Pay Compression

Questions we will address:
• What is pay compression?
• Where are the problems?
• What is causing the problem?
• Why should it be addressed?
• How can we fix compression?
Identifying Pay Compression

**Definition**

- Subordinate is paid more than their supervisor based on regular, not overtime, pay;
- Pay of new or less-tenured employees (staff and faculty) is equal to or greater than pay of current, longer-tenured, employees in the same or similar job
  - This is the most common form of compression, especially in recent years
  - Lack of recent pay increases but need to hire/attract new employees
  - More severe during economic downturns
Identifying Pay Compression

Does your institution have pay compression?

• Yes!
• If you are hiring new employees you probably have some form of pay compression
• Economic downturns accentuate compression issues
• The market has continued to move since 2008:
  – Average higher education salary budgets have moved between 0%-1% per year
  – Average market salary budgets have moved between 1.8%-2.5% per year
• Market rates have continued to increase, new hire rates continue to increase
Identifying Pay Compression

How do we find where there is pay compression?

• You probably already know about it, or have HEARD about it!

• Pay of new or less-tenured employees (staff and faculty) is equal to or greater than pay of current, longer-tenured, employees in the same or similar job

• Causes:
  – General pay freezes over the past 5 years
  – Need to hire replacements or new employees
  – New employees asking for and receiving higher pay offers than current employees
Identifying Pay Compression

Where in our institution do we have pay compression?

• Perceived compression between employees and supervisors when comparing take home pay.
  – Technically, not compression, but causes promotion issues

• Review the pay administration guidelines.
  – How current employees move through the salary range
  – Overlap of salary ranges
  – New employee hiring ranges
### In-Range Compression

<table>
<thead>
<tr>
<th>Range</th>
<th>Minimum $</th>
<th>A</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employee A</td>
<td>10 years with institution, 4 with frozen salary</td>
<td>B</td>
</tr>
<tr>
<td>Employee B</td>
<td>hired 5 years ago within established hiring range of first quartile</td>
<td>C</td>
</tr>
<tr>
<td>Employee C</td>
<td>new employee hired in 2012</td>
<td></td>
</tr>
</tbody>
</table>

Midpoint

To identify, compare range penetration with years in the current position in each salary grade.
Between Grades Compression

**Employee A** – 10 years with institution, 4 with frozen salary
**Employee B** – hired 5 years ago within established hiring range of first quartile
**Employee C** – new employee hired in 2012

To identify, review salary range overlap, possible regression analysis between salary grade and current salary.
Identifying Pay Compression

Overlap of salaries identifies possible compression. Requires additional research into why.

Causes:
- Inconsistent salary range structure, too much or too little overlap
- Red circle identifies bad compression
- Blue circle identifies OK compression
Employee A – Placed in grade 5 of the Facilities salary structure, due to negotiations salary structure has moved each year along with employee step increases.

Supervisor B – Placed in grade 1 of Management salary structure, structure has been developed separately the Facilities structure, no structure movement or increases over past 3 years.
Solutions to Pay Compression

Job Evaluation – Employee and Supervisor jobs are evaluated on same internal hierarchy
  - Multiple systems available
  - Needs to be used across all types and levels of jobs at the organization
  - Supervisor – Employee internal equity (at least two grade difference)

Salary Structure Development – Complete salary structure is developed across all job titles
  - Market data is merged with internal hierarchy through regression analysis (samples on following pages)
  - Job Evaluation system should ensure appropriate pay progression (minimum of 5% difference between salary ranges)
Solutions to Pay Compression

Market Pay

$0.00 $10.00 $20.00 $30.00 $40.00 $50.00 $60.00 $70.00
0 1000 2000 3000 4000 5000 6000 7000 8000 9000

Market Pay

Linear (Market Pay)
Solutions to Pay Compression

Proposed Salary Ranges

Proposed Structure shows appropriate progression of midpoints, with established internal relationships between employees & supervisors.

Proposed Midpoint Equation:
\[ y = 0.0061x + 9.8081 \]
\[ R^2 = 0.91811 \]
Solutions to Pay Compression

Prudent Salary Management Solution:
Do not throw money at the above problem! – Temporary solution that does not solve root problem, you will have to hire employee D somewhere.

COLA v. Salary Structure adjustment – utilize two different adjustments, salary structure and individual employee increase.

- Salary Structures are used to control salaries and offer competitive rates

Employee Movement – Separate from the COLA or Salary Structure Adjustment, employees have an increase amount, either based on performance or a step increase.

Elected officials will complain about the ongoing costs of prudent salary management, but the alternative is an expensive one-time solution that will be out-of-whack if not maintained through prudent salary management practices!
Solutions to Pay Compression

One-time Solution:
Only do this with Prudent Salary Management practices!

Review Seniority – Places employees at appropriate spot in range based on years in current position, different algorithms available:
- One step or X% per one/two/three year(s) of service up to certain number of years
- Depending on quartile of the salary range (example above)
- Results in 20-30 year spread
- Capped increases at midpoint or other points in salary range
- Dependent on money available

Needs to be maintained through prudent salary management practices!
Pay Compression

What are the results if compression is not addressed?

– Lower morale

– Requests for reclassifications (without substantial justification)

– Possible gender/race equity issues

– Demands for fixes

– Increased turnover of valuable staff

Pay compression can never be eliminated as long as new employees are hired!
Pay Compression

Words You Hear in HR:

• Our pay system is out of whack!
• New employees are paid more than current employees.
• Current employees would be better off quitting and getting hired again to get a raise.
• We have not had raises in X years.

What is happening out there?
Pay Compression

Overall Results:

• Pay compression is reduced, but not eliminated
• Requires constant review, education, and prudent salary management practices
• Negative effects can be reduced
• Costs money

Now what?
Pay Compression

Major Takeaways

• Pay compression is self induced.
• Often created when ranges change
• Usually created when a new person is hired
• Impossible to hide or explain away
• Likely to result in expensive legal action
• Solvable only with money

So now you know!
Thank You

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