

# Wage and Salary Administration

By: Ashok Arora

This reference book can be useful for  
BBA, MBA, B.Com, BMS, M.Com, BCA, MCA  
and many more courses for Various Universities



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# Sample Preview of The Chapter

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# WAGE AND SALARY ADMINISTRATION

## COMPENSATION: CONCEPT AND CONTEXT



### Role of Compensation and Rewards in Organisation

#### INTRODUCTION

Compensation and rewards play a major role in an organisation. In this chapter, we will discuss the concepts and roles of various forms of compensation. We will also discuss the current trends in compensation, a comprehensive view of compensation policy and the compensation structure and programme.

#### CHAPTER AT A GLANCE

#### COMPENSATION: THE CONCEPT

Compensation is a system of rewards for motivating employees to perform well in an organisation. It may be direct or indirect. The direct compensation provides remuneration in cash while the indirect compensation provides the various benefits to the employees.

#### INDIRECT COMPENSATION

Indirect compensation includes statutory, non-statutory, social security and welfare-oriented benefits. Indirect compensation is also called wage supplements or fringe benefits. It is given to employees not only due to legal obligation, but also due to the organisation's own interests. It varies as a consequence of the compensation policy and consequence of the compensation policy and human resource needs of the organisation.

Organisations spend money on fringe benefits because the indirect compensation attracts and retains

labour and induces the employees' commitment for the organisation. It also generate good morale in employees and promote their welfare. By providing indirect compensation, organisations also avail tax benefits, which are applicable to expenditure on welfare programmes. Cafeteria plans are part of such welfare programmes, which enable employees to select a benefit programme from the available options. Employee benefits programmes are determined by the organisation compensation policy and its objectives.

#### ROLE OF COMPENSATION

The compensation policy plays a major role in the survival, growth, competitiveness and overall financial position of the organisation. Compensation enables an organisation to attract and retain its required manpower. It encourages employees to develop skills and competencies required by the organisation. It also motivates employees and builds an organisation culture.

#### COMPENSATION STRUCTURE

The gross earnings of an employee include basic salary, dearness allowance, overtime, bonus, fringe benefits, and social security benefits. The basic salary is generally a small element of the gross salary. Dearness Allowance is determined and influenced by various factors such as union and management policies, government policy, consumer price index, labour court decisions, etc. Overtime rates vary with nature of job

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and type of organisation. Bonus may be on the basis of profit or incentive schemes of the organisation.

**THE COMPENSATION PROGRAMME:  
FUNCTIONS AND RESPONSIBILITIES**

The compensation programme of an organisation mainly determines the wage rates, wage structure and methods of wage payment. It also maintains the rationality of wage structure. Wages are determined on the basis of job evaluation, which is a systematic method of evaluating each job. The wage structure could be either equitable or inequitable. In equitable wage structure, the differences in wage rate depend on the job evaluation. The equitable wage structure is also called Internal Equity. In inequitable wage structure or external equity, the wage rates are determined on the basis of similarity of jobs in the industry. There are many forces that affect internal and external equities in wage structures. They mainly include Labour court decisions, Impact of trade union movement, Taxation rates, Effects of implementation of wage board recommendations, Minimum wage legislation, Dearness allowance, etc.

Compensation is a tool used by management for a variety of purposes:

- 1. To recruit and retain qualified employees:** Recruitment and retention of qualified employees is a common goal shared by many employers.
- 2. To increase or maintain morale of employees:** Morale and job satisfaction are affected by compensation. Often there is a balance that must be reached between the monetary value the employer is willing to pay and the sentiments of worth felt by the employee. In an attempt to save money, employers may opt to freeze salaries at the expense of satisfaction and morale. Conversely, an employer wishing to reduce employee turnover may seek to increase salaries and salary levels.
- 3. To reward and encourage peak performance of employees:** Compensation may also be used as a reward for exceptional job performance. Examples of such plans include bonuses, commissions, stock, profit sharing, and gain sharing.

**CORPORATE COMPENSATION POLICY**

The corporate compensation policy should be based on the community goals and environment such as price

stability, employees' standards of living etc. The strategy of wage increase should be on the basis of production plans of the organisation. The rationality of pay-packed, internal equity and external equity should be ensured to achieve company objectives. The payroll policy should also be analysed regularly. A specialised wage and salary administration function should be built during formulation of the corporate compensation policy. A single integrated compensation plan is needed to develop for all hierarchical levels in the organisation.

**(a) Corporate Compensation Policy and Community Concern:** The corporate compensation policy should be in the interests of the organisation, employees, shareholders and the community as a whole.

**(b) Strategy of Wage Increases:** The increase in wages depends upon the improvement in productivity, reduction in cost, intensive management communication with union and economic concessions.

**(c) Rationality and Hygiene Factors:** Rationality of salary package means the remuneration is linked with the performance and fringe benefits depend upon the needs of the employees.

**(d) Internal Equity:** All employees compare their jobs to other jobs within the organisation. Generally, they consider skill, effort, responsibility and working conditions in this comparison in order to determine the value of their jobs relative to other jobs. Internal equity deals with the perceived worth of a job relative to other jobs in the organisation.

**(e) External Equity:** An employer's goal should be to pay what is necessary to attract, retain and motivate a sufficient number of qualified employees. This requires a base pay programme that pays competitively. External equity deals with the issue of market rates for jobs.

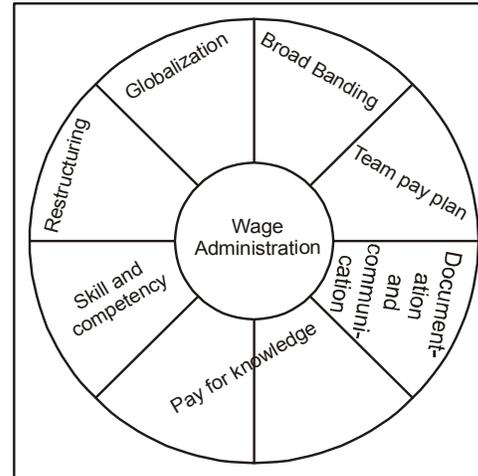
**(f) Payroll Analysis and Policy Correctives:** Payroll policy should be based on regular analysis of wages and trends in the market and pay structures should be updated accordingly.

**(g) Corporate Compensation Structure and Managerial Compensation:** The salary structure of managers varies with that of other employees in an organisation. For instance, managers get more perks and benefits than their subordinates. Therefore, the corporate compensation structure should follow a systems approach.

**(h) Wages and Income Policy:** There should be an integral policy on wages, incomes and prices. The primary objective should be on fiscal measures for regulating income and providing positive approach for savings and investment.

**ISSUES AND CURRENT TRENDS**

The various issues and latest trends in wage administration are: Broad banding, Team pay plan, Documentation and communication of compensation and communication of compensation policy to employees, Pay for knowledge, skill and competency, Restructuring of wages based on changes in the organisation and Compensation based on globalisation.



**REVIEW QUESTIONS**

**Q. 1. What are the major functions of the compensation programme?**

**Ans.** The various functions and responsibilities of a compensation programme are as follows:

1. Formulation of compensation plans and establishing criteria for wage and salary determination: The compensation programmes determine the criteria for salary and wages and hence help in making the appropriate compensation plans.
2. Recommending and administering plans for wage incentive systems: Many wage incentive systems such as fringe benefits are based on compensation programmes.
3. Supervising and maintaining records pertaining to all matters or compensation. The HR manager keeps records of compensation paid to every employee, which help in solving salary related matters.
4. Analysing government wage regulations, company wage policies, and agreements with unions: Using compensation programmes, the HR manager can analyse the various government policies along with their affect on establishing the compensation structure.
5. Establishing job evaluation systems and ascertaining on-going rates for jobs in industry: There are many job evaluation methods that need to be implemented in determining compensation structure.

**1. Broadbanding:** The traditional narrowly structured pay grades are generally determined through job evaluation. However, using broad banding, they are replaced by fewer and wider bands. So, there is a greater flexibility in setting and adjusting pay rates using broad-banding.

**2. Pay for Knowledge, Skill and Competency:** Pay for knowledge, skill and competency is a common practice in scientific and technical organisations. It helps in motivating employees to improve their knowledge and skills.

**3. Team Pay Plans:** Team pay plan supports team work and their empowerment. It also helps in improving organisation’s culture and achieving the organisation’s mission and objectives.

**4. Documentation and Communication:** Proper documentation and communication of compensation policy is necessary to motive staff. Such communication provides information about revised salary structures and changing roles of various employees, which encourage the staff to work in the organisation.

**5. Coping with Change:** Rapidly expanding techniques, growing competition, increase demand for competencies, higher consumer expression, changing manpower, etc., are some of the changes that are common to every organisation.

**6. International Competition:** With increase in multinational organisations in the country, the competition has increased among national organisations for providing an attractive salary package to their employees.

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6. Rating employees and thus recommending increase in their wages: With a compensation programme, HR manager can rate the employees' based on their performance and thus recommend the revision of their salaries.
7. Establishing fringe benefits and other supplementary compensations: Fringe benefits encourage employees to work better for the organisation. They are established through a compensation programme.
8. Assisting management in framing a compensation policy that is aligned to mission of the organisation: All organisations work to achieve their mission. The appropriate compensation policy can be framed with a compensation programme.
9. Promoting the desired values and organisational culture: Organisational culture is affected by compensation. Often there is a balance that must be reached between the monetary value the employer is willing to pay and the sentiments of worth felt by the employee. In an attempt to save money, employers may opt to freeze salaries at the expense of satisfaction and morale. Thus, compensation promotes the desired values in employees.
10. Promoting team effort and unit performance: Compensation may also be used as a reward for exceptional job performance. Examples of such plans include bonuses, commissions, stock, profit sharing, and gain sharing.

**Q. 2. What is the overall objective of a compensation policy?**

**Ans.** The overall objective of a compensation policy of an organisation is to consider the following three concerns:

1. Community as a whole (both economical and social)
2. Organisation's Mission, Objectives, Goals and Strategies (MOGS) for expansion and diversification
3. Employees' benefits.

All organisations have a compensation policy, written or unwritten, formal or informal. For some organisations, the purpose of that policy may be merely

to meet compliance requirements. For other organisations, the goal of the compensation policy may be to attract qualified employees, to retain those employees, and to motivate employees to direct their efforts towards achieving the goals of the organisation. Regardless of the goal, size and complexity of a compensation policy, there are generally many easily-identified elements to any compensation policy.

Compensation is a tool used by management for a variety of purposes. Compensation may be used to recruit and retain qualified employees, increase or maintain morale/satisfaction, reward and encourage peak performance, achieve internal and external equity, reduce turnover and encourage company loyalty and modify practices of unions. Recruitment and retention of qualified employees is a common goal shared by many employers. To some extent, the availability and cost of qualified applicants for open positions is determined by market factors beyond the control of the employer. While an employer may set compensation levels for new hires and advertise those salary ranges, it does so in the context of other employers seeking to hire from the same applicant pool. Morale and job satisfaction of employees are affected by the compensation policy.

**Q. 3. What factors go into the determination of pay in an organisation?**

**Ans.** The various factors that determine pay in an organisation are as follows:

1. **Corporate Compensation Policy and Salary Structure:** The corporate compensation policy should be in the interests of the organisation, employees, shareholders and the community as a whole. The salary structure of managers varies with that of other employees in an organisation. For instance, managers get more perks and benefits than their subordinates. Therefore, the corporate compensation structure should follow a systems approach.
2. **Rationality and Hygiene Factors:** Rationality of salary package means the remuneration is linked with the performance and fringe benefits depend upon the needs of the employees.
3. **Internal and External Equities:** All employees compare their jobs to other jobs within the organisation. Generally, they consider skill, effort, responsibility and working conditions in this comparison in order