
Motivating Employees through Compensation

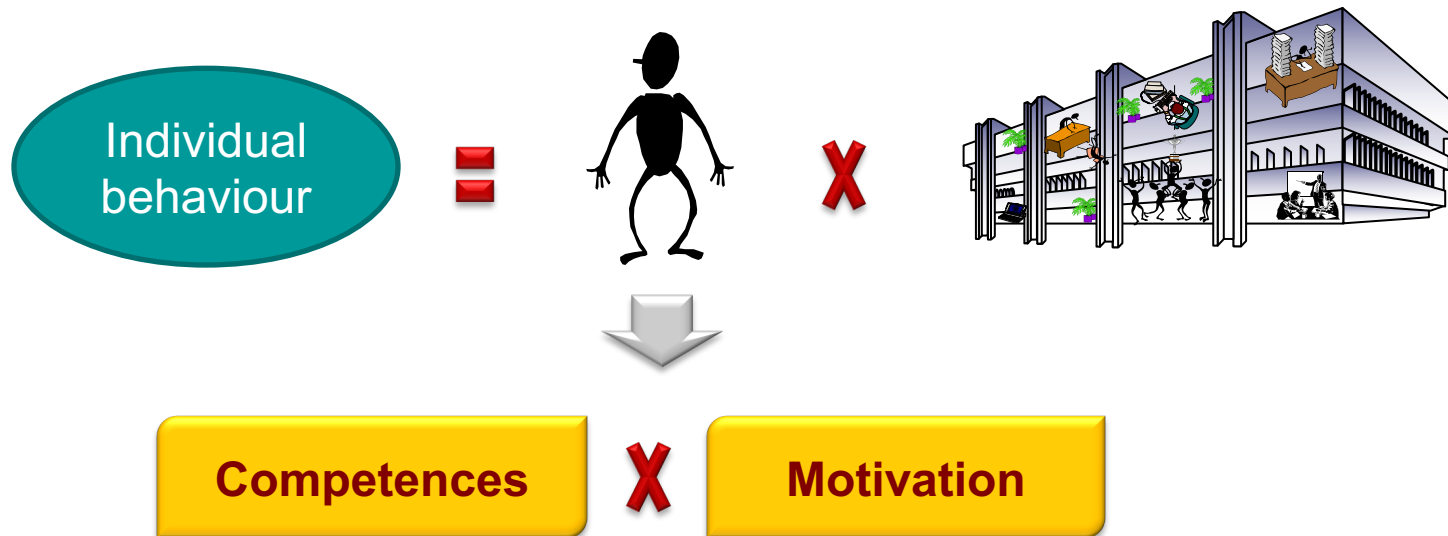
Lesson7

Learning Objectives

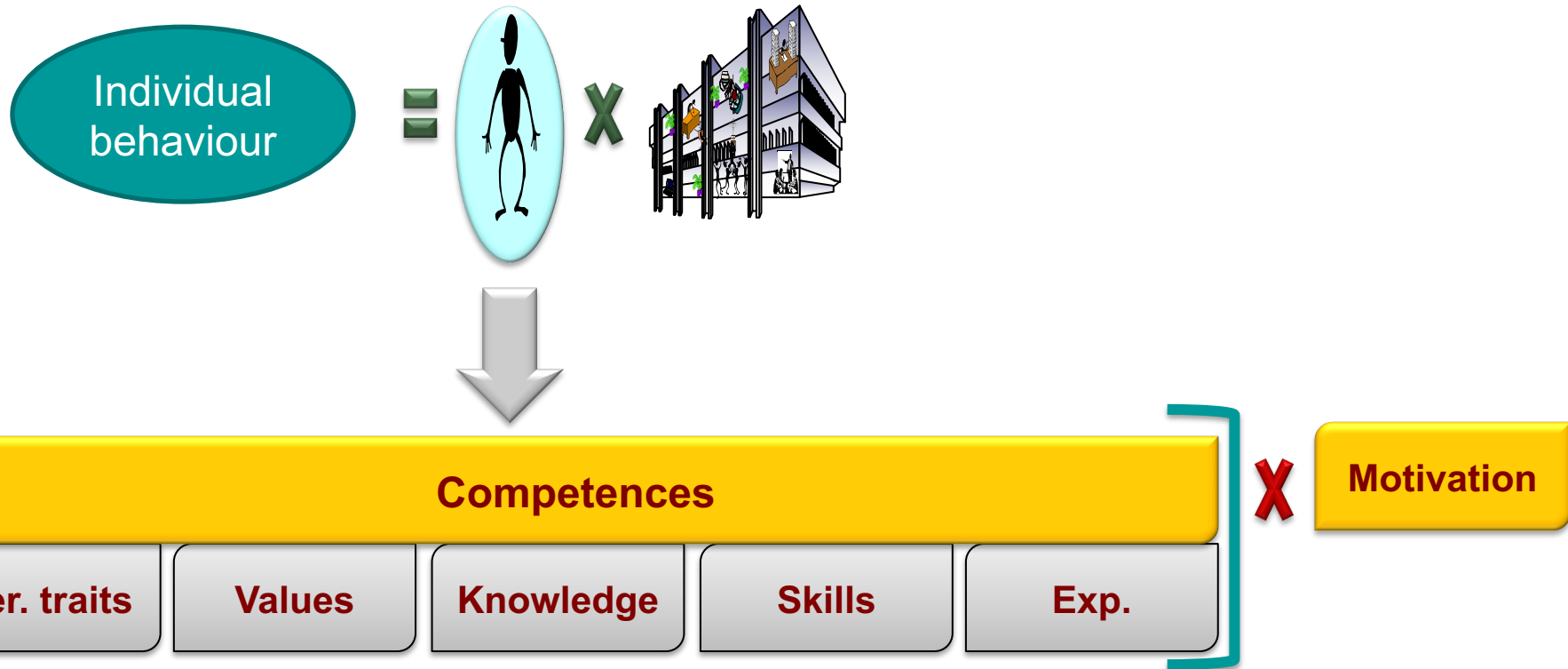
After this lecture you should be able to:

- ❑ Describe **employee compensation practices**.
- ❑ Connect **motivation theories** to compensation practices.
- ❑ Describe pay surveys and their use to create **compensation level strategies**.
- ❑ Explain **job-based** pay and **skill-based** pay approaches.

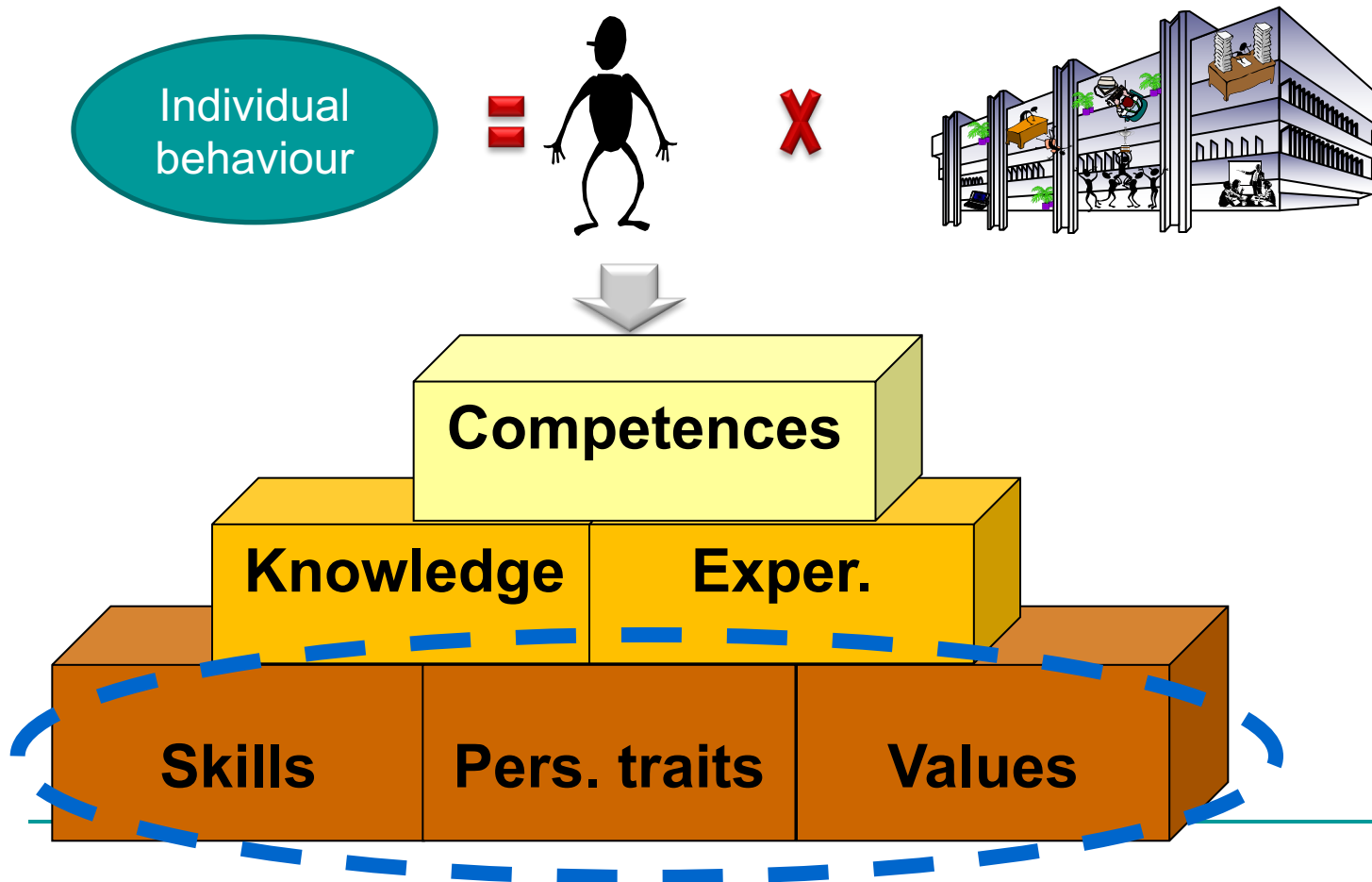
The individual behaviour ...



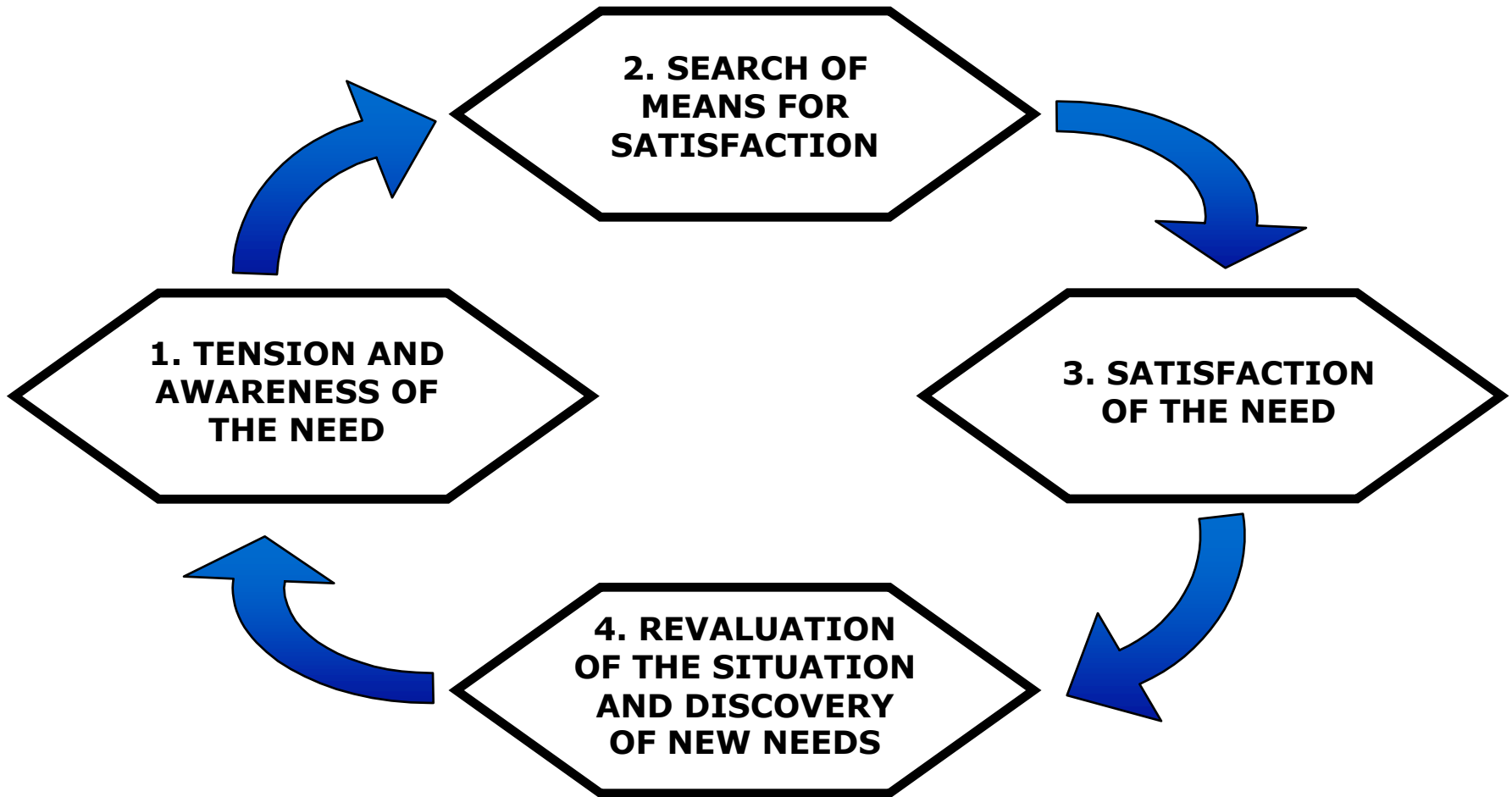
The individual behaviour ...



The individual behaviour ...



Motivational process



Employee Compensation

- It is the **process of paying and rewarding** people for the contributions they make to an organization.
 - Compensation is a broad term which includes **pay** and **benefits** such as **insurance**, **retirement savings**, and **paid time off from work**.
 - Compensation represents the total package, both monetary and nonmonetary.
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External vs Internal Equity

- Employees' perception of **external equity** - which concerns the fairness of what the company is paying them compared with what they could earn elsewhere—are critical in such employment relationships.
 - An external labor orientation requires a comparison with the compensation offered by other organizations.
- Employees' perceptions of **internal equity** - their beliefs concerning the fairness of what the organization is paying them compared with what it pays other employees.
 - An internal orientation requires a comparison among the organization employees.
 - Pay practices, such as how much each person makes, are usually less secretive in these organizations than in organizations with an external orientation.
 - Internally oriented organizations also use long-term incentives to reward employees who stay with them for long periods.

Differentiation vs Cost Strategy

- Organizations following a **differentiation strategy** seek high performing employees who create superior goods and services
 - Usually applied for “**free agent**” and “**committed expert**”
- Organizations following cost strategy want to reduce labor expenses, paying fixed salaries.
 - Usually applied for “**bargain laborer**” and “**loyal soldier**”

How does compensation motivate people?

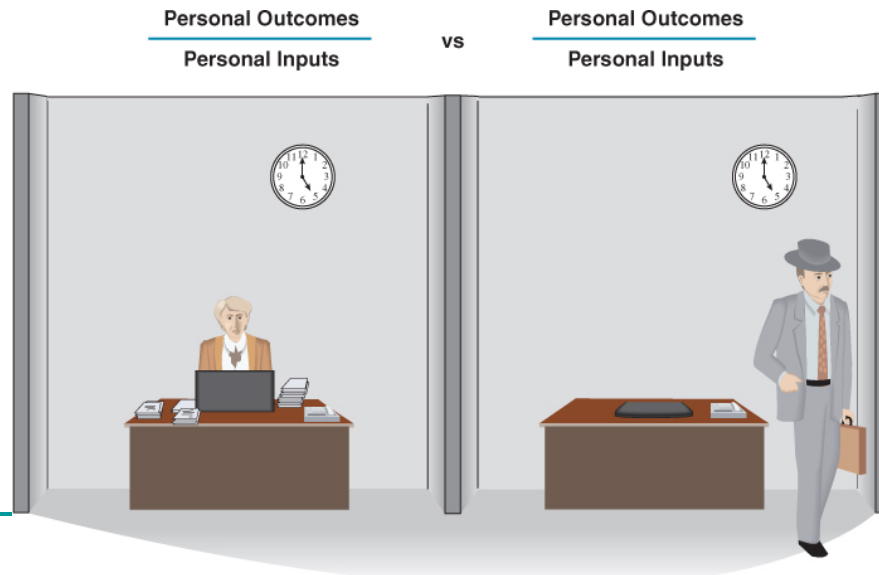
- **Motivation** can be defined as a force that causes people to engage in a particular behavior rather than other behaviors.
- Motivation is represented by three elements:
 - **Behavioral choice** involves deciding whether or not to perform a particular action.
 - **Intensity** concerns deciding how much effort to put into the behavior.
 - **Persistence** involves deciding how long to keep working at the behavior.

Motivation Theory

- Motivational theory and Compensation
 - Justice (or Equity) theory
 - Reinforcement theory
 - Expectancy theory
 - Goal-setting theory
 - Agency theory

Justice (or Equity) Theory

- Motivation depends on beliefs about fairness.
 - People compare their inputs and outcomes to the inputs and outcomes of others.
- Equity theory is an example of what is known as distributive justice.
 - **Distributive justice** is concerned with the fairness of outcomes. In terms of compensation, distributive justice focuses on whether people believe the amount of pay they receive is fair.
 - A different form of justice is the **Procedural justice**, which is concerned with the fairness of the procedures used to allocate outcomes. The focus here is on the process used to decide who gets which rewards.



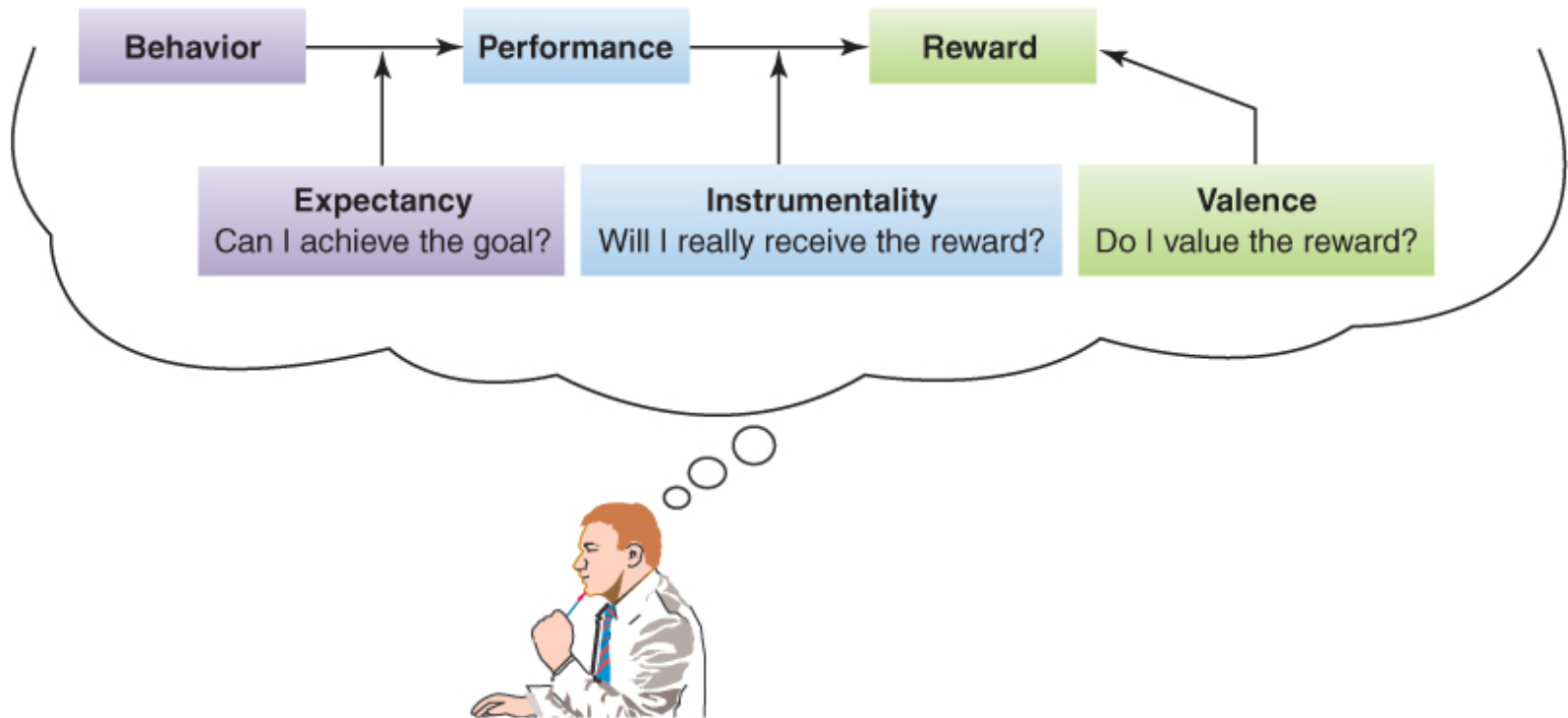
Motivation is determined by comparisons with others.

Reinforcement Theory

- Comes from the field of psychology, holds that behavior is caused by chains of antecedents and consequents.
 - **Antecedents** are factors in the environment that cue someone to engage in a specific behavior.
 - **Consequents** are results associated with specific behaviors.
 - Antecedents and consequents are linked together because the antecedent causes people to think about the consequent.
- When linked to compensation the theory states people will engage in the behaviors for which they are rewarded.

Expectancy Theory

This theory proposes that motivation comes from three beliefs: valence, instrumentality, and expectancy.



Motivation is a function of beliefs.

Goal-Setting Theory

- **Goal-setting theory** is grounded in cognitive psychology and holds that behavior is motivated by choices.
- Goals improve performance through four specific motivational processes:
 - ❑ **Goals focus attention away from other activities toward the desired behavior.**
 - ❑ **Goals get people energized and excited about accomplishing something worthwhile.**
 - ❑ **People work on tasks longer when they have specific goals.**
 - ❑ **Goals encourage the discovery and use of knowledge.**

Agency Theory

- Agency theory, developed in the 1970s, focuses on the way management of a firm manages its relations and enters into **contractual arrangements** with its managers or employees.
- The conditions under which subordinate agents work with corporate managers may directly influence the behavior of the organization, such as taking risks related with new ventures.
- Issues such as remuneration, accounting techniques or risk-taking are among the major concerns of both parties in this relationship.

Linking motivation with strategy

Table 11.1

Principles for Increasing Motivation through Compensation

Develop pay-for-performance plans.

Link pay with goals that encourage stretch efforts.

Understand the referent groups employees use when assessing the fairness of pay.

Follow principles of procedural fairness, including accurate assessment, lack of bias, and opportunity to have input.

Provide rewards that are large enough to matter.

Coordinate with selection and training to ensure that employees have the skills they need to meet goals.

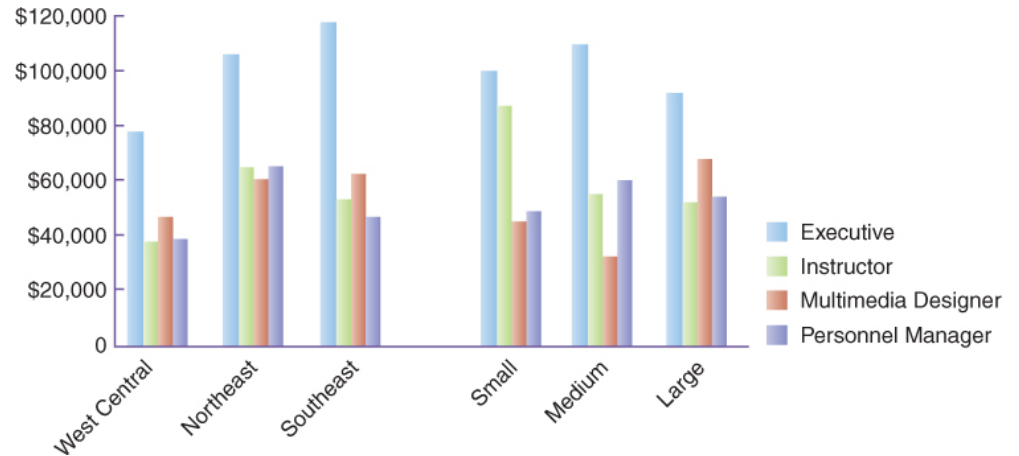
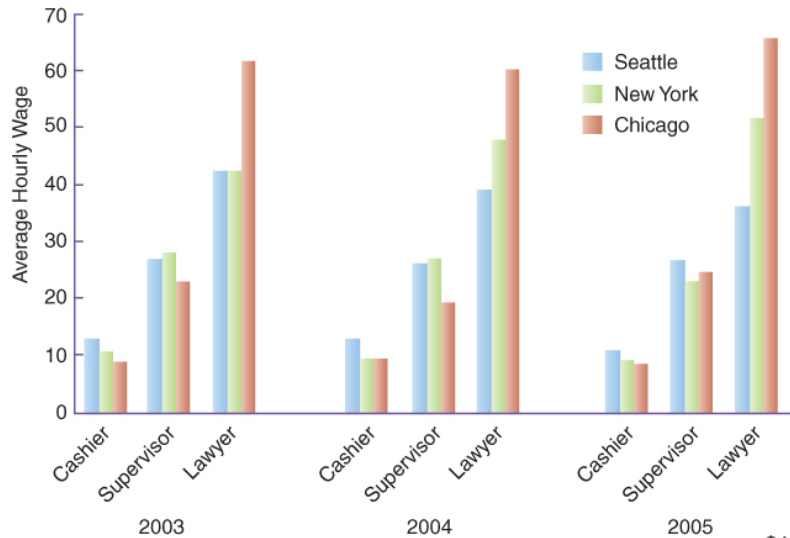
Align the interests of employees with the interests of owners.

Give higher rewards for employees who assume risk.

How is compensation level determined?

- The role of the **pay survey**.
 - The pay survey provides **information about how much other organizations are paying employees**.
 - Pay surveys are conducted by **consulting firms**, which obtain confidential pay information from numerous organizations and create reports that describe average pay levels in other organization.
 - This information is grouped by industry, number of employees, sales volume and/or operating budget.
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Samples Pay Survey Results



Pay-Level Strategies

- There are three market strategies
 1. **meet-the-market** which establishes pay that is in the middle of the pay range for the selected group of organizations.
 2. **lag-the-market** where an organization establishes a pay level that is lower than the average in the comparison group.
 3. **lead-the-market** where the average pay level is higher than the average in the comparison group.

How is compensation structure determined?

- The **pay structure** focuses on how compensation differs for people working in the same organization:
 - **Job-based pay** focuses on evaluating different tasks and duties associated with various jobs in the organization.
 - **Skill-based pay** focuses on the difference in skill and ability required to perform the job.
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