Developing a Pay Policy Plan

An effective pay policy is an important aspect of a company’s overall competitive strategy. Just as organizations compete to sell their products and services, they also compete with one another for talented employees. Toward that end, a competitive pay policy is the cornerstone of an organization’s human capital investment strategy.

How a company competes depends on three recruiting market conditions:

- The extent to which qualified employees are available in targeted recruiting markets.
- The aggressiveness of other employers competing within those same recruiting markets.
- The company’s clout in the marketplace to recruit qualified employees (e.g., financial resources to pay employees, perception of the company as an employer of choice, etc.).

A competitive pay policy addresses these three market conditions. It articulates the company’s strategic position for competing within its recruiting markets in terms of the pay elements it will offer employees and the pay levels it will target for each element. The policy sets forth the principles that guide design, implementation, and administration of the company’s compensation program.

Types
The organization’s strategy toward the labor market requires a salary-level policy decision which involves determining how competitive the organization wishes to be. There are three common organization pay policies:

- Lag the market
- Lead-lag
- Lead the market

Inputs
In order to determine the appropriate organization pay policy, you must establish the pay policy line. This is developed based upon a holistic assessment of internal factors (such as current pay rates and job relationships) and external factors (such as the labor market, industry trends, and laws).
**Internal Job Relationships**
Start by evaluating all the jobs in your organization. Determine which jobs represent most of the total labor costs, since policy changes that directly affect these jobs may significantly impact the bottom line and largely determine the competitive salary level of the organization. Salary relationships are built around these labor costs.

**Current Market Rates**
Once the jobs are evaluated, market rates are relied upon to determine the competitiveness of the current salary levels in the organization.

**Pay-Policy Line**
Now you can define a pay-policy line by plotting points reflecting the jobs in your organizations based on two dimensions: compensation value and a job ranking (or job evaluation result).

This framework will enable an employer to develop a competitive pay strategy relative to overall total rewards and HR strategy. Organizations looking to compete effectively need to keep their HR and related programs aligned with business objectives. If you need support in determining current market rates for positions or need an overall resource to develop your pay policy, ERA’s Compensation Services are available by contacting Monique Kahkonen at 513-679-4120 or mkahkonen@hrxperts.org.