prohibited except as otherwise permitted by law.

incentives. *Short-term incentives* include bonuses based on the year's profits, return on investment, or other measures related to the organization's goals. Sometimes, to gain tax advantages, the actual payment of the bonus is deferred (e.g., by making it part of a retirement plan). *Long-term incentives* include stock options and stock purchase plans. The rationale for these long-term incentives is that executives will want to do what is best for the organization because that will cause the value of their stock to grow. A corporation's shareholders—its owners—want the corporation to encourage managers to act in the owners' best interests. They want managers to care about the company's profits and stock price, and incentive pay can encourage this interest. One study has found that relying on such long-term incentives is associated with greater profitability.[65]

As well as legally required benefits and the benefits extended to other employees in the organization, executives often receive extra benefits and services. These executive benefits and services may include such far-reaching benefits as use of corporate aircraft, company-provided or subsidized homes, memberships and tickets to sporting and cultural events, in addition to benefits such as company vehicles, sabbaticals, and extended vacations.

Performance Measures for Executives

The balanced scorecard approach discussed in Chapter 7 is also useful in designing executive pay. Table 8.5 shows how the choice of performance measures can be guided by a desire to balance shareholder, customer, and employee objectives. Financial results can be seen as a lagging indicator that tells the company how it has done in the past, whereas customer and employee metrics like those in Table 8.5, used by the global biopharmaceutical company Merck, are leading indicators that tell the company how its financial results will be in the future.

TABLE 8.5

Merck Performance (Balanced) Scorecard—CEO

Financial 1. Revenue vs. plan 2. Earnings per share vs. plan 3. Value of growth (e.g., ROI vs. plan)	60
Customer 1. Merck customer service level (% orders delivered on time) 2. Merck Trust & Value Customer Survey	14
Key Business Drivers 1. Cost structure (operating expense vs. plan) 2. Revenue growth in high-priority areas	16
Culture (high performance, sustainable) 1. Employee Culture Survey	10
Total	100

Source: Proxy Statement, Merck & Co., Inc., April 14, 2014, www.merck.com/finance/proxy/pr2014.pdf.

Thinking Ethically

Volkswagen Changes How It Pays

Volkswagen (VW) has an integrity problem. Volkswagen was discovered to have installed software that sensed when an engine was being tested for emissions and (temporarily) reduced emissions to a level that would pass the test. In actual driving conditions, however, VW diesel engines emitted emissions up to 40 times the legal limit. VW's marketing campaign had emphasized the wonder of the diesel engine's performance combined with environmental benefits, even though it was not true. That campaign in turn was a vital part of VW's Strategy 2018 growth plan to bypass General Motors and Toyota to become the world's largest automaker. Employees were subjected to tremendous pressure and intimidation from the top cascading down to every level to do whatever was necessary to achieve this growth goal (and keep their jobs). This apparently included engineers "willing to commit crimes to defraud the public."

As a result of this scandal, multiple legal actions have been brought against the company. VW has entered into settlements of civil lawsuits brought by drivers who found themselves stuck with noncompliant vehicles. This includes the largest class action settlement ever. The company has also paid criminal fines that together total nearly $25 billion (so far).

In an effort to avoid such problems in the future and to "quell investor ire" that executives earned large bonuses (despite their role in the scandal and large VW losses), the company is changing the way it pays. No bonuses will be paid in the future if certain financial objectives are not met. Base salary will be increased 30 percent, but the total amount of base salary plus bonus that an executive can receive will now be capped at $10 million for the CEO and $5.5 million for other board members. Also, for the first time, executives will be given company stock, presumably in an effort to better align their interests with those of shareholders. It appears that this stock-based compensation is not subject to the caps. Thus, if shareholders do well, executives can still do quite well.

Questions

1. What caused the Volkswagen scandal? What can you infer about the nature of its former pay strategy and the role it may have played?
2. Consider Volkswagen's revised pay strategy. How well do you think it will succeed going forward? Do you have suggestions for other changes? Explain.

Sources: W. Boston, "VW Revamps Pay, Imposes Caps," *Wall Street Journal,* February 25/26, 2017; S. Randazzo, "U.S. Court Gives Initial Approval to Volkswagen Vehicle Emissions Settlement," *Wall Street Journal,* February 14, 2017; J. Rothfeder, "The Volkswagen Settlement: How Bad Management Leads to Big Punishment," *The New Yorker,* July 1, 2016

SUMMARY

LO1 Discuss how organizations implement a "total rewards" approach to compensating and rewarding employees.

Many organizations are recognizing the strategic value of taking a comprehensive approach to compensating and rewarding employees. This "total rewards" approach frequently involves creating a value proposition for current and prospective employees that clearly identifies all of the aspects that are valued by employees in exchange for their time and expertise. Companies take a total rewards approach to attract and retain valued employees and improve capacity to meet organizational goals.

LO2 Identify the kinds of decisions and influences involved in providing base pay to employees.

Organizations make decisions to define a job structure or relative pay for different jobs within the organization. Organizations must also establish pay levels, based on the organization's goals, market data, legal requirements, and principles of fairness. Together job structure and pay level establish a pay structure policy. Organizations typically begin with a job evaluation to measure the relative worth of their jobs. To obtain more flexibility, organizations may reduce the levels in the organization's job structure. Other organizations reward employees according to their competencies.

LO3 Describe how organizations recognize individual, team, and organizational performance with incentives.

Organizations may recognize individual performance through incentives such as piecework rates, standard hours plans, merit pay, sales commissions, and bonuses for meeting individual performance objectives. Common team incentives include gainsharing, bonuses, and team awards. Incentives for meeting organizational objectives include profit sharing and stock ownership.

LO4 Summarize the role of employee benefits and the types of benefits offered by employers.

Like pay, benefits and services help employers attract, retain, and provide a source of motivation for employees. Employees expect at least a minimum level of benefits, and providing more than the minimum helps an organization compete in the labour market. Benefits and services are also a significant expense, but employers provide benefits and services because employees value them and many are required by law.

LO5 Review the importance of effectively communicating the organization's approach to total rewards.

A comprehensive communications strategy is needed to help employees understand and value all the components in an organization's approach to total rewards. Managers and the human resource department share responsibility for this important requirement. Technology can provide employees access to information and other tools associated with administration of compensation and rewards. Employers have many options for communicating information about total rewards.

LO6 Examine issues related to compensating and rewarding executives.

Executive compensation has drawn public scrutiny because top executive compensation is much higher than the average worker's pay. Executive compensation is complicated, contains a variety of elements, and is increasingly based on incentives rather than base salary.

CRITICAL THINKING QUESTIONS

1. Some individuals evaluate prospective employers' job offers based only on direct pay considerations. What additional factors should be considered when evaluating job offers from employers?
2. Why might an organization choose to pay employees more than the market rate? Why might it choose to pay less? What are the consequences of paying more or less than the market rate?
3. What are the advantages of establishing pay ranges, rather than specific pay levels, for each job? What are the drawbacks of this approach?
4. Suppose a small start-up business wants to establish a competency-based pay structure. What would be some advantages of this approach? List the issues the company should be prepared to address in setting up this system. Consider the kinds of information needed and the ways employees may react to the new pay structure.
5. With some organizations and jobs, pay is primarily wages or salaries, and with others, incentive pay is more important. For each of the following jobs, state whether you think the pay should emphasize base pay (wages and salaries) or incentive pay (bonuses, profit sharing, and so on). Give a reason for each.
   a. An accountant at a manufacturing company
   b. A salesperson for a software company
   c. A mechanic for a major airline
   d. A marketing manager for a communications company
   e. A recruitment specialist for the federal government
6. Why do some organizations link incentive pay to the organization's overall performance? Is it appropriate to use stock performance as an incentive for employees at all levels? Why or why not?
7. Why do employers provide benefits, rather than providing all employee compensation in the form of pay and letting employees buy the benefits they want?
8. Of the benefits discussed in this chapter, list the ones you consider essential—those benefits you would require in any job offer. Why are these benefits important to you?
9. Why is it important to communicate information about total rewards? Suppose you work in the HR department of a company that has decided to add employee financial wellness counselling services to its total rewards. How would you recommend communicating this change? What information should your messages include? How would you know if your communication strategy was successful?
10. Do you think executive total compensation is too high? Why or why not?

EXPERIENCING HR—HOW TO ASSESS ROI OF A WELLNESS PROGRAM

Form groups of four or five. (Alternatively, your instructor may ask students to complete the research independently and discuss their findings in class.) You have been asked by your manager to be part of a workplace task force that will examine how to assess the return on investment (ROI) of a corporate wellness program.

Conduct research using recent academic (e.g., *ACSM's Health & Fitness Journal*) *and* HR practitioner publications (e.g., *Benefits Canada*) *and* credible websites (e.g., the website for the Canadian Centre for Occupational Health and Safety. Discuss your findings about how to determine the ROI of a corporate wellness program. Write a one-page report or make a brief class presentation summarizing your findings.

CASE STUDY: EVIDENCE-BASED HRM

Improving the Quality and Reducing the Cost of Employee Health Benefits

The new Health Transformation Alliance, a collaboration of 38 companies employing 6 million workers (including American Express and Johnson & Johnson) will use data and technology to improve the quality and reduce the cost of health benefits for its employees. The Alliance hopes to save as much as $600 million on drug spending, representing a reduction of approximately 15 percent. Part of the savings comes from the Alliance's bargaining power. However, another part of the plan is to change how care is delivered for conditions like diabetes, hip and knee replacements, and lower back pain.

IBM's Watson software will be used to "help" select drugs that provide the best value for the money and to predict which employees are most likely to develop conditions such as diabetes so as to take preventive action sooner. To perform these analyses, the goal is to use four years of data on pharmacy and insurance claims and electronic employee health records from each company.

Other companies are taking similar steps, sometimes focusing on particular issues that are most critical to them. For example, engine maker Cummins, Inc. is devoting considerable attention to the misuse of prescription opioid painkillers and is working to find alternative pain control methods for employees. Cummins notes the need for caution as most pain medication is legally prescribed and control of pain is critical. At the same time, use of such medication raises safety issues on the job and also can imperil employees' long-term health. According to one estimate, annual medical expenses for opioid abusers are about twice as high as the employer cost for other employees. Cummins relies on programs that use drug-test data and works with a pharmacy-benefits manager to track data on opioid prescriptions and attempts to detect pill shopping. The company recently opened a new facility at its headquarters that provides services such as massage, acupuncture, physical therapy, and a full-time pharmacist, all in the interest of finding better and safer ways to control pain. Cummins has also trained supervisors on how to identify employees who may be having problems with painkillers and has trained plant managers on how to triage employees having an overdose.

Questions

1. As an employee, what would your reaction be to these initiatives? Explain.
2. Do you have ideas for other ways to use data to improve the cost effectiveness and quality of health-related employee benefits?

Sources: J. Walker, "Alliance of Companies Unveil First Steps Aimed at Cutting Health-Care Costs," *Wall Street Journal*, March 7, 2017; R. E. Silverman, "One Employer Fights against Prescription-Drug Abuse," *Wall Street Journal*, November 15, 2016.

CASE STUDY: HRM SOCIAL

Bell Gets Social to Get Healthy

One of the big challenges with a wellness program is motivation—especially motivating the employees who would benefit the most. Typically, many employees never complete the health assessment used for entering these programs and then even fewer sign up for activities that would improve the health issues identified in the assessment. An important consideration is that wellness programs work best when they are part of an integrated strategy that combines realistic goals with incentives, clear communication, and a supportive culture.

Some of that education and support can come through social media tools. The knowledge-sharing function of social media readily lends itself to educating employees about health. For example, the employer could feature healthy items on the cafeteria menu each week or a page to share ideas for managing stress or working exercise into one's daily routine.

In the area of support, just as employees might use the company's computer network to find colleagues with knowledge, the company could set up web pages or a Twitter feed for groups with health-related interests such as a group that walks during lunch breaks or a weight-loss challenge group. While the company cannot disclose personal health information, it could reward team successes. For example, employees could form teams and see which team logs the most steps during a challenge period.

Bell has a walking challenge that starts during the company's mental health week in May. Marie-Josée Boivin, vice-president of human resources describes the initiative: "So our employees could either join a team or create a team, but for a full month, people were counting their steps and we were encouraging them to go out for a walk, to walk as colleagues and so on. It was a way to say it's good to keep an active lifestyle, and we also linked it to mental health, because if you're healthier up here, if you take time to relax at lunch time, at the end of the day and so on, then you have a better lifestyle."

As part of the challenge, Bell has an internal website where employees taking part can post about themselves, write comments, and compete with one another, says Boivin. " . . . In HR, we had two teams and, I have to admit, we had a very nice, happy competition going on. I think it brought a lot of the team together. We even had people writing on the wall that they ended up connecting with people they didn't know through that challenge. So they created walking groups."

Questions

1. Would you expect participation in wellness programs to be greater if they have a social media component? Why or why not?
2. How might the ideas described here be applied to a stop-smoking program for an organization's employees?

Sources: Ryan Murphy, "Bell walks toward wellness," *Benefits Canada*, April 23, 2018, www.benefitscanada.ca, accessed May 23, 2018; Stephen Walkiewicz, "Don't Go It Alone: Social Media Can Help You Quite Smoking," *Men's Fitness*, http://www.mensfitness.com, accessed June 8, 2016; Lindsay Rothfeld, "7 Companies with Amazingly Unique Wellness Programs," *Mashable*, May 5, 2015, http://mashable.com; Barb Hendrickson, "Increasing Employee Participation in Corporate Wellness Programs," *Occupational Health and Safety*, September 1, 2013, http://ohsonline.com; David Roddenberry, "Six Keys to Maximize the Value of Wellness Incentive Programs," *EHS Today*, February 2013, pp. 37–38.

PART 5

Meeting Other HR Goals

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