

A Small Business Guide to COMPENSATION BENCHMARKING



Intro

These days, employment candidates are more informed than ever about the market value of their job. After searching online, they weigh their decision to join or not join your organization based on salary, benefits, commute time, opportunities for advancement, and more. According to the US Bureau of Labor Statistics, the unemployment rate for college graduates over age 25 is less than 2.5%. That makes for an incredibly competitive talent market.

Now factor in Millennials, who are bringing their 'fair pay' expectations to workplaces. Although, this expectation is something that all generations are rapidly getting behind. The concept of pay fairness doesn't mean compensating everyone the same. Rather, it means having a market-based understanding of job worth and then appropriately differentiating pay by factors like performance, skills, education, and experience. At a time when fair pay is increasingly legislated, these differentiators are both legal and necessary. Use the following steps to benchmark your jobs and develop pay guidelines in your organization.

Step #1 - Decide on Your Compensation Strategy

The first step to getting great market data is deciding on your compensation strategy. In your compensation strategy, you decide on the following key sets of information:

- Who is your talent market? Identify the industry, size, and location where you compete for talent, not necessarily where you compete for business. You may use just one market for comparison, or you may decide that for some functions you need a different market.
- Your compensation strategy should also reflect how competitive you want to be in your talent market. Are you looking to meet the market at the 50th percentile? Slightly exceed at the 65th? Be competitive at the 75th? Or maybe be aggressive at the 90th?
- Finally, your strategy should align the goals of your compensation program to your overall business objectives. Are you trying to drive performance, emphasize certain skills, or reward longevity? It's not enough to just define the strategy, you also have to earn employees' trust by being transparent about your strategy goals.

PRO-TIP

You may not be able to be as competitive in pay as your larger competitors down the street. That's ok. You definitely have something of value to offer your employees: doing meaningful work, having better work/life balance, and opportunities to have direct impact in organizational success are all strong motivators for the right kind of talent. Be sure to talk about what you have to offer with incoming candidates and existing employees alike.

Step #2 - Apply Your Compensation Strategy to the Data

Once you've identified where you compete, it's time to get some data for that market. Picking your market data is the most tangible part of your compensation strategy. Your data source or sources should give your organization the best quality, value, and data coverage. Apply your level of competitiveness to your data set in order to get the right segment for comparison.

When you're looking for data, keep these questions in mind:

- Is the data source fresh, accurate, and validated?
- Does the data source cover my industry, geography, and breadth of my jobs?



For data sources, you have a few basic options:



Step #3 - Match Your Jobs to Your Data Source

Once you've got your data source, it's time to match your jobs.

A) Select the positions within your organization that you wish to benchmark. When selecting your benchmark jobs, start with those positions that are standard across different industries, such as HR, accounting, and administrative roles.

B) Next, choose industry-specific positions that are standard at your company compared to positions in other organizations within your industry, such as civil engineer, registered nurse, and assembly line worker. You should try to obtain data for as many jobs as you can, with the understanding that not all jobs are benchmark jobs. By definition, a benchmark job is a job that regularly exists in the market.



There will be some jobs for which there are no appropriate market matches. That's ok. Using no data is definitely preferable to using bad data. Instead, we'll show you a better way to handle these positions next when we discuss the creation of guidelines for pay.

In a perfect world, your job descriptions would be current, accurate, and easy to translate into market data. Failing that, you can still do a market study by identifying the following for each job:

- Basic function, responsibilities, and level
- Experience, education, and certification
- Special skills required

At that point, it's time to actually identify the market data points in your data source.

PRO-TIP

Don't match on title alone. A manager isn't a manager isn't a manager. The actual scope of responsibility may differ from organization to organization. Take a careful look at the job tasks listed in your data source.

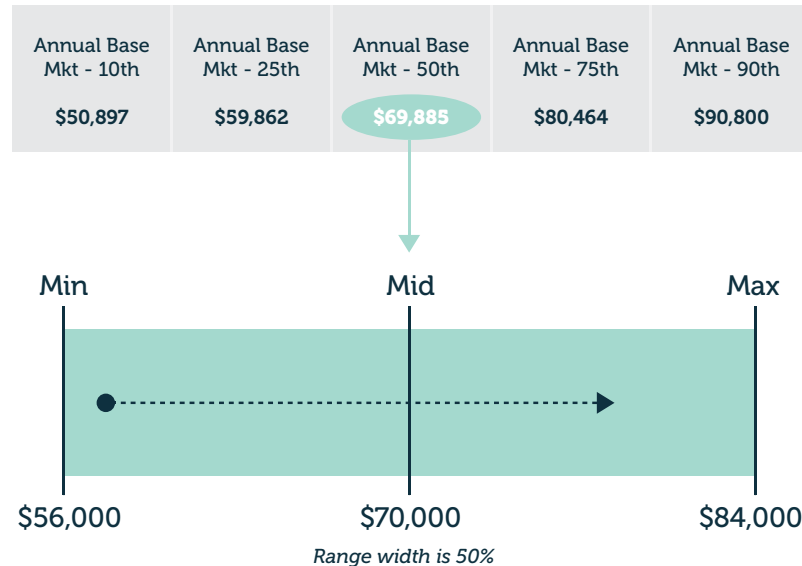
Step #4 - Turn Market Data into Guidelines for Pay or Pay Ranges

With your fresh market data in hand, it's time to make it actionable with pay ranges. Pay ranges help you apply market data points when determining what to pay your employees. They also help smooth out daily or monthly market fluctuations and set upper and lower bounds of possible pay.

- Establish your pay ranges. Pay ranges provide a min, mid, and max for each job in each geographic location. They are built using the market value for the job as the midpoint of the range.
- Determine range widths. Like most things in compensation there is no hard and fast rule here. As a general rule, your range widths should get wider as you go up levels in the organization. Ranges at the top are wider in order to allow for more differentiation of skill set, experience, performance, and longer tenures in the role. Widths should be narrower at the base of the structure to allow for movement between jobs.
- Calculate the minimum and maximum of ranges. The final step to creating a salary range is determining the minimum and maximum for the range. After you identify the midpoint for the salary range from the market, the following formulas will help you arrive at the min and max.

Formula for Range Calculations	Minimum = $\frac{\text{Midpoint}}{(1 + (\text{Range Width}/2))}$	Maximum = Minimum x (1+Range Width)
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The following illustrates calculating a range minimum and maximum:



Typically, you'd bring people into a job at or near the minimum of the range. As they gain in skills and experience, and begin to demonstrate high performance and deliver results, employees move through the midpoint of the range towards the max.

At this point, if you have jobs you were not able to benchmark, identify another job that is similar in terms of level of responsibility, skills, and value to the organization. Use the range for the similar job for your job without benchmark data.

If you are a growing organization, or an organization that has multiple job levels, you may consider developing a more formal pay structure with grades and ranges.

Step #5 - Handle “Hot Jobs”

There will be times when meeting your company’s goals will require paying at a premium. This usually happens when you need highly specialized skills and to retain or fill ‘hot jobs,’ where the market pay has been increasing due to higher demand. Typical approaches to salary benchmarking will not apply to these positions.

When this happens, here are some options:

- Double-check the job match and market movement for the job.
- Consider offering a market premium in the form of variable pay. For example, if the average of the market data for the hot job is 20% above the market rate for the midpoint of the range, consider offering a market premium bonus for people in this job. Make the premium contingent on a certain level of performance. Be as transparent with employees as possible about the market premium, then when the job is no longer hot you can more easily explain why the premium needs to be taken away.
- Develop a special market premium pay range for the job. Again, this should be clearly communicated, so if the job becomes less ‘hot’ you can adjust the range back down. This option would then apply to all employees in the job, regardless of performance or demonstrated results.

Conclusion

In order to compete in today's market, your organization must know what the market pays for certain skills so you can develop fair and competitive offers. Understanding the market, then determining guidelines for pay isn't just a nice to have for today's talent, it's a must have. Visit [PayScale's Resource Center](#) for more free content, or [reach out](#) to hear how we can help benchmark your jobs.

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