

## ***How much is fair?***

### ***Basic Compensation Training for Non-HR***

It's been a while since I wrote my last post; I let my daily routine take over the pleasure of writing. To make up for all this time, I am bringing an article that I was saving for a special time as it touches a pain point for almost anyone in the workforce: pay.

During nearly two decades in the world of Compensation and Benefits, I have negotiated salary offers in different geographies and participated in multiple debates with HR executives and employees on what is fair and what is competitive when it comes about pay. I've learned many things, but maybe my biggest pick up is at the same time my greatest concern: employers and employees have very different comp information and knowledge. While employers count on robust and factual data, and expensive teams of consultants, employees only have access to scattered and less specialized sources e.g. general magazines, newspapers, and the internet.

In Contract Theory and Economics, this power imbalance is called "Information Asymmetry." If you have an interest in Academia, George A. Akerlof published an excellent article named "The market of Lemons" (1970), which offers multiple views including the case of minorities. But in today's world, this disparity is less about race or gender thanks to the existence of affirmative action policies (employment equity in Canada, reservation in India, positive discrimination in the UK or Australia, racial quotas in Brazil, etc.). The actual disparity starts with uneven access to information, which sounds like a joke in a time of excessive data availability.

Also, it is interesting how much financial literacy is made available to the typical employee, while ironically there is almost zero education on Compensation. This is like trying to fill a bottle with a hole in the bottom: the amount of water remaining in the bottle (think of this as your savings) will depend on the water inflow (your salary) and the outflow (Financial Education). Financial Education without Comp Education is incomplete.

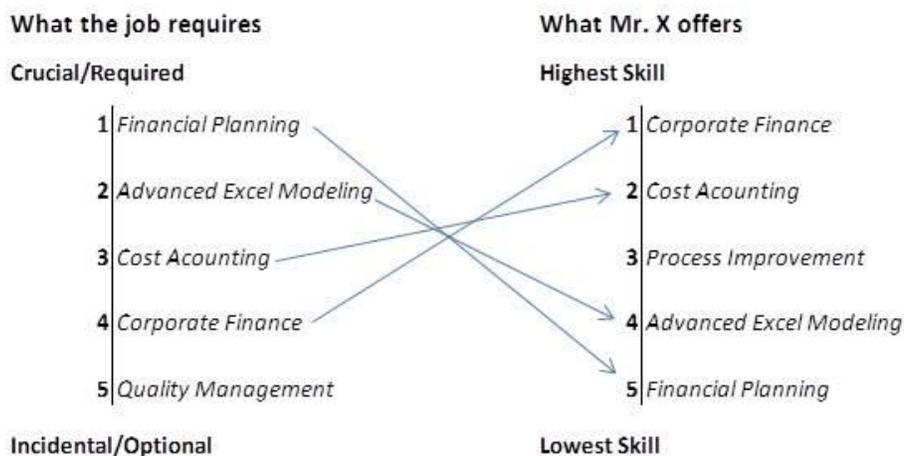
For the reasons above, I feel obliged to share some of my learnings on Compensation and Benefits, especially those that are usually kept only for HR, generating most of the existing information asymmetry.

#### ***Learning #1 – Salaries are not set in stone***

I find that most high earners are also good salary negotiators. But they typically negotiate on the basis of value, as opposed to mere tactics or "haggling". But how to determine someone's value? Good Salespeople can teach us how.

I have not always been a Compensation guy; during different moments of my career, I was also an international salesperson. In those years I learned that the best salesmen focus less on their pitch and more on meeting the client's "Buying Criteria." In other words, they place particular attention to the customer's perceived value.

Neil Rackman, an authority in sales strategy, in his book "Major Account Sales Strategy" uses a diagrammatic method to uncover client's criteria, which I am borrowing below. In my example, I ranked the skills needed for a Financial Analysis job (left) and mapped them vs. Mr. X's strengths.



Despite Mr. X being highly skilled, his capabilities don't map what is essential for the job. Is he in a position to negotiate salary? I think he would be lucky to keep his job.

Of course, this is an exaggerated picture for illustrative purposes. But I am sure you get the point.

**Learning #2 – Joining and leaving a company are not the only two moments to discuss salary**

I believe that there isn't a pre-defined time to talk about pay (however, I would keep from doing it during a restructuring period or when all you hear is cost savings). In some cultures and at some pay levels, salary negotiation is not even a practice. But where it is possible, we already learned that it is a "value added" conversation rather than a regular bargaining process. Yet in order to have the arguments and seize the limits, you also need to understand how the compensation system works, so I invite you to keep reading.

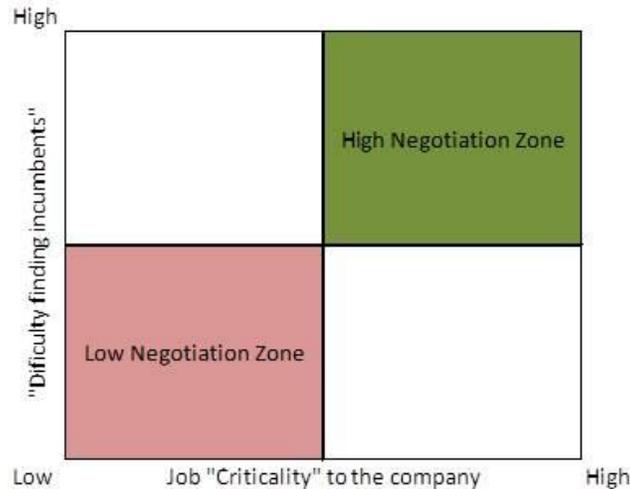
**Learning #3 – Compensation is both science, and art**

Most seasoned Comp professionals know this expression. Salaries are determined by a mix of elements that cluster and produce the "magic figure." Let's look at some of those elements.

**Market Value:** While many organizations count on tailored salary surveys and Compensation teams to assess the market price of jobs, regular job seekers and staff can also build reliable data from public sources. This exercise requires time and dedication to reviewing multiple open sources, crossing information and creating market medians to "mimic" the way salary surveys work. Bear in mind that this is still not as accurate as tailored salary surveys, but if you use enough sources, you can get sensible data.

**Employee Value:** Emotional pressure and anecdotal information e.g. "my salary does not cover the bills", "Margie does the same and makes more" (BTW, who told you Margie's salary?), etc., seldom work and can ruin your image. Remember, productive salary conversations focus on value.

**Criticality:** This can be represented by a 2X2 matrix, as shown below.



The green area represents the situation where you have better chances to negotiate. If you understand your job and the industry, you'll be able to spot your place on this matrix.

**Internal equity:** Companies strive to maintain salaries in line with their philosophy. For example, if pay for performance is relevant, Company X will be more open to raises for those regarded as high performers. Although internal equity still means “similar job-similar pay” in some places, in most cases today is about alignment with pay principles. To understand your company’s pay philosophy, I recommend studying all compensation information that is accessible to you. You will be surprised how much you will find.

**Politics:** HR, Comp and hiring Managers typically face additional challenges before they can move a salary, especially above maximum of the range i.e. a) Senior Management has to approve the exception; b) They will have to explain when the next pulse (climate) survey exposes internal equity issues, and c) Their reputation could be questioned if the employee does not perform as expected. To overcome these challenges, I recommend to seek alignment from your key stakeholders before starting any conversation on salary; also "rehearse" your boss to represent you in front of his stakeholders, and offer robust, clear and fact based arguments. If you are a job seeker and do not know anyone internally, prove your value during the interview process, offering Hiring Managers and HR the ammunition they need to defend a higher salary for you.

**Learning #4 – Understanding how pay ranges work will give you leverage**

You probably know that companies use salary ranges to define salary max/min, but more important is to understand how they work. These are three key aspects to consider:

1. Although Max and Min are usually references, breaking the limits requires further approvals, which Line Managers and HR tend to avoid.
2. Typical salary ranges have “zones” where employees are placed on the base of value and experience. For example, company XYZ breaks the ranges into four zones:



3. HR uses Position in Range (PIR) or Compa-Ratios (CR) to indicate the position of every employee within the salary range. Several companies make these indicators available to employees. Find out if our company is one of those (For PIR and CR definitions visit [www.worldatwork.org/waw/Glossary](http://www.worldatwork.org/waw/Glossary)).

When you get an offer or when you are discussing a pay adjustment, remember to ask where your salary sits on the range (if you feel it is pertinent to ask). This will tell you: a) how they assess you and your value b) how much room for negotiation you have (higher position in range = lower room for negotiation) and c) what your future increases will look like (higher in range = more moderate increases).

#### **Learning #5 - It is not only about base salary**

I am sure you already know that your pay package also includes benefits, allowances, and incentives. However, there are additional details to consider. Wrong assumptions lead to unnecessary disappointment, or to bad decisions.

#### **About benefits**

- Not all benefits are relevant to you. Ask if the company offers any flexible scheme in which you can choose the benefits that mean more to you.
- Not all companies offer competitive benefits. Even similar companies have different negotiation power and in consequence get more/fewer advantages from benefit providers. Always make sure that you look at details like coverage, periods, amounts, out of pocket expenses, etc. Typically there is a lot of qualitative information on the corporate web page that you can use. And ask if you have doubts.

#### **About Variable/Bonus**

- Some companies offer higher bonuses. How attractive they are will depend on your risk aversion, your cash flow, and on the amounts. In any case, I recommend to find out if targets have been met in the past, as it will give you a flavor of what you will be able to collect in the future.
- Bonuses are frequently expressed as a percentage of base pay. But in some cases, they are presented as a proportion of the whole package e.g. 20% over base salary is not the same as your bonus weighting 20% of the total compensation package. To avoid surprises down the road, ask, never assume.
- Make sure you know what is included in the bonus calculation. Some markets offer more than 12 payments as a practice (mandatory in some countries). Does your bonus calculation include those additional payments? Are allowances included in the calculation? If so, which ones? This can make a big difference between two offers.

#### **About Long Term Incentives**

- It is not infrequent to use the word “stock” and “stock option” interchangeably. But they are very different. A “stock option” refers only to the opportunity to buy shares at a pre-specified

price and collect any appreciation upon selling. By definition, options are valued lower than stock. Pay attention to what is being offered to you.

- If you expect a larger base pay to offset stock lost in a negotiation, you will probably be disappointed. The basic compensation principle is to cover long term pay with long term (e.g. stock with stock) and vice-versa.

### ***A Few Considerations on Global Assignments***

- If you are being considered for a cross-border move, I suggest you look beyond pay and make sure that the assignment is aligned with your life and career plans. Trying to establish pay equivalences between countries will not get you anywhere, and may lead you to wrong decisions.
- Keep in mind that full expatriation packages are not as common today as they used to be. Companies are migrating to “local-plus” arrangements, which mean local salary with some additional allowances. If this is the case, you will be paid in local currency. I’ve seen two common errors here:
  - Using only FX Conversion to determine the new salary at the host: cost of life is different everywhere, as well as compensation practices. If you want to know the equivalency, ask your company to make a *net-to-net* comparison to ensure you will keep similar living standards.
  - Using the same position within the salary range at the new location. Salaries are structured differently from one country to the next as markets differ; therefore, position in the range hardly translates correctly. Instead, ask how well the offer compares vs. peers at the host and vs. similar jobs in that market.
- The concept of “Benefit” is not the same everywhere. For example, some locations include allowances and working tools on the list of benefits. Make sure you are clear about what is included as a benefit at the host as this can have tax implications for you.
- Expatriation packages used to include a “Tax Equalization” component to ensure employees do not pay additional taxes than those at home. But due to high cost, “Local-Plus” packages rarely include this equalization. Make sure to ask for tax support so you can understand how income taxes at the host will affect you.
- Learn about your health coverage well. If you go on an assignment and return, after a few years your insurance circumstances may change (preexisting conditions, etc.). Make sure you clarify this well.
- Learn how your pension scheme will be affected by the move. Even if the company has an international pension plan, portability does not work the same everywhere. Make sure you get this straight too.

In the past, being an expat was perceived as an opportunity to save a lot of money. While this may still hold true in some cases, many companies view expatriation today more as an investment *on you*, and also expect the same *from you*. And with the new local-plus packages, both the company and the assignee have high stakes at play. Make sure you are well informed to make wise decisions.

### ***Final thoughts***

As you can see, there are multiple considerations when it comes to how pay is assigned. I made an effort to summarize the most important aspects, using simple language. However, be mindful that pay

practices vary by company, by industry, geography, job level (e.g. executive vs. non-executive), type of population (e.g. exempt vs. nonexempt, salaried vs. hourly), etc. But despite this complexity, if you understand the basic principles offered here, I am confident that you will have better salary conversations.

I invite the dozens of Compensation and Benefits professionals on my LinkedIn network to add their thoughts. I am sure all readers can also benefit from this experience. And if you have questions, please visit [www.IsraelLozanoUSA.com](http://www.IsraelLozanoUSA.com) and click on "Contact" to access my email. I will reply as soon as possible.