



Compensation Philosophy Resources

What is a compensation philosophy? What should be included in a compensation philosophy? (Source: SHRM.org)

A compensation philosophy is simply a formal statement documenting the company's position about employee compensation. It essentially explains the "why" behind employee pay and creates a framework for consistency. Employers can benefit from being transparent about their compensation philosophy and having an official pay strategy.

Compensation philosophies are typically developed by the human resources department in collaboration with the executive team. The philosophy is based on many factors, including the company's financial position, the size of the organization, the industry, business objectives, salary survey information, and the level of difficulty in finding qualified talent based on the economy, as well as the unique circumstances of the business. It is important for the compensation philosophy to be reviewed periodically and modified based on how well it is working and current factors affecting the business. For example, market conditions may make it really difficult to find qualified talent in a particular specialization, and an employer may need to pay a premium for these candidates. If the employer's current compensation philosophy does not support this value, then the organization may need to change its philosophy to meet its current needs.

A well-designed compensation philosophy supports the organization's strategic plan and initiatives, business goals, competitive outlook, operating objectives, and compensation and total reward strategies.

As such, most compensation philosophies seek to:

- Identify the organization's pay programs and total reward strategies.
- Identify how the pay programs and strategies support the organization's business strategy, competitive outlook, operating objectives and human capital needs.
- Attract people to join the organization.
- Motivate employees to perform at the best of their competencies, abilities and skill sets.
- Retain key talent and reward high-performing employees.
- Define the competitive market position of the organization in relation to base pay, variable compensation and benefits opportunities.
- Define how the organization plans to pay and reward competitively, based on business conditions, competition and ability to pay.

An effective compensation philosophy should pass the following quality test:

- Is the overall program equitable?

- Is the overall program defensible and perceived by employees as fair?
- Is the overall program fiscally sensitive?
- Are the programs included in the compensation philosophy and policy legally compliant?
- Can the organization effectively communicate the philosophy, policy and overall programs to employees?
- Are the programs the organization offers fair, competitive and in line with the compensation philosophy and policies?

While HR is clearly in the lead in developing an organization's compensation philosophy and policy, success lies in close collaboration with the leadership team to obtain valuable input, direction and concurrence.

EXAMPLE

Direct Relief (a CA nonprofit)

Direct Relief seeks to recruit and retain qualified, high performing, and motivated employees to fulfill the organization's mission and support the organization's strategies and values. Fair compensation of employees is integral to this goal.

In establishing compensation levels, Direct Relief recognizes that its character as a public benefit nonprofit employer creates special considerations that relate to public trust and confidence.

The policy of Direct Relief is to provide compensation that is fair, reasonable, and consistent with compensation paid in the nonprofit sector for positions of comparable complexity and responsibility. The goal of this policy is to recruit and retain high-performing employees and to motivate, recognize, and reward excellent performance.

The bases upon which compensation is provided to each employee shall be documented and reviewed by management and the Board of Directors. The compensation of executive staff is determined by the Board of Directors. [...]

On an annual basis, the organization shall review the compensation level for each staff position. This review shall include a comparative analysis of compensation paid by Direct Relief to compensation paid by local, sector, and national nonprofit organizations. This analysis shall also consider compensation levels within the local Santa Barbara employment market, including compensation at for-profit entities. This process is designed to benchmark Direct Relief's practices against relevant market data.

At least two surveys shall be used to assess compensation in the nonprofit sector for each staff position. In making such comparisons, job descriptions, special requirements and skills, and the level of complexity and responsibility related to each position are examined. Surveys currently used for benchmarking purposes include:

- Local Labor Market Benchmark: Santa Barbara Human Resources Association Benefits & Compensation Survey (Santa Barbara: Santa Barbara Human Resources Association) or the

regional data from the U.S. Bureau of Labor Statistics, if no equivalent position is provided in the SBHRA data.

- Regional Nonprofit Sector Benchmark: Center For Nonprofit Management Compensation & Benefits Survey of Southern & Central California Nonprofit Organizations (Los Angeles: Center for Nonprofit Management).
- • National Nonprofit Sector Benchmark: Guidestar Nonprofit Compensation Report (Williamsburg: Philanthropic Research, Inc.)
- U.S. International Nonprofit Sector Benchmark: InsideNGO U.S. Headquarters Salary, Benefits, and Human Resources Policies Report (Westport: InsideNGO).

(Note: The above surveys are published annually, and the then-most recent and available survey is used for annual benchmarking purposes.)

Annual Performance Review. All employees receive annual performance reviews conducted by their supervisors. The annual performance review of the Chief Executive Officer is conducted by the Chairman and approved by the Executive Committee of the Board.

Compensation of the Chief Executive Officer, the Chief Financial Officer, the Chief Operating Officer, and other key staff are reviewed by the Compensation Committee of the board, which makes recommendations on compensation for such positions to the Executive Committee.

Avoidance of Conflict of Interest regarding Compensation Decisions. Decisions regarding executive staff's compensation are the sole responsibility of the Board of Directors. No member of the staff, including the Chief Executive Officer and the Chief Financial Officer, is a member of the Board of Directors, and the Board of Directors may not delegate the authority to set executive compensation to a member of the executive staff. The foregoing policy is adopted to ensure that no member of the staff has a vote on any matter concerning compensation paid to himself or herself.