



# How to Perform Compensation Benchmarking and Set Salary Ranges

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# Why external market analysis is important



“The war for talent and proliferation of pay information, especially free and low-cost data online, are increasing pressure on HR offices to have and use accurate, up-to-date market pay information, to share it with managers and employees and, at times, to defend its use while refuting incorrect or inferior data. Knowledge of and skill in selecting and using compensation surveys are required”

- Kenneth H. Pritchard in: ***Selecting and using compensation surveys: critical issues for today's HR professionals***

# Creating Market Centered Ranges - Steps



- **Selecting survey data**
- **Applying your compensation philosophy to the data**
- **Choosing benchmark jobs**
- **Getting the data right**
  - Aging data
  - Weighting your sources
- **Determining your pay grades**
- **Building your ranges**
- **Hot jobs**

# Selecting Survey Data



- **Best practice is to choose 3 salary sources**
  - You want surveys with good coverage for your industry/geography/type of organization
  - The goal is to be able to benchmark 75-80% of the positions within your organization, this is best accomplished with multiple sources or a single source such as PayScale which provides good coverage
- **Understand the methodology of the survey that you are using**
  - How do they collect data?
  - Do they use aging or geographic differentials?
  - What is the effective date of the data?
- **Price is important – make sure you are getting good value**
  - Participation may be required for traditional surveys (indirect costs)
  - High cost does not always equal high value
  - Which surveys are going to give the most value for the price (cost vs. number of positions matched)

# Applying your compensation philosophy to the data



- What industry are you going to use for comparison?
- What size organization are you going to use for comparison?
- What geography are you going to use for comparison?
- What “target” are you going to use from the survey data?
  - There is a difference between the average and the median
  - If you choose a percentile, make sure you can get that number from every source
  - Will you be looking at base salary or Total Cash Compensation (TCC)

# Choosing Benchmark Jobs



- **When selecting your benchmark jobs you want to:**
  - Focus on those positions that are standard across different industries.
    - ✦ For example: HR Generalist, Accountant, Administrative Assistant
  - Choose industry specific positions that are standard at your company compared to positions within other organizations within your industry.
    - ✦ For example: Civil Engineer, RN, assembly line worker
  - Avoid hybrid positions
- **What should you do with non-benchmark positions?**
  - Don't force matches to market data for non-benchmark positions
  - Instead, use your job evaluation tool to slot the position within a pay grade, or use your own internal assessment of comparable positions within your organization with similar skill, scope, decision making and responsibility

# Getting the data right



- Aging data from an effective date in the survey to the effective date for your organization
  - Choosing a multiplier ([www.worldatwork.com](http://www.worldatwork.com))
  - Finding the effective date of the survey data
- Geographic differential if expanding your search to capture more data
  - Choosing a cost of labor/living multiplier
- Matching the job
  - Don't match on title alone
  - Look at the scope: who the job reports to, education, experience, decision making
  - Decide how to handle hybrid jobs
  - Decide how to handle leveling within your organization



# Aging Data



<u>Aging data</u>				2.9%				
	Effective Date	Target Date		Source 1	Source 1 aged	Source 2	Source 2 aged	Source 3
Buyer II	12/1/2008	6/1/2009	1.47%	\$38,500	\$39,064	\$41,000	\$41,601	\$43,000
Marketing Coordinator	12/1/2008	6/1/2009	1.47%	\$31,000	\$31,454	\$32,000	\$32,469	\$33,000
Accountant 2	12/1/2008	6/1/2009	1.47%	\$54,000	\$54,792	\$56,500	\$57,328	

1. Step one – find the effective date of the survey data and decide on the target date for the data
2. Decide on an annual adjustment factor
3. Calculate the portion of the factor to use based on the effective date
4. Apply the aging factor to the market data

# Weighting Your Sources



<b>Position</b>	<b>Source 1</b>	<b>Weight</b>	<b>Source 2</b>	<b>Weight</b>	<b>Source 3</b>	<b>Weight</b>	<b>Weighted Average</b>
Buyer II	\$39,064	0.25	\$41,601	0.5	\$43,630	0.25	<b>\$41,474</b>
Marketing Coordinator	\$31,454	0.25	\$32,469	0.5	\$33,484	0.25	<b>\$32,469</b>
Accountant 2	\$54,792	0.5	\$57,328	0.5			<b>\$56,060</b>

1. Choose the weight you will assign to each source
2. Use the aged data from that source
3. Multiple the source data by the weight assigned to that source
4. Come up with your weighted average

# Determining your pay grades



- Pay grades are used to group jobs that have approximately the same relative internal worth; in other words, all jobs within a particular grade are paid the same rate or within the same pay range.
- The number of pay grades varies in response to:
  - The size of the organization
  - The vertical distance between the highest and lowest level job
  - How finely the organization defines jobs and differentiates between them
  - The pay increase and promotion policy of the organization

***The bottom line: the number of pay grades should be sufficient to permit the distinguishing of difficulty levels but not so great as to make the distinction between the two adjoining grades insignificant.***

# Building your pay ranges – finding the midpoint



- Pay ranges set the upper and lower bounds of possible compensation for individuals whose jobs fall in a pay grade; pay ranges are created for each grade.
- The market midpoint is the value of the aged, weighted market data for the position or positions.
- Once you establish the job evaluation method you want to use to assign jobs to a pay range, you use the market data for those ranges to create a market mid point. This can be done by simply averaging the market data for all the positions within the pay range (watch for outliers).

# Building your pay ranges - determining the range spread



The spread between the minimum and maximum will depend on many variables within your organization and based on your compensation policy and practices, but some general guidance is provided below:

- Generally, pay spreads are narrower for lower-level job, and wider for higher level jobs
  - Tenure in position
  - Learning time necessary to achieve “job rate” (midpoint)
- There should be overlap between pay ranges, which makes it possible for an experienced person in a job in a lower grade to be paid more than an inexperienced person in a higher job.
- Typical range spreads:
  - Hourly positions – 40%
  - Salaried positions – 50%
  - Executive positions – 60%

# Building your pay ranges – determining the minimum and maximum



- Once you have calculated your midpoint, and you have determined the range that is most appropriate, you will calculate the minimum by dividing your range spread percentage in half. Then, you will take your midpoint and divide it by 1.xx half of your range spread. For example:
  - If your midpoint is: \$30,000 and you want your width to be 40%, then you would divide \$30,000 by 1.20. This equals \$25,000. \$25,000 is your minimum for the range
- To find your maximum, take your minimum and multiply it by 1.xx your range spread. For example:
  - If your minimum is: \$25,000 and your width is 40%, then you would multiple \$25,000 by 1.40. This equals \$35,000. \$35,000 is your maximum for your salary range
- In this example, your full salary range would be **\$25,000 - \$35,000** with a midpoint of **\$30,000**

# How to handle “hot jobs” or range busters



- First, double check that this position is appropriate assigned to the right pay grade.
- Do not include market data in the calculation of the market midpoint.
- Assign employees in this “hot job” to the appropriate pay grade, but develop a special market premium range for these employees.
  - For example – if the average of the market data for the “hot job” is 20% above the market rate for the rest of the position in the same pay grade, apply a market premium for people in this job.
  - Best rule of thumb is to make this market premium as transparent as possible to the employee, so that if it needs to be taken away, it can be explained clearly to employees.



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