Strategic Compensation (Canadian) 1st edition Martocchio Solutions Manual

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INSTRUCTOR'S MANUAL

Strategic Compensation:

A Human Resources Management Approach

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CHAPTER 1

Strategic Compensation: A Component of Human Resources Management Systems

Preface

Chapter one introduces students to the history and foundation of strategic compensation. In particular, this chapter explains compensation, strategic compensation, and the profession of compensation and role of the strategic business partner. This chapter continues to explore compensation in the broader organizational and human resources management contexts.

Learning Objectives

1-1. Define strategic compensation.

1-2. Summarize the role of compensation as a strategic business partner.

1-3. Explain strategic compensation decisions.

1-4. Identify and discuss the building blocks and structural elements of strategic compensation systems.

1-5. Describe the fit of the compensation function in organizations.

1-6. Identify the stakeholders of the compensation function and summarize their stakes in the work compensation professionals perform.

Outline/Table of Contents

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Lecture Outline/Syllabus

I. Overview

A. Manpower planning
   1. Predecessor to contemporary human resources management (HRM), focus was on effective deployment of employees, now called workforce planning or human resources planning
   2. Goal was to achieve maximum productivity per employee

B. Personnel management
   1. Evolved due to government regulations concerning:
      a. Payroll taxes
      b. Minimum wage laws
      c. Equal pay for equal work and employment equity
   2. Competitive advantage
      a. Since 1980's recognition that employees can contribute to competitive advantage
      b. Competitive advantage describes an organization's success when the organization acquires or develops capabilities that facilitate outperforming the competition
      c. HRM becomes a strategic function

II. Defining Strategic Compensation

A. What Is Compensation?
   1. Intrinsic and extrinsic rewards employees receive for performing their jobs
      a. Intrinsic compensation: reflects employees' psychological mindsets that result from performing their jobs
      b. Extrinsic compensation: includes both monetary and nonmonetary rewards for:
         i. Obtaining certain job performance levels
         ii. Acquiring new skills and knowledge
   2. Monetary compensation represents core compensation
   3. Nonmonetary rewards (also known as employee benefits) include:
      a. Protection programs (e.g., medical insurance)
      b. Paid time off (e.g., vacations)
      c. Services (e.g., daycare assistance)

B. What is Strategic Compensation?
   1. Competitive business strategy refers to the planned use of organization resources
   2. Human resources management strategies specify the use of multiple HRM practices to reinforce competitive business strategy.

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3. Strategic compensation refers to the design and implementation of compensation systems to reinforce the objectives of both HRM strategies and competitive business strategies.

III. The Transformation of HRM into a Strategic Business Partner

A. HRM and compensation professionals today need to think like the chief executive officer (CEO) to become a strategic partner in achieving organizational plans and results

B. Compensation professionals can give the CEO and CFO an understanding of the roles employees play in the organizations to expand or shrink shareholder value

C. How HRM functions serve as strategic business partner

1. Capital refers to factors that enable companies to generate income, raise stock prices, bring economic value, strong brand identity, and reputation
2. Human capital, refers to sets of collective skills, knowledge, and abilities that employees can apply to create value for their employers
3. Compensation professionals can leverage the value of human capital in a variety of ways such as a well-designed merit pay program to reinforce performance

IV. Strategic Compensation Decisions Explained

A. Environmental scanning

1. Used for strategy formulation
2. Main focus is discerning threats and opportunities

B. Competitive business strategy choices

1. Lowest-cost strategy or cost leadership focuses on gaining completive advantage by being the lowest-cost producer of a product or service within the marketplace
2. Differentiation strategies develop products or services that are unique from those of their competitors

C. Compensation decisions that support the firm's strategy

1. Compensation professionals use two broad elements to support strategic initiatives
    a. Basic building blocks
    b. Structural design elements
2. Employee roles associated with competitive strategies
    a. Compensation professionals must design and implement compensation practices that elicit strategy-consistent employee roles

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V. Building Blocks and Structure of Strategic Compensation Systems

A. Building blocks: Core compensation and Employee Benefits

1. Core compensation

a. Base pay includes hourly pay or wage or salary

b. Is governed by the provincial and territorial employment standards

c. Is set according to compensable factors such as level of skill, effort, and responsibility required to perform the job and the severity of the working conditions

i. Compensable factors are used to determine if jobs are equal within equal pay for equal work in the provincial and territorial employment standards and pay equity

d. Is adjusted periodically for cost-of-living allowance (COLA) increases, differences in an employee's job performance, and increases in an employee's skill level or job knowledge

e. Seniority pay systems reward employees with periodic additions to base pay according to employees' length of service in performing their jobs

i. Designed according to the human capital theory: employees will become more productive as they refine existing skills and acquire new skills and knowledge through length of service

f. Merit pay is permanent base pay increases granted because of job performance

g. Incentive pay or variable pay rewards employees for partially or completely attaining a pre-determined work objective

h. Person-focused pay or competency-based pay rewards employee for specifically learning new curricula

i. Pay-for-knowledge plans reward managerial, service, or professional workers for successfully learning specific curricula

ii. Skill-based pay is used mostly for employees who perform physical work and increases as workers master new skills

2. Employee Benefits

a. Represent nonmonetary rewards

b. Discretionary benefits include three broad categories

i. Protection programs that provide social insurance in the form of family benefits, promote health, and guard against income loss caused by factors such as unemployment, disability, or serious illness

ii. Paid time off such as vacation

iii. Services provide such enhancements as tuition reimbursement and day care assistance

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c. Government mandated benefits that attempt to promote worker safety and health and maintain family income streams
    i. Canada and Quebec Pension plans
    ii. Employment Insurance
    iii. Workers' Compensation

B. Fundamental Compensation System Design Elements
1. Internal consistency
    a. Internally consistent compensation systems clearly define the relative value of each job among all the jobs within an organization
    b. Is based on the principle that employees working at jobs that require greater qualifications, more responsibilities, and/or more complex job duties should be paid more
    c. Is achieved using job analysis and job evaluation
        i. Job analysis is a systematic process for gathering, documenting, and analyzing information in order to describe jobs
        ii. Job evaluation is used to systematically recognize differences in the relative worth among a set of jobs
2. Market competitiveness
    a. Market-competitive pay systems are based on results of compensation surveys
    b. Compensation surveys collect and then analyze competitors compensation data
3. Recognizing Individual Contributions
    a. Pay structures recognize differences in employee contributions, such as credentials, job knowledge, and job performance
    b. Pay grades group jobs for pay policy application
    c. Pay ranges include minimum, maximum, and midpoint pay rates

C. Alternative Pay Structure Configurations
1. Merit pay plans
2. Sales compensation plans
3. Broadband structures
4. Two-tier wage structures
5. Executive compensation
6. Contingent worker compensation
7. Expatriate compensation
8. Pay and benefits outside Canada

VI. Fitting the Compensation Function in an Organization's Structure

A. How HRM Professionals Fit into the Corporate Hierarchy

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1. Line employees are workers who are directly involved in producing a organization's goods or services
2. Staff employees are workers whose job it is to support the line functions- human resources management professionals are staff employees
3. HRM practices include:
    a. Recruitment
    b. Selection
    c. Performance appraisal
    d. Training
    e. Career development
    f. Labour-management relations
    g. Employment termination
    h. Managing HRM within the context of legislation

B. The Compensation Function
    1. An executive is a top-level manager who reports directly to the corporation's CEO or to the head of a major division
    2. A generalist, who may be an executive, performs tasks in a variety of HRM-related areas
    3. A specialist may be an HRM executive, manager, or non-manager who is typically concerned with only one of the areas of compensation practice

C. How the Compensation Function Fits into HRM Departments
    1. Compensation, recruitment, and selection
        a. Companies can spark interest by communicating the positive features of the core compensation and employee benefits programs
        b. Companies may offer inducements such as signing bonuses
    2. Compensation and performance appraisal
        a. Is key to effective merit pay programs
        b. Employees must perceive a strong relationship between attaining performance standards and receiving pay increases
    3. Compensation and training
        a. Successful pay-for-knowledge plans depend upon an organization's ability to develop and implement systematic training programs
        b. Companies implementing pay-for-knowledge plans typically increase the amount of classroom and on-the-job training
    4. Compensation and career development
        a. Employees make lateral moves across an organization's hierarchy or vertical moves up the hierarchy
        b. Employees compensation changes reflect career development

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5. Compensation and labour-management relations
    a. Companies grant COLAs
    b. Companies establish base pay on seniority pay
6. Compensation and employment termination
    a. Employment terminations are either involuntary or voluntary
    b. Some companies offer severance pay for involuntary terminations
    c. Companies sponsor pension programs in the case of retirement
    d. Companies sometimes use early retirement programs to reduce workforce size
7. Compensation and legislation
    a. Laws were enacted to establish acceptable employment practices and protect employees' rights
    b. Are grouped on four main themes
        i. Income continuity, safety, and work hours
        ii. Pay discrimination
        iii. Accommodation of disabilities and family needs
        iv. Prevailing wage laws
    c. Relevant laws include:
        i. Income continuity, safety, and work hours
        ii. Pay discrimination
        iii. Medical care and the accommodation of disabilities and family needs
        iv. Prevailing wage laws

VII. Stakeholders of the Compensation System

A. The success of HRM departments depends on how they will serve various stakeholders including:
    1. Employees
    2. Line managers
    3. Executives
    4. Unions
    5. Provincial, territorial, and federal governments
B. Employees
    1. Must educate employees on training options and connections between training and their pay
    2. Must determine which objectives of discretionary benefits are most important to their particular workforce
C. Line managers
    1. Use their knowledge of relevant laws to help them make sound compensation judgments

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2. Advise them on establishing pay rates

E. Executives
   1. Develop and manage sound compensation systems

F. Unions
   1. Abide by their collective bargaining agreements

G. Canadian Government
   1. Keep updated and comply with all employment relevant legislation
   2. Demonstrate that alleged discriminatory pay practices are not discriminatory

End of the Chapter

VIII. Key Terms

Competitive advantage: Describes an organization's success when the organization acquires or develops capabilities that facilitate outperforming the competition

Intrinsic compensation: Reflects employees' psychological mind-sets that result from performing their jobs

Extrinsic compensation: Includes both monetary and nonmonetary rewards

Core compensation: Monetary compensation

Employee benefits: Non-monetary compensation

Competitive business strategy: The planned use of organization resources—financial capital, equipment capital, and human capital— to promote and sustain competitive advantage

Human resources management strategies: Specify the use of multiple HRM practices to reinforce competitive business strategy

Strategic compensation: Refers to the design and implementation of compensation systems to reinforce the objectives of both HRM strategies and competitive business strategies

Capital: Refers to the factors that enable companies to generate income, higher organization stock prices, economic value, strong positive brand identity, and reputation

Human capital: Refers to sets of collective skills, knowledge, and abilities that employees can apply to create value for their employers

Environmental scanning is a task to decern external threats and opportunities and internal organizational strengths and weaknesses

Cost leadership (lowest-cost strategy): Focuses on gaining competitive advantage by being the lowest-cost producer of a product or service within the marketplace, while selling the product or service at a price advantage relative to the industry average

Differentiation strategies: Companies adopt this strategy when they develop products or services that are unique from those of their competitors

Base pay: Recurring money employees receive for doing their jobs

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Hourly pay ~~or wage:~~ Base pay received for each hour worked

Wage is one type of pay. Employees earn hourly pay for each hour worked

Salary: Base pay received for performing a job, regardless of the actual number of hours worked

Compensable factors: Skill, effort, responsibility, and working condition factors

Cost-of-living adjustment (COLAs): Represent periodic base pay increases that are founded on changes in prices as recorded by the Consumer Price Index (CPI)

Seniority pay: A system to reward employees with periodic additions to base pay according to employees' length of service in performing their jobs

Human capital theory: Employees' knowledge and skills (human capital) add value

Merit pay programs: Program that assumes that employees' compensation over time should be determined, at least in part, by differences in job performance as judged by supervisors or managers

Incentive pay: Compensation (other than base wages or salaries) that fluctuates according to employees' attainment of some standard based on a pre-established formula, individual or group goals, or organization earnings

Variable pay: Compensation (other than base wages or salaries) that fluctuates according to employees' attainment of some standard based on a pre-established formula, individual or group goals, or organization earnings

Person-focused pay: Programs that reward employees for specifically learning new curricula

Pay-for-knowledge: Programs that reward managerial, service, or professional workers for successfully learning specific curricula

Skill-based pay: Programs that increase workers' pay as they master new skills

Government-mandated benefits are protection programs that attempt to promote worker safety and health, maintain family income streams, and assist families in crisis. The key government-mandated by the following laws: the Social Security Act of 1935, various state workers' compensation laws, the Family Medical Leave Act of 1993, and the Patient Protection and Affordable Care Act of 2010

Paid time off: Provides employees with pay for time when they are not working (e.g., vacation)

Services: Provide such enhancements as tuition reimbursement and day care assistance to employees and their families

Protection programs: Legally required benefits that attempt to promote worker safety and health, maintain the influx of family income, and assist families in crisis

Internally consistent compensation systems: Clearly define the relative value of each job among all jobs within an organization

Job analysis: A systematic process for gathering, documenting, and analyzing information in order to describe jobs

Job evaluation: A process to recognize differences in the relative worth among a set of jobs and to establish pay differentials accordingly

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Market-competitive pay systems: Compensation professionals build market-competitive compensation systems based on the results of compensation surveys

Compensation surveys: Collect and then analyze competitors' compensation data

Pay structures: Represent pay rate differences for jobs of unequal worth and the framework for recognizing differences in employee contributions

Pay grades: Group jobs for pay policy application

Pay ranges: Include minimum, maximum, and midpoint pay rates

Line employees: Employees that are directly involved in producing companies' goods or delivering their services

Staff employees: Employees that support the line functions

Executive is a top-level manager who reports directly to the coporation's CEO or to the head of a major division

Severance pay: Companies may choose to award and amount, usually the equivalent of several months' pay following involuntary termination

Pension programs: Provide income to individuals throughout their retirement

Early retirement programs: Contain incentives designed to encourage highly paid employees with substantial seniority to retire earlier than they had planned

Generalist: A human resource professional that may be an executive that performs tasks in a variety of HRM related areas

Specialist An HRM executive, manager, or non-manager who is typically concerned with only one of the areas of compensation practice

IX. Discussion Questions and Suggested Answers

1-1. Define strategic compensation.

Compensation represents both the intrinsic and extrinsic rewards employees receive for performing their jobs. Together, both intrinsic and extrinsic compensation describes a organization's total compensation level. Intrinsic compensation reflects an employee's psychological mindsets that result from performing his or her job. Extrinsic compensation includes both monetary and nonmonetary rewards.

Learning Objective: 1-1. Define strategic compensation.

1-2. Identify two organizations—one that you believe pursues a lowest-cost strategy and another that pursues a differentiation strategy. Relying on personal knowledge, company annual reports, or articles in newspapers and business periodicals, or credible online sources, discuss these companies' competitive strategies. How might compensation professionals contribute to these objectives?

The cost leadership or lowest-cost strategy focuses on gaining competitive advantage by being the lowest-cost producer of a product or service within the marketplace, while

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selling the product or service at a price advantage relative to the industry average. Ryanair is an excellent illustration of an organization that pursues a lowest-cost strategy because its management successfully reduced operating costs. At least two noteworthy decisions have contributed to Ryanair's goals. First, Ryanair's training and aircraft maintenance costs are lower than similar competitor's costs because the airline uses only Boeing 737 aircraft. Ryanair enjoys substantial cost savings because it does not need to use different curricula for training flight attendants, mechanics, and pilots to learn about procedures specific to different aircraft models. Second, newer aircraft sport seats that do not recline, have seat-back pockets, or life jackets stowed under the seat. These cost less and also allow service personnel to clean aircraft more quickly, saving on labour costs. Third, Ryanair airplanes include one toilet to make room for additional passenger seats. Fourth, passengers are required to carry their luggage to the plane, reducing the cost of baggage handling.

Differentiation strategies are used to develop products or services that are unique from those of competitors. Differentiation strategies can take many forms, including design or brand image, technology, features, customer service, and price. P&G Corporation successfully pursues a differentiation strategy based on brand image and price premiums. The organization offers two separate dog food lines—Iams, a super-premium line that is nutritionally well balanced for dogs and uses high quality ingredients and Eukanuba, which is an ultra-premium line that contains more chicken and vital nutrients than the Iams line, as well as additional fatty acids. Together, Iams and Eukanuba appeal to a substantial set of dog owners. The Iams Company distinguishes Eukanuba from Iams by claiming that Eukanuba is "Extraordinary Nutrition." The Eukanuba slogan is the organization's basis for brand image.

Learning Objective: 1-3. Explain strategic compensation decisions.

1-3. Stakeholder expectations pose challenges for compensation professionals. At times, there may be conflict among the expectations of different stakeholders. Give two examples and explain how compensation professionals meet their expectations.

1-4. Are the three main elements of compensation systems—internal consistency, market competitiveness, and recognizing employee contributions—equally important, or do you believe that they differ in importance? If different, which do you believe is most important? Least important? Give your rationale.

X. End of Chapter Case; Instructor Notes, and Questions and Suggested Student Responses

Case Name: Competitive Strategy at Mountain Equipment Co-op

Mountain Equipment Co-op (MEC) has been a leader in the athletic-gear industry for more than 48 years. MEC's strategy of market differentiation focuses on members' needs, the environment. and offering quality products at a reasonable price.

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Mountain Equipment Co-op sells a wide array of athletic equipment for all types of sports to its members. As MEC has established members as owners, it has created a deep commitment among them to shop at MEC rather than other sports stores. This membership builds an inclusive environment with member events and member voting. Additionally, MEC carries sports gear for numerous sports, for the amateur to expert sports enthusiasts. Further, MEC is working to engage younger generations in their sports store and culture and stay relevant. MEC is growing both its online and brick and mortar stores; however, MEC recognizes it must grow its membership of outdoor enthusiasts to remain current and continue its growth. There are various competing sports gears retailers such as Sport Chek, Sports Experts, Sporting Life, and Cabelas in this competitive market place.

Instructor Notes

The human resources planning process follows the organization's strategic planning process. In this case, the organization adopted a differentiation strategy. Under the differentiation strategy will require some employees with a different skill set. Certain functions will need high levels of creativity and innovation. Human resources management practices must shift to support these needs by attracting the right talent, and motivating the right behaviours to produce shoes for the new niche markets.

Questions and Suggested Student Responses:

1-5. Following Mountain Equipment Co-op's differentiation strategy, what are some considerations for the company's human resources management practices?

Answers may vary.

1-6. What kind of challenges will Mountain Equipment Co-op face specifically in the area of compensation?

The new hires the organization will need to make will create some compensation challenges. The organization will need to make compensation competitive in the market place to make sure that they are able to attract the new talent needed. However, they must also keep compensation internally consistent at the same time. The organization will need to examine its entire compensation strategy (including benefits and incentive pay) to make sure it is aligned with the organization's new goals.

Learning Objective: 1-3. Explain strategic compensation decisions.

XI. Crunch the Numbers! Questions and Suggested Student Responses

Calculating the Costs of Increasing the Total Compensation Budget at Butcher Enterprises

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1-7. On an average hourly basis, how much does Butcher Enterprises spend on wages and benefits, respectively, in dollars?

Butcher Enterprises spends an average of $19 per hour on wages and benefits. 70% of this amount or $13.30 is allocated for wages and 30% or $5.70 for benefits.

Learning Objective: 1-4. Identify and discuss the building blocks and structural elements of strategic compensation systems.

1-8. How much does the company spend on wages and benefits over the course of one year for 100 office workers? Assume that each worker provides 2080 hours of service each year.

The number of hours for 100 workers = 100 x 2080 = 208,000. The average hourly wage of $19 x 208,000 hours = $3,952,000 is how much the organization spends on wages and benefits over the course of one year.

Learning Objective: 1-4. Identify and discuss the building blocks and structural elements of strategic compensation systems.

1-9. How much additional money does the company need to match the market rates for this group of 100 employees?

You must first calculate the total for wages and benefits for market rate which is $23 x 208,000 hours = $4,784,000. The difference between $4,784,000 and $3,952,000 = $832,000. Therefore, Butcher Enterprises would need to spend an additional $832,000 per year to match the market rate for this group of employees.

Learning Objective: 1-4. Identify and discuss the building blocks and structural elements of strategic compensation systems.

XII. Simulation

This text includes an artificial intelligence simulation through the Revel platform. This simulation includes all of the organizational information required for students to interact with artificial intelligence either individually or in teams to build a job evaluation, salary survey, and employee compensation strategy assignments in the simulation.

Faculty can elect to allow students to explore the simulation as an applied sandbox, assign the simulation activities as exercises, assign one or more of the assignments, or finally, require students to complete all simulation assignments as a comprehensive suite of assignments assessing all course learning goals.

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The simulation is ready to play out of the box, requiring no faculty setup or configuration. Students simply login into the simulation, read instruction files, and begin to interact with the avatars. Throughout the instructors' manual the simulation will be discussed to support the faculty member.

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