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Risk Management

Human Resource Management: Employee Compensation Guide

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Most managers think in terms of: "What do I have to pay to . . .?" That is not an easy question to answer. A better question might be: "What do I want my compensation package to say?" It is already saying a lot, whether you realize it or not.

Compensation can be linked to business structure and to employee recruitment, retention, motivation, performance, feedback and satisfaction. It is typically among the first things potential employees consider. For employees, compensation signifies not so much how they are paid, but how they are valued.

What is a Compensation Package?

It's easy to think "dollars per hour" when thinking about compensation. However, successful compensation packages go a lot further and can be considered total rewards systems that contain non-monetary, direct and indirect elements.

- **Non-monetary compensation** is any benefit an employee receives from an employer or job that does not involve tangible value. This includes career and social rewards such as job security, flexible hours, opportunity for growth, praise and recognition, task enjoyment, and friendships.
- **Direct compensation** is an employee's base wage, which can be an annual salary or hourly wage, plus any performance-based pay an employee receives, such as profit-sharing bonuses.
- **Indirect compensation** is far more varied. It includes everything from legally required public protection programs such as Social Security to health insurance, retirement programs, paid leave, child care or moving expenses.

All types of compensation are important. Employers have a wide variety of compensation elements to choose from and are limited as much by their own preconceptions about compensation packages as they are by budget restraints. By combining many of these compensation alternatives, progressive managers can create packages that are as individual as the employees who receive them.

The general consensus of recent studies is that pay should be tied to performance to be effective. However, with agricultural jobs, that is not easily done. A manufacturing company may offer a bonus for meeting a performance objective, but farm performance is affected by many factors over which employees have no influence. Successful managers must then search for areas the employees do influence and base performance objectives on these areas. Your farm may benefit from offering tenure bonuses for long-time employees, equipment repair incentives to encourage good equipment maintenance, or bonuses for arriving at work on time.

RISK MANAGEMENT EDUCATION

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Direct Compensation Alternatives	
Base pay:	Cash wage paid to the employee *Because paying a wage is a standard practice, the competitive advantage can come only by paying a higher amount.*
Incentive pay:	A bonus paid when specified performance objectives are met *Incentives may inspire employees to achieve higher performance levels and motivate them to accomplish farm goals.*
Stock options:	A right to buy a piece of the business, which may be given to an employee to reward excellent service *An employee who owns a share of the business is far more likely to go the extra mile for the farm.*
Bonuses:	A gift given occasionally to reward exceptional performance or for special occasions *Bonuses can show that an employer appreciates his or her employees; they ensure that good performance is rewarded.*

Indirect Compensation Alternatives	
Flexible working schedules	Elder care
Retirement programs	Moving expenses
Insurance (health, dental, eye)	Subsidized housing
Paid leave (sick, holiday, personal days)	Subsidized utilities
Tickets to events (ball games, concerts)	Magazine subscription
Boots and clothing	Laundry service
Wellness programs	Use of farm trucks or machinery
Farm produce, foods, meals	Cellular phones, pagers
Child care	Use of farm pastures and gardens

The perks farm employers provide give them a competitive edge over other employers. Some kinds of indirect compensation are required by law, such as social security, unemployment and disability payments. Other indirect elements are up to the employer. For example, a working mother may take a lower paying job with flexible hours so that she can be home when her children get home from school. A recent graduate may be looking for stable work and also an affordable place to live. Both of these individuals have different needs and, therefore, would appreciate different compensation elements.

Determining the Cash Wage

Ask ten different people what a fair wage is and you'll get ten different answers. While there are no hard and fast rules for determining a fair wage, the importance of the task is obvious. Research indicates that employees expect wages to: 1) cover basic living expenses; 2) keep up with inflation; 3) provide some funds for savings or recreation; and 4) increase over time. Discussing wage expectations with employees can help determine what your compensation package should look like.

The first thing employers should consider when developing compensation packages is fairness. It is vital that businesses maintain internal and external equity. Internal equity refers to fairness between employees in the same business, while external equity refers to wage fairness as compared to other farms or businesses. No matter the compensation level, if either internal or external equity is violated employees may become dissatisfied. This becomes apparent through decreased productivity, absenteeism, or employees leaving the business.

So, what constitutes a fair wage? One approach to determining a fair wage is a market survey. This is a fast and easy way to establish compensation guidelines for many businesses. A few phone calls to other employers in similar businesses can determine the "market" value for a specific job. Unfortunately, this technique is not necessarily well suited for agricultural producers. An agricultural manager can do informal surveys of other agricultural producers to determine the "going rate" for labor, or modify existing studies of non-agricultural businesses to compare employees by skill sets rather than job titles. For example, operating a forklift in a factory and driving a tractor may require similar skills and therefore can be compensated similarly.

Job evaluation is another technique that can be used to establish an equitable wage rate. This method is a more systematic and rational approach to internal equity because it evaluates workers according to factors such as education, skill, experience and responsibility.

Skill-based pay is an approach that bases the wage rate on the qualifications of the individual doing the job, rather than on the job itself. Employees with similar skills are grouped together, regardless of job title, to form skill classes or grades. These classes determine pay level. This technique can be applied to agricultural enterprises rather easily.

Broadbanding was used in a Cornell University study. Five competency levels were developed to classify employees according to their decision-making authority, skill level, and supervisory capacity. Every employee was classified as being in one of the following five competency levels:

- **Level one:** Employees who are either very new to the farm or have no advanced skills.
- **Level two:** Very specialized individuals who perform from one to many specific tasks that require training.
- **Level three:** Employees who are very skilled in at least one specified area and have supervisory capacity and decision-making authority over a very limited portion of the business.
- **Level four:** Employees with exceptional skill levels, who make decisions that affect entire areas of the operation. These people have potential for broad supervisory and decision-making authority.
- **Level five:** These are the most skilled and qualified full-time employees. They have complete supervisory authority and the most decision-making authority given to any full-time employee.

By using a competency scale, each employee can be cross-referenced by job title and competency level or studied solely within either category. Employees with similar skill levels, or competency, are taken together in compensation "bands," regardless of job title. These bands then compensate similar employees at similar rates across the entire organization and maintain both internal and external equity.

Conclusions

Farm managers face many decisions every day. Finding the time to build and implement an equitable wage structure can be difficult. Using the following checklist can make the process easier.

1. Decide what you want your compensation package to do:
   - Recruit new employees
   - Motivate current employees
   - Reward employees for good performance
   - Minimize risk of violating federal laws
   - Build employee loyalty
   - Any combination of the above
2. Pick your compensation philosophy, either:
   - Job evaluation
   - Employee evaluation
   - Combination of both (like the Cornell Study)
3. Determine your internal wage structure, either:
   - Evaluate the jobs
   - Evaluate the employees
   - Create competency groupings
4. Talk to your employees about their indirect compensation needs:
   - Health insurance
   - Paid vacation
   - Housing
   - Child care
   - Retirement planning
5. Structure your total rewards system, including:
   - Indirect compensation (based on your employee's needs and your compensation objectives)
   - Direct compensation (based on labor market information and your compensation objectives)
6. Implement your new system, remembering to:
   - Communicate with your employees about their needs
   - Review your compensation package regularly to make sure it is fair, equitable and competitive

- Be flexible and innovative to maintain a competitive advantage
- Maintain both internal and external equity

Successful agricultural producers rely heavily on common sense when it comes to management decisions. The area of employee compensation should be no different. If you want your employees to be innovative, reward them for new ideas. If you want your employees to stay with you for a long time instead of having to train new employees every season, offer bonuses or tie their wages to their tenure. If you need employees who show up on time, work hard, and can be trusted with the most challenging of tasks, recruit those people; reward those people; promote those people. The future of your business could depend on it.

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