Remuneration – What's your definition of fair?

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In an increasingly tight labour market where unemployment rates are low and employees across all sectors and cities are challenging their employers about their 'worth' every day, the pressure is on for organisations to ensure they 'get it right'.

On that basis, the determination of a remuneration policy which is aligned to your organisation's objectives and which articulates the goals and principles of pay has become an essential tool for effective management. Common objectives of remuneration policy include principles such as:

- Attraction and retention of key talent
- Ensuring external (market) competitiveness
- Ensuring remuneration decision-making is fair and defensible.

One subject that attracts a lot of discussion and debate is this concept of fair remuneration or fairness in remuneration management. At the end of the day, what fair means to you as an employer, may be materially different than what it means to your employees. So who decides what is 'fair' and what are the key bones of contention here that are getting people so hot under the collar?

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What do we mean by fair?

What do we mean by fair? The dictionary seems as good a place as any to start. The Cambridge Dictionary offers the following definition of fair:

> *"treating someone in a way that is right or reasonable, or treating a group of people equally and not allowing personal opinions to influence your judgment."*

And fairness? Fairness is defined as

> *"considering everything that has an effect on the situation, so that a fair judgment can be made."*

Well, that still leaves quite a bit of room for interpretation. So what are the common schools of thought with respect to fairness in remuneration?

'Fairness' in traditional organisations

It is reasonably common in traditional/paternalistic organisations and/or environments where collective employment agreements predominate, to define fair in the following terms:

- All employees should be treated the same when it comes to remuneration
- Employees performing the same job should have the same pay.

In addition there is often the expectation that at salary review time, 'across the board' increases should be provided and that these should reflect CPI movements as a minimum.

So fairness in this sense is defined as people being treated the same and all employees having the right to expect that, as a minimum, their salaries/wages should be keeping up with inflation. *"If I can't buy the same amount of milk, bread and petrol with my earnings that I could last year, then that's unfair isn't it?"* Or is it?

'Fairness' in contemporary organisations

The school of thought seen more and more in performance-driven, contemporary organisations is to define 'fairness' in remuneration very differently.

The role of the individual in a job and their competence levels and performance can be considered a critical part in the establishment of a 'fair' remuneration outcome, especially at salary review time.

Many organisations are evolving their salary review approach away from the traditional 'across the board' increases, to an approach which enables managers to significantly differentiate remuneration outcomes for their staff, based on individual performance.

Differentiating performance 'fairly'

This concept of 'robbing Peter to pay Paul' – is a basic one. Let's assume Peter and Paul earn the same salary currently. If you have a 4% salary review budget, you don't have to give both Peter and Paul a 4% increase.
Peter is not competent in his role, has a difficult attitude and has problems with absenteeism. Paul is a godsend,

he's conscientious and driven and delivers above and beyond agreed performance targets.

In this scenario, perhaps Paul should be given an 8% increase while Peter receives no increase. The principle here is that to provide both Peter and Paul with the same increase, is actually <u>unfair</u> to Paul. If we don't differentiate Paul in a positive way to reward all the right behaviours he demonstrates, then what is his motivation to continue to perform in this way?

While money is often talked about as a motivator, it is just one element of many that contribute to job satisfaction. For example, a challenging position, good development opportunities, a good relationship with your manager are often cited as important to employees and potentially even more important than remuneration. So why then is it important to differentiate pay based on performance?

Why differentiate pay based on performance?

Because this provides <u>recognition</u> to the employee. At the end of the day, it's not necessarily the dollars, but the message you are sending to the individual about your recognition of their contribution which is so critically important to them and therefore to effective remuneration management.

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Employees learn very quickly whether there are genuine consequences for performance and for non-performance in their workplace. If we are not differentiating remuneration to reflect contribution and performance, then our high performers are likely to become demotivated, disenfranchised and eventually move on.

So why is it so hard for managers to create this differentiation and accept that the most commercial definition of fairness <u>may not</u> be treating everyone the same when it comes to pay?

New Zealand's society and culture has definite egalitarian influences and the 'tall poppy' syndrome is still strongly evident in our decision making and values. Managers often want to be perceived as nice/good people and to be liked by their employees. On that basis, we are not necessarily good at providing feedback on poor performance and 'going to the hard place' in terms of addressing issues with staff. There's no bones about it, a zero percent increase at salary review time sends a very clear message to employees, but it's a message that a lot of managers shy away from sending.

The other main reason that managers don't like the zero percent increase scenario, comes back to expectations that employees have with respect to CPI increases. There is still a strong 'entitlement culture' in New Zealand and an expectation that the employer needs to 'care' for the employee and guarantee them the same standard of living year on year. However, from a commercial perspective, there's a strong argument that it's <u>not</u> actually an employer's responsibility to ensure that an employee <u>can</u> buy the same milk, bread and petrol with their remuneration dollar that they could this time last year.

Summary

So, to summarise – have we decided what we mean by fair? What is fair? Ultimately, this is going to be partly driven by your personal and/or business philosophies and values.

To some, 'fair' means everyone gets an equal piece of the pie and a remuneration focus on keeping up with inflation and ensuring no one is 'disadvantaged'. In this scenario, the outcomes are likely to be:

- An entitlement mentality amongst staff regarding annual increments
- Pay having little link to performance – with decisions based on market movements or relativity
- Little differentiation in pay levels or increases between poor, average and high performers
- A focus on internal relativity (let's pay everyone about the same for doing the same job)
- Increasing fixed remuneration costs year on year, which are not linked to improved business returns.

To others, for whom performance is a vital part of business success, 'fair' will mean something quite different. It will mean:

- Remuneration and rewards are commensurate with performance and contribution
- Motivation and retention are being driven by this overt link to performance/ contribution (keeping high performers engaged through appropriate recognition)
- Demonstrating, through the differentiation of remuneration, the <u>value</u> of respective employees to your business
- Strong consequences for non-performance (i.e. exit) and strong consequences for high performance
- Using remuneration as a means of recognition to support/reinforce organisational objectives
- Management behaviours and decisions sending a clear consistent message about what's valued and rewarded
- Rewards being directly linked to performance, with managers confident to justify pay based on performance
- Maximising your return on your remuneration investment.

At the end of the day, our view is that remuneration is the most significant, tangible, visible statement of worth to an employee, by an organisation.

So with all that said, what <u>do you think</u> is the best definition of fair? We know which camp we are in – come on over!