

RESEARCH PAPER ON COMPENSATION- INDIAN CONTEXT

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INTRODUCTION

1.1. Compensation

Efforts of employees are to be compensated for their efforts based on volume of time or volume of production. Compensation refers to all forms of financial rewards received by employees. It arises from their employment. It occupies an important place in the life of the employee. It is a considerable cost to the employer. Compensation dissatisfaction can lead to absenteeism, turnover, job dissatisfaction, low performance, strikes and grievances. Majority of labor-management disputes relate to compensation.

“Compensation refers to the extrinsic rewards that employees receive in exchange for their work. It is composed of the base wage or salary and incentives or bonuses and any benefits.”

Byars and Rue

Compensation is a key factor in attracting and keeping the best employees and ensuring that the organization has the competitive edge in an increasingly competitive world. The Compensation component enables to differentiate between the remuneration strategies and those of competitors while still allowing flexibility, control and cost effectiveness. It provides a toolset for strategic remuneration planning that reflects the organization culture and pay strategies, and it empowers line managers within a framework of flexible budget control. Compensation management allows controlling bottom-line expenditures and offering competitive and motivating remuneration, being it fixed pay, variable pay, stock options, merit increases, or promotion – in other words, total compensation.

1.2. Types of Compensation

Compensation can be of two types. They are Direct or Indirect Compensation

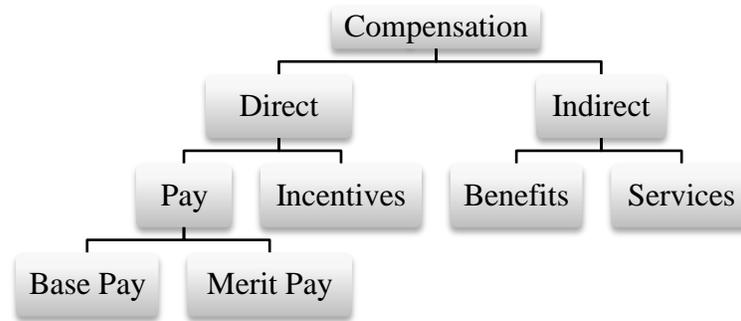


Figure 1 Types of Compensation

Source: Dynamics of Human Resources Management, Tower Watson

Direct compensation is remuneration provided to employees in exchange for their labor and services. What makes it direct is that it is given to the employee without an intermediary. Under direct compensation there are two sub types of compensation.

- Pay: It consists of wages and salaries received for performing work. It can be base pay and merit pay based on job performance.
- Incentives: They are provided for higher performance. They can be piece wage, commission, bonus, profit sharing, stock option etc.

Indirect compensations are provided for the employee's benefit, but are not given directly to the employees. Under indirect compensation there are two types of compensation

- Benefits are the payments addition to pay. They can be
 - Pay for time not worked: Paid vacation, holidays, leaves
 - Protection Programs: Pension, gratuity, insurance etc
 - Executive Benefits: Free Newspapers, telephone rental, car, flat etc
- Services and Perquisites: They increase employees wellbeing at no cost or significantly reduced cost to employees. They can be
 - Housing, transport, food
 - Loans, children's education expenses
 - Discount on purchases, credit cards
 - Social-cultural recreational activities; club subscriptions.

1.3. Compensation as component of Human Resource Management

Compensation management consists of designing the lowest cost pay structure that will attract, retain, and motivate the competent employees and which is perceived as fair by the employees. However, compensation systems should balance organization's ability to pay with employee satisfaction.

1.3.1. Objectives of compensation management

The following are the objectives of compensation management:

- An ideal compensation system will have positive impact on the efficiency and results produced by employees. It will encourage the employees to perform better and achieve the standards fixed.
- It will raise the morale, efficiency and cooperation among the workers. It, being just and fair would provide satisfaction to the workers.
- Sound Compensation/Reward System brings peace in the relationship of employer and employees, collective bargaining generally focus on compensation issues
- The perfect compensation system provides platform for happy and satisfied workforce. This minimizes the labor turnover. The organization enjoys the stability.
- The business organization can think of expansion and growth if it has the support of skillful, talented and happy workforce.
- The sound compensation system is hallmark of organization's success and prosperity. The success and stability of organization is measured with pay-package it provides to its employees.

1.4. Job Evaluation

Job evaluation is one of essence of compensation administration and the establishment of pay structure. Job evaluation uses the information collected through job analysis and systematically determines the value of each job in relation to all jobs within the organization. Job evaluation seeks to rank all the jobs in the organization and place them in a hierarchy that will reflect the relative worth of each and determines the organization's pay structure.

1.5. Job Evaluation Methods

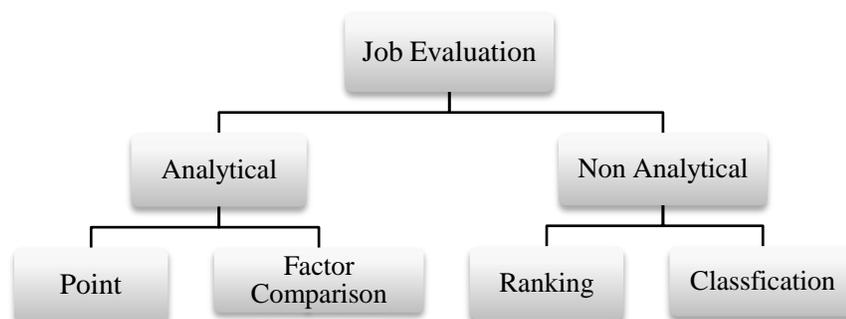


Figure 2 Job Evaluation Methods

Source: Compensation management – Ramaswami and namakumari

1.6. Establishing Pay Structure

Once the job evaluation is completed, its data become the nucleus for the development of the organization's pay structure. This means establishing pay rates or ranges that are compatible with the ranks; classifications or points arrived at through job evaluation. The pay structure can be determined through following process.

1.6.1. Wage survey

Wage survey is the systematic gathering of factual information on pay practices from comparable firms within or outside the industry. The gathered information gives an idea of the standard market practices which are used to set the actual wage levels. The data can be generated or the organization can collect the data through secondary sources such as publications, research firms or organization can generate the data through primary sources such as conduction their own surveys. Typically the structured question comprises of questions like wage ranges for jobs, overtime pay, festival allowances, bonuses, length of normal workday and workweek etc.

1.6.2. Wage Curves

When management arrives at point totals from job evaluation and obtains survey data on what comparable organizations are paying for similar jobs, then a wage curve can be fitted to the data. A complete wage curves tells management the average relationship between points of established pay grades and wage base rates.

| Jobs | Total points (derived through job evaluation) | Monthly salary in "000" (found out through wage survey) |
|--------|---|---|
| Job 1 | 10 | 8 |
| Job 2 | 20 | 10 |
| Job 3 | 30 | 12 |
| Job 4 | 40 | 14 |
| Job 5 | 50 | 16 |
| Job 6 | 60 | 18 |
| Job 7 | 70 | 20 |
| Job 8 | 80 | 30 |
| Job 9 | 90 | 40 |
| Job 10 | 100 | 50 |

Table 1 Job points and Monthly Salary

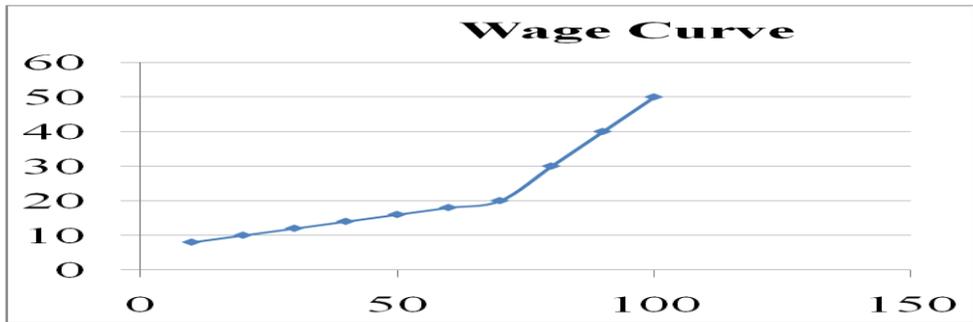


Figure 3 Wage Curve

Source: Compensation management – Ramaswami and Namakumari

1.6.3. Wage structure

It is only a short step from plotting a wage curve to developing the organization’s wage structure. It is the final step in establishing the pay structure. The points are grouped into buckets and accordingly pay grades are defines for each bucket.

| Points range | Monthly salary range in "000" |
|--------------|-------------------------------|
| 1-10 | 8-13 |
| 11-20 | 12-17 |
| 21-30 | 16-20 |
| 31-40 | 19-23 |

Table 2 Salary Range

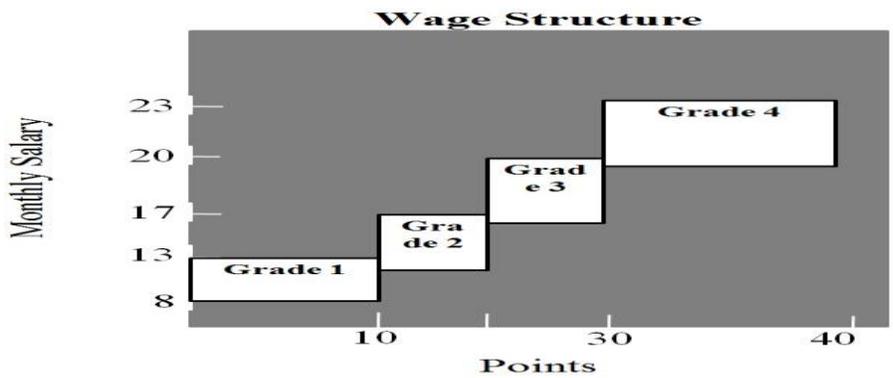


Figure 4 Wage Structure

Source: Compensation Management – Ramaswami and Namakumari

1.7. Incentive Compensation Plan

In addition to the basic wage structure, organizations that are sincerely committed to developing a compensation system that is designed around performance will want to consider the use of incentive pay. Incentive can be paid based on individual, group or organization wide performance

1.7.1. Individual Incentives

Individual incentives plan pay off for individual performance. Popular approaches include piecework plans, time-saving bonuses and commission.

Under straight piecework plan, the employee is typically guaranteed a minimum hourly rate for meeting some pre established standard output. For output over this standard, the employee earns so much for each piece produced.

Individual incentives can be based on time saved as well as output generated. As with piecework, the employee can expect a minimal guaranteed hourly rate, but in this case the bonus is achieved for doing a standard hour's work in less than sixty minutes. Employees who an hour's work in fifty minutes can do obtain a bonus that is some percentage of the labor saved.

Sales personnel frequently work on commission basis. In addition to low wage rate, they get an amount that represents a percentage of the sales price.

1.7.2. Group Incentives

Each of individual incentive can also be used on a group basis. That is two or more employees can be paid for their combined performance. One problem with group incentives is that employees do not see them as being directly linked to their own behavior. The pay of the employee under group incentives is influenced by the behavior of others with whom that employee works.

1.7.3. Organization wide incentives

The goal of organization wide incentive is to direct the efforts of all employees toward achieving overall organizational effectiveness. This type of incentive produces rewards for all employees based on organizational wide cost reduction or profit sharing

1.8. Executive compensation

Executive compensation is significantly higher than the benefits given to the middle level managers and operational staff. This is how executive of business corporations are paid which includes basic salary, bonuses, shares, options and other company benefits. There are three components of executive compensation they are explained below:

1.8.1. Executive Salary

Top managers are expected to demonstrate good decision making abilities. Eventually the supply of qualified senior executives is scarce, and organizations have bid up the price for this talent. They too must keep their salaries in line with the competition or potentially lose an executive to another organization. High salary also acts to motivate both top executives and lower level managers. High pay encourages top level managers to perform well in order to keep their jobs. But high pay also acts to stimulate lower level managers to work hard so that they can someday move up the ladder to the 'big money'.

1.8.2. Supplement Financial Compensation

Financial incentives like bonuses or stock option plans are the exception among rank and file workers, but it is the rare senior business executive whose compensation does not include such incentives. The executive's bonus is computed on the basis of some formula, usually taking into account increases in sales and profits. This bonus although earned in the current period is distributed over several future periods. The major purpose of such deferred compensation is to increase the cost to the executive of leaving the organization.

Similarly stock options have been a common incentive offered to executives. They generally allow executives to purchase, at some time in the future, a specific amount of the company's stock at a fixed price. Under the assumption that good management will increase the company's profitability and, therefore the price of the stock. Stock options are viewed as performance based incentives

1.8.3. Supplement Non- Financial Compensation

Executives are frequently offered benefits of perquisites not offered to other employees. These benefits includes such as medical insurance, life insurance, interest free loan, club membership, vehicles/fuels, quarters, supplemental retirement accounts etc.

LITERATURE REVIEW

2.1 Kentucky and Charlotte-Mecklenburg Studies of Teacher Attitudes

This study found that teachers considered 'goal attainment rewards', including payment bonuses for attaining rewards and the public recognition from attaining these rewards, as very important. 'Learning' outcomes were also important for the teachers surveyed (Heneman and Milanowski, 1999), including seeing and being responsible for improvements in student performance and working collaboratively

with peers. This may be rhetoric, as the actual evidence supports the hypothesis that teachers are motivated by financial rewards. While teachers in the Kentucky school-based rewards system rated 'school improvements' as more beneficial than extra salaries in the research conducted, when teachers allocated program rewards, 98% voted to use some or all of the rewards as a salary bonus (Kelley, 1999). There was some concern in relation to goal clarity in school-wide program, meaning there would be some concern about the motivational capacity of schools (Kelley, Heneman and Milanowski, 2002). Despite this concern, Kelley, Heneman and Milanowski (2002) concluded that teachers knew about school goals, and were committed to them. Other analysts have taken these results to show that school-based performance awards also support school improvement efforts (see, for example, Tomlinson, 2000), as there are motivation impacts from both positive and negative circumstances.

Teachers were concerned that they would not be paid the bonus upon successful completion of school-wide criteria. "A striking finding in both the qualitative and quantitative data from both program sites was the low perceived probability that the bonus would actually be paid when school goals were met." (Kelley, Heneman and Milanowski, 2002)

In conclusion, Kelley, Heneman and Milanowski (2002) argued, that in all models, the higher the average teacher expectancy of student results, the greater the school-based evaluation outcomes. These analyses, it is argued, shows that between-school differences in teacher expectancy are a predictor of schools' future outcomes. "Overall, we believe that our results suggest that SBPA programs have the potential to contribute to motivating teachers to improve student achievement. However, the potential was not fully realized in these first-generation programs. The implication is that program designers should set goals that are perceived by teachers as achievable and should develop coherent systematic approaches to support goal attainment...These considerations suggest that providing a bonus may be the least problematic aspect of a SBPA program, whereas setting realistic goals, maximizing perceptions that achieving the goals will lead to positive outcomes, minimizing stress reactions, and providing enabling conditions are where effort and attention need to be focused. Motivational impact is not guaranteed simply by promising a bonus."

2.2 Ballou and Podgursky's Study of Teacher Attitude

The conclusions of Ballou and Podgursky are somewhat limited in their application to current performance-based reward systems. First, their conclusions are based on old data. The extent to which these attitudes can now be generalized is unknown. More recent research would be needed, especially given the growth of performance-related pay as an issue since this data was gathered. Teacher attitudes may have changed significantly since this survey given the recent level of debate surrounding performance-related pay.

Second, these conclusions are limited in the extent they can be generalized to other performance based pay system because the question format of the survey does not reflect the reality of contemporary

program. The survey asked teachers about their attitudes to 'additional pay' so it is fair to assume surveyed teachers would have concluded pay would supplement current income. This would have the effect of over-emphasizing support for merit-pay program for teachers, since these programs rarely supplement overall teacher income. While Ballou and Podgursky (1993) argue their findings would remain robust even given a change of wording or context, this is doubtful given the strong teacher opposition to merit-pay reported elsewhere (see Kelley, 1999). Even though the statistical analysis proved to be appropriate, there is considerable doubt whether these results on teacher attitudes would be replicated if different worded questions were used.

2.3 The Dallas School Accountability and Incentive Program (Clotfelter and Ladd)

For all four years, pass rates increased more in Dallas than they did in any of the control groups. However, there were gains before the program was fully implemented. This phenomenon could reflect a movement back to the state mean, or the positive effects of publicity of the program (Ladd, 1999). One possible positive conclusion is that Dallas schools maintained a consistent level of advancement even when the novelty of the program diminished, meaning the program was successful. Further evidence of increased student outcomes was apparent when the other cities were factored into the analysis. Dallas had increased student outcomes in comparison to all the control cities, except for one small district in one city that undertook reform comparable to Dallas. The relative pass rates of students of economic disadvantage, blacks, Hispanics, and students with limited English proficiency is lower as the percentage of each of these categories increase as a proportion of the grade (Ladd, 1999). The less transient the school population, the higher the average increase in passes rates.

Results based on race showed that in reading and math, Hispanic and white students in Dallas increased significantly more than Hispanic and white students relative to the baseline year and the control cities. There was no evidence that black students improved (Ladd, 1999). Differences in the number of teachers with at least five years experience, and the average number of pupils per teachers produced no significant results, with the exception of Hispanic students in math, who had increased pass rates the greater the proportion of teachers with over five years experience.

These results were complicated by the introduction by the Texas government of an aggressive policy aimed at increasing the resources of low-performing schools during the surveyed period. To overcome this, an analysis was done excluding 25% of schools with the highest proportion of students of economic disadvantage. The results followed the same pattern of the previous data, with significant increases in the scores white and Hispanic, but not black students (Ladd, 1999). The evaluation of the program depends on the interpretation of the first year results. If all the measured gains were true program impacts, then increases in student outcomes were in the order of 10 to 20% relative to the state average. If the gain in 1992 were because of a return to the mean, the program impacts can be viewed less favorably (Ladd, 1999).

The dropout rate of high-school student decreased more for Dallas than any other city in comparison across all years, with two years (out of three surveyed) showing significance. Turnover rates for principals jumped dramatically after the first year of the program. It appears that the school districts were more willing to change principals than in the past. Qualitative research suggests that these principals were either demoted or fired, so this does not represent a shuffling of poorly performing principals (Ladd, 1999). Ladd (1999) concludes that the turnover of principals is desirable as it represents district administration being more proactive in making principals accountable to student results.

Overall, Ladd (1999) concludes there is reason to be cautiously optimistic about performance based reward programs. The seventh grade results are positive and large, but only significant for Hispanic and white students. Other positive results are the reduction in dropout rates and the high turnover of principals. However, more research needs to be to examine the ranges of student increases in scores. Further research could be conducted to make a more accurate cost-benefit analysis of performance-based reward systems.

PRACTICES IN INDIAN ORGANIZATIONS

3.1 Compensation practices in Indian context

Compensations are practiced by every organization in every country. Thus some of the compensation administration that are practiced in context of India are explained below and covered under Employees compensation Act 1923. In addition, it is not applicable to the entire informal sector of the workers in the formal sector; the provision relating to social security is applicable only to the permanent ones. Otherwise these provisions are not applicable.

3.1.1 Formal Sector

Remuneration: The Remuneration includes:

Basic Pay: Basic salary is an amount which is paid to an employee in accordance with the grade in which he / she is placed.

Conveyance Allowance: This is also paid to all employees. Employees are also offered the option of buying vehicles at reduced prices.

House Rent Allowance: All the employees are entitled to this allowance max of 50% of the basic salary.

Cost of living Allowance: As per law employees are entitled to Cost of living allowance

Recreation Allowance: All the employees up to junior executive Grade are paid on a sliding scale, statutory special allowance.

Special Allowance: All employees are entitled to a special allowance as per their respective grade.

Social security benefits: There is no comprehensive social security system under the Indian labour law. Employees are entitled to receive following benefits as part of social security under the Labour Act and Rules.

Provident fund: Provident fund is a contributory old age benefit under the labour law. According to the provision, the employer should deduct 12 percent of basic salary + DA of the employees and add 12 percent to it (by the employer), out of this 8.33% of Basic + DA (maximum-6500) goes to EPS (Pension fund) with the Govt. and, the balance to employees PFa/c.

Gratuity: Gratuity is also part of an old age benefit. It is also known as a severance pay. As per the provision in the Labour Rules, the employees serving for five years or more and retiring from the service are entitled to get gratuity at the following rates:

Applicability: Any Employer of the above noted establishments where 10 or more persons are employed or were employed on any day of the preceding 12 months is liable to pay gratuity to its employees. Once the Act becomes applicable, it continues even if the number of employees falls below ten.

Entitlement: Gratuity is payable to an employee (nominee - in case of death of employee) who has rendered continuous service of five years or more on his termination of employment, superannuation, retirement or resignation. Completion of continuous service of five years is not necessary where the termination of employment is due to death or disablement.

Calculation: $W \times Y \times 15/26$ where W = Last Wage drawn i.e., basic + DA

Y = number of completed years of continuous service (six months or less to be ignored and more than six months to be counted as full year.

15 = 15 days salary

26 = No. of working days in a month.

Maximum Limit: Rs.3.5 lacs. (W.e.f 24-09-1997)

Time Limit for application to employer: Employee has to make an application in Form-I to his employer within 30 days from the date of gratuity becomes payable.

Salary during treatment: During the period of treatment, employer should pay full salary for the period of their stay in hospital or half of their salary if they have undergone treatment at home.

However, if the period of such treatment exceeds a year, the employer is not obliged to pay the salary after one year.

Disability compensation: If an employee is physically disabled as a result of an accident while in employment, the employer must pay a lump sum amount equivalent to the salary of five years of the last drawn salary in case disability is found to be 100 percent. In case disability is less than 100 per cent, the amount of compensation shall be calculated according to the percentage of disability. The percentage of disability should be determined by a doctor recognized.

Sick Leaves: All workers or employees who have completed one year of service in the establishment without any interruption shall be granted a sick leave with half-pay for not more than 15 days in a year.

Maternity Leaves: Pregnant women workers or employees shall be granted a maternity leave with full pay for 52 days before or after delivery. Such a leave may be obtained not more than twice during the entire period of service. However, in the event of the death of two children of a woman employee, who has already utilized the maternity leave twice, she may be entitled to a maternity leave for two times more.

Change by collective bargaining: An employee working in the organization has the right to union. Ten or more employees working in an organization can form a Plant Level union. The Plant Level union has the right to submit a charter of demand and bargain collectively with the management. The collective agreement may change social security provisions of a particular organization. This can be settlement shall be valid for up to two years.

3.1.2 Informal Sector

There is no concrete social security arrangement for the informal sector. Some of the workers working in the informal sectors are covered partly by the legislation.

There is no provision for social security benefits for workers in the informal sector. They are treated as a general citizen and are provided with some sort of relief on an ad-hoc basis, such as the senior citizen allowance.

3.2 Compensation practices in Indian Organizations

Compensation is essential for the motivational factor of employee. It is the key factor in attraction the best employees and retaining them to have the competitive edge in competitive world by the organization. Thus Indian organization too practices the compensation management. Here are some of the nature of the organization and the types of compensation schemes that the Indian organization practices.

Financial Institution

Financial Institution such as Commercial banks, finance companies provide their employees with various kinds of benefit like providing stock option, shares in the organization to ensure that the employees too are the owners of the organization. By doing this, not only the employees are compensated but also they are motivated in the performance.

Similarly this institution provides its employee with the Earned leave generally for 15 days for which the employees aren't cut any salaries i.e. although the employees are in leave they can earn their salary. Besides sick leave and casual leaves, these institutions also provides with the various perks, benefits and bonuses during national festival like Diwali etc.

CONCLUSION

Compensation Management is an integral part of the management of the organization. Compensation is a systematic approach to providing monetary value to employees in exchange for work performed. It may achieve several purposes assisting in recruitment, job performance, and job satisfaction. It is the remuneration received by an employee in return for his/her contribution to the organization. It is an organized practice that involves balancing the work-employee relation by providing monetary and non-monetary benefits to employees. Compensation Management contributes to the overall success of the organization in several ways. To be effective, the managers must appreciate the value of competitive pay, their human resources, and have an investment view of payroll costs. We want to maintain pay levels that attract and retain quality employees while recognizing the need to manage payroll costs.

The increasing competitiveness of the labor market and turnover of employees had resulted in nightmare in compensation planning. Apart from this, the growing demands of the employees and competitive salaries offered by multinational companies had almost resulted in a compensation war in certain industries. Therefore, the human resources managers and tax experts have to evolve proper compensation planning for High end and qualified employees. The components of compensation have to be devised in such a way that, it focuses on the growing demands of employees while retaining the competitiveness and profitability of the company.

Compensation management is concerned with designing and implementing total compensation package. The traditional concept of wage and salary administration emphasized on only determination of wage and salary structures in organizational settings.

Jobs are accepted or rejected based in part on starting salary and the opportunity for future increases in pay. Employees compare their pay to that of others in the same line of work. They constantly compare

their pay level to their level of contribution, trying to determine whether the ratio of give and receive is a fair one. While it may not be a frequent topic of open discussion, employees think about pay often.

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