

10th EDITION

# Strategic Compensation

A Human Resource  
Management Approach

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University of Illinois at Urbana-Champaign



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# Preface

## NEW TO THIS EDITION

*Strategic Compensation: A Human Resource Management Approach*, Tenth Edition, contains substantial new content and changes, including the following:

- Three new features appear in each chapter that enable students to integrate knowledge and valuable skills regardless of whether they are choosing a career in the compensation profession or other business functions in smaller or larger organizations.
  - **Ethics Dilemma.** Ethics is the discipline dealing with what is good and bad, right and wrong, or with moral duty and obligation. Most executives, managers, and professionals believe that integrity and ethical values have an important place in business and should form the foundation of a company's culture. Ethics focuses on individual decision making and behavior as well as the impact of ethical choices on employee welfare. The *Ethics Dilemma*, presented in the end-of-chapter material, will keep these important matters in the forefront as you move ahead in your career.

### Case 2: Ethics Dilemma: Pay for Performance Disconnect

You are the new vice president for HR of a company that has not been performing well, and everyone, including yourself, has a mandate to deliver results. The pressure has never been greater. Shareholders are angry after three years of a tough market that has left their company stock losing value every day. Many shareholders desperately need stock performance to pay for their retirement. Working for you is a 52-year-old manager with two kids in college. In previous evaluations, executives told him he was doing fine, when he clearly was not, and his performance is still far below par. At the same time, the executives awarded him impressive annual pay raises.

If you are to show others in the company that you are willing to make tough decisions, you feel you must fire this individual. The question is, who is going to suffer—the firm and, ultimately, the shareholders, whose retirements are in jeopardy—or a nice guy who's been lied to for 20 years?

#### Questions:

3-9. What would you do?

3-10. What factor(s) in this ethical dilemma might influence a person to make a less-than-ethical decision?

### FYI

Both private-sector companies and the federal government are competing for cyber security talent; however, the difference in annual pay between the government and private sector is staggering, particularly for chief information officer jobs:

- Private-sector: \$500,000 to \$2,000,000
- Federal government: \$123,175 to \$185,100<sup>14</sup>

- **FYI.** This feature provides tidbits of information from survey research and extensive databases (e.g., employment statistics) that illustrates trends, opinions, and the use of specific compensation practices.

### Working Together: Team Exercise

In small groups of three or four, come up with specific answers to the following questions. Talk through your perspectives and come up with a team response. Be prepared to share your ideas with the class.

We studied competency models in this chapter and viewed the U.S. Department of Labor competency model framework (Figure 5-1). The Department of Labor has the Competency Model Clearinghouse that contains several competency models across industries. As a group, review some of these competency models available on the *Careeronestop* website (<https://www.careeronestop.org/CompetencyModel/>) after clicking on the industry models link. Select a competency model from two industries.

#### Questions:

5-14. Summarize the information available on your chosen models. What are some of the similarities?

5-15. What are some of the differences in occupation- and industry-competencies between your chosen models?

- Other major updates to the tenth edition include:
  - Extend coverage of evolving compensation practices, statistics, and business professionals' perspectives. For instance, Chapter 3 (Traditional Bases for Pay: Seniority and Merit) includes a section on trends in performance appraisal practice. In a nutshell, some companies are providing performance feedback more frequently and as needed on a less structured basis rather than putting off providing feedback until structured annual reviews are given. This section also addresses the pros and cons of this more contemporary thinking as well the same for longstanding approaches to provide students a balanced view.
  - Chapter 15 has been converted into an Epilogue. It includes many important topics not covered in previous editions and makes significant updates to other topics. Some of the topics are the compensation productivity gap, the gender pay gap, and pay transparency.
  - Fifty percent of the Cases and nearly fifty percent of the Crunch the Numbers features are new.

## SOLVING TEACHING AND LEARNING CHALLENGES

Increasingly, students expect to see the applicability of their coursework to life and work after graduation. When the connection is not clear to students, many may lose interest and, perhaps, choose to do as little as possible to earn a good enough grade on quizzes and exams. The choice of pedagogical features and the writing style in this text would pique interest in the subject matter and enhance learning and development of seven critical employability skills, which have been discussed in the ‘Developing skills for your career’ section in this textbook.

*Strategic Compensation: A Human Resource Management Approach* provides the foundation for building compensation systems in a variety of work organizations. The content of this textbook establishes the structure and design elements of compensation systems in a *forward-looking framework* that addresses decision making that supports companies’ strategic plans. This approach, therefore, positions compensation practice as essential and compensation professionals as business partners. Individuals who pursue careers outside the compensation field will understand how to interact with compensation professionals for promoting effective recruitment, motivation, and retention of talent. This textbook is *readable* with a conversational tone and clear explanations for concepts and practices. It conveys the *relevance* of compensation system design overall as well as individual topics for organizations and aspiring professionals; and, this textbook takes on *contemporary topic coverage* in every chapter.

I approach the study of compensation in a realistic, practical, interesting, and stimulating manner. I focus on showing how compensation is practiced in the real world. Throughout the book, you will see examples of how organizations practice compensation management. In explaining a concept, I often quote compensation professionals and other business professionals, yet all compensation discussion is based on sound theoretical concepts and practice. Where appropriate, the strategic role of compensation is apparent, particularly in Chapter 1. In addition, I show how compensation practices are related to other Human Resource Management (HRM) topics. For instance, a firm that emphasizes recruiting top-quality candidates but neglects to provide satisfactory compensation is wasting time, effort, and money. If a firm’s compensation system pays below-market wages, the firm will always be hiring and training new employees only to see the best leave for a competitor’s higher wages. Besides this one example, the interrelationship of compensation practices set in a dynamic business environment will become more obvious as these topics are addressed throughout the book. These interrelationships are also shown to be important as organizations operate within the global environment. I included several features that appear in the textbook and MyLab (some of which are listed and discussed below) to actively engage students in the learning experience.

To improve student results, I recommend pairing the text content with MyLab Management, which is the teaching and learning platform that empowers you to reach every student. By combining trusted author content with digital tools and a flexible platform, MyLab personalizes the learning experience and will help your students learn and retain key course concepts while developing skills that future employers are seeking in their candidates. From Videos to Personal Inventory Assessments, MyLab Management helps you teach your course, your way. Learn more at [www.pearson.com/mylab/management](http://www.pearson.com/mylab/management).

Homework: Chapter 6:  
Warm Up Show completed problem Save

Score: 0 of 1 pt 1 of 10 (0 complete) HW Score: 0%, 0 of 10 pts

Warm-up 6.1.1 Question Help

Which two processes are used by compensation specialists to create internally consistent job structures?

A. Job description followed by job analysis  
 B. Job duties followed job orientation  
 C. Job design followed by job evaluation  
 D. Job analysis followed by job training  
 E. Job analysis followed by job evaluation

Click to select your answer and then click Check Answer. ?

All parts showing Clear All Check Answer

### Chapter Warm-Ups

*Chapter Warm-Up* assessment helps you hold your students accountable for learning key concepts in each chapter. These questions can be assigned to the students ahead of time and will ensure that they are coming to class prepared.



### Crunch the Numbers Exercises

*Crunch the Numbers* provide an excellent opportunity to sharpen problem solving skills through the analysis of numerical data, creating the foundation for quantifying compensation concepts and practices. There are two data-driven exercises per chapter, one in the book and both in MyLab Management. Answers are found in the Instructors Manual and in MyLab Management.

Homework: Chapter 4: Crunch the Numbers: 1 Show completed problem Save

Score: 0 of 1 pt 1 of 1 (0 complete) HW Score: 0%, 0 of 1 pt

CTN 4.1 Question Help

Piecework standard: 13 stitched garments per hour

Hourly base pay rate awarded to employees when the standard is not met: \$6 per hour. That is, workers receive \$6 per hour worked regardless of whether they meet the piecework standard of 13 stitched garments per hour.

Piecework incentive award: \$0.9 per garment stitched per hour above the piecework standard.

Over the course of a six-hour shift, the worker's productivity varies as follows:

First hour	14 garments above the hourly standard
Second hour	2 garments above the hourly standard
Third hour	18 garments above the hourly standard
Fourth hour	7 garments above the hourly standard
Fifth hour	9 garments above the hourly standard
Sixth hour	0 garments above the hourly standard

Enter your answer in the answer box and then click Check Answer.

2 parts remaining

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**Crunch the Numbers!**

**Calculating Profit Sharing Pay Awards**

*An additional Crunch the Numbers! exercise can be found on [www.pearson.com/mylabmanagement](http://www.pearson.com/mylabmanagement)*

In your new role as compensation analyst, you have been asked to estimate the dollar amount of the profit sharing pool based on three approaches as well as the allocation of profit sharing awards to eligible employees. The company's profits equal \$35 million. You are considering the following three formulas for determining the total profit sharing pool.

- **First-Dollar of Profits:** The company agrees to share two percent of all profits up to \$12 million.
- **Graduated First-Dollar-of-Profit:** The company agrees to share three percent of all profits up to \$15 million, and five percent of all profits up to \$40 million.
- **Profitability Threshold Formula:** The company will share three percent of the profits above \$10 million up to \$17 million.

There are 250 employees whose total annual base pay equals \$2,100,000.

**Questions:**

4-11. Calculate the total profit sharing pool for the following scenarios: (a) first-dollar of profits, (b) graduated first-dollar-of-profit, and (c) profitability threshold formula.

4-12. Calculate the average profit sharing award per employee based on the equal payments formula.

4-13. Calculate the profit sharing awards based on the proportional payments based on annual base pay formula for (a) Jim, whose annual base pay equals \$55,000, (b) Margaret, whose annual base pay is \$125,000, and (c) Ella, whose annual base pay is \$210,000. (Note: Profit sharing awards equal 10 percent of annual salary.)

Quiz: Chapter 4 Quiz Show completed problem Submit Quiz

This Question: 1 pt 2 of 25 (0 complete) This Quiz: 25 pts possible

Incentive or variable pay is defined as compensation, other than \_\_\_\_\_ that fluctuate(s) according to employees' attainment of some standard, such as a pre-established formula, individual or group goals, or company earnings.

A. performance-based pay

B. group-based pay

C. bonus pay

D. merit pay

E. base wages or salaries

Click to select your answer.

### Chapter Quizzes

A powerful tool used to assess your students understanding of the chapter learning objective after studying the chapter. After reading the chapter, these questions can be assigned to the students to test the knowledge they gained for respective topic(s).

### Videos Exercises

*Video exercises* are available for select chapter topics to help engage students and hold them accountable for their learning. A video clip can be assigned to students for outside classroom viewing or it can be watched in the classroom. The video corresponds to the chapter material and is accompanied by multiple choice questions that reinforce student's comprehension of the chapter content.



Homework: Watch It: Video - Fast Food Workers Walk Out, Demanding Higher Pay (2:23 mins) Show completed problem Save

Score: 0 of 1 pt 1 of 5 (0 complete) HW Score: 0%, 0 of 5 pts

Video 2.1 Question Help

Chapter 2 Video: Fast Food Workers Walk Out, Demanding Higher Pay, 2:23 mins

Fast food restaurants tend to pay less than entry-level positions in other industries. One reason for this interindustry wage differential is \_\_\_\_\_.

A. because fast food restaurant owners are greedy

B. because fast food workers are highly skilled

C. the product market in the fast food restaurant industry

D. the capital intensity of the fast food restaurant industry

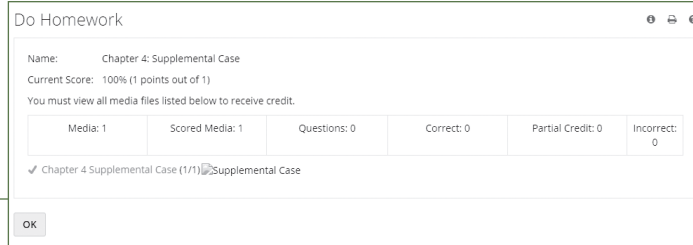
E. the fact that fast food workers aren't concerned about their pay

Click to select your answer and then click Check Answer.

All parts showing Clear All Check Answer

## Cases

Additional Supplemental cases are available in the MyLab to complement cases in the book. These cases help to keep students actively engaged and improve skills like problem solving and decision making.



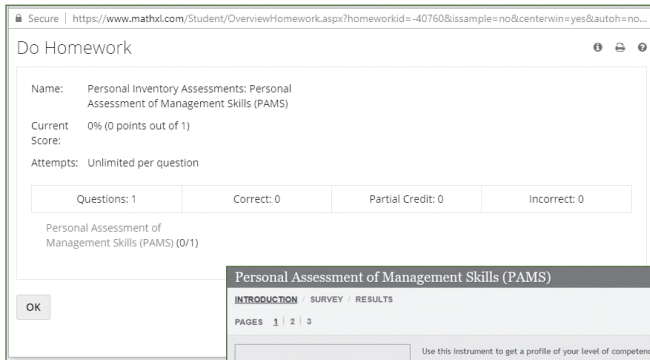
### Cases

★ An additional Supplemental Case can be found on MyLab Management.

#### Case 1: The Dreaded Performance Appraisal

“There—at last, it’s finished,” thought Rajiv Chaudhry, as he laid aside the last of 12 PA forms. It had been a busy week for Rajiv, who supervises a road maintenance crew for the Georgia Department of Highways.

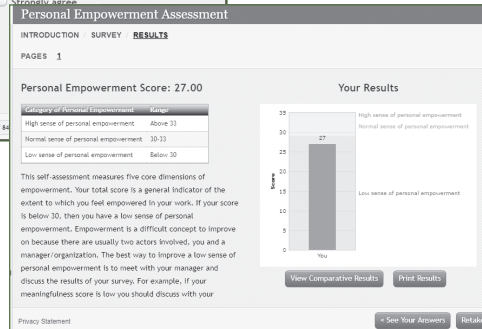
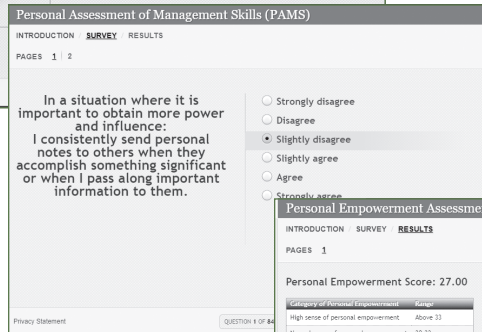
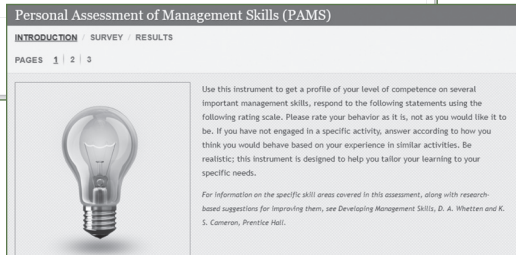
In passing through Rajiv’s district a few days previously, the governor had complained to the area superintendent that repairs were needed on several of the highways. Because of this, the superintendent assigned Rajiv’s crew an unusually heavy workload. In addition, Rajiv received a call from the HR office that week reminding him that the PAs were late. Rajiv explained his predicament, but the HR specialist insisted that the forms be completed right away.



## Personal Inventory Assessments (PIA)

PIA is a collection of online exercises designed to promote self-reflection and engagement for students. It enhances their ability to connect with concepts taught in principles of management, organizational behavior, and human resource management classes. Students learn better when they connect what they are learning to their personal experiences.

Instructors can assign and track students’ completion of the assessments. Student results include a written explanation along with a graphic display that shows how their results compare with the class as a whole. Instructors also have access to this graphic representation of results to promote classroom discussion.



## Compensation in Action

*Compensation in Action* explains how compensation professionals and managers throughout an organization work together to address important workplace issues. This feature highlights some of the specific connections between managers and compensation professionals, and the reality that compensation activities are never performed in isolation.

### PREPARING FOR MY CAREER

#### Compensation in Action

Employee compensation will ultimately be a managerial decision. As a line manager, your focus will be on the broader issues of production, revenue, and competition; however, the rate at which employees are paid—and why—will be an important factor in sustaining high levels of production, revenue, and competitive advantage. In making these decisions, line managers and HR (and in many cases the compensation specialist within the HR department) must work together in order to reward employees on measurable accomplishments and effectively communicate how the measured performance led to the resulting compensation decision.


## Working Together Exercises

As noted earlier, *Working Together* offers opportunities for students to collaborate through sharing ideas, listening to others' ideas, and coming up with a cohesive team response to the assignment. If assigned by the instructor, students may make brief oral presentations of their ideas to the class, creating an additional opportunity for working together.

## Building Strategic Compensation Systems Project


*Building Strategic Compensation Systems Project* is an experiential case, available online in MyLab Management. It allows students to work in small compensation consulting teams charged with the responsibility for developing a compensation plan for a company named *e-sonic*. The project is divided into four sections. The first section, *Strategic Analysis*, is described fully in the casebook for faculty and students who choose to complete this optional analysis of the business environment prior to the remaining three sections that directly address compensation system design, as it relates to Chapter 1 of the textbook. Section two relates to Chapter 6 of the book and introduces students to the specification of internally consistent job structures. Section three relates to Chapter 7 of this book and shifts students' focus outside of their firm to understand its relationship with the external marketplace. Finally, in Section four, students will recognize the contributions of employees through the creation of a merit-pay system and put their plan into action by paying employees within their firm. This section relates to Chapters 2 through 5, 8 through 9 in the book.

Building Strategic Compensation Project
Manage View



**Building Strategic Compensation Project**  
Barcelona • Martocchio

*This project teaches the fundamentals of compensation system design through a semester long exercise.*



**Comp Analysis Software**

*The CompAnalysis software was developed by Howard Weiss at Temple University to work in association with the Building Strategic Compensation Systems Project that*

## DEVELOPING EMPLOYABILITY SKILLS

For students to succeed in a rapidly changing job market, they should be aware of their career options and how to go about developing a variety of skills. In this book and MyLab, students will have the opportunity to develop and practice seven important skills based on various learning features that are summarized in the matrix (given on the following page) and subsequently illustrating some of the connections between the employability skills and learning features:

	Communication	Critical Thinking	Collaboration	Knowledge Application and Analysis	Business Ethics and Social Responsibility	Information Technology and Computing Skills	Data Literacy
<b>FYI</b>				✓			✓
<b>Watch It!</b>		✓		✓			
<b>Personal Inventory Assessment</b>			✓	✓			
<b>Compensation in Action</b>	✓		✓	✓			
<b>Case (end-of-chapter)</b>		✓		✓	✓		
<b>Ethics Dilemma</b>		✓		✓	✓		
<b>Crunch the Numbers!</b>		✓		✓		✓	✓
<b>Working Together: Team Exercise</b>	✓		✓	✓			
<i>Building Strategic Compensation Systems (accompanying case)</i>	✓	✓	✓	✓		✓	✓

## INSTRUCTOR TEACHING RESOURCES

*Strategic Compensation* comes with the following teaching resources.

Supplements available to instructors at <a href="http://www.pearsonhighered.com/irc">www.pearsonhighered.com/irc</a>	Features of the Supplement
<b>Instructor’s Manual</b> authored by Lori Long	<ul style="list-style-type: none"> <li>• Chapter-by-chapter summaries</li> <li>• Examples and activities not in the main book</li> <li>• Teaching outlines</li> <li>• Solutions to all questions and problems in the book</li> </ul>
<b>Test Bank</b> authored by Angela Boston	<p>More than 650 multiple-choice, true/false, short-answer, and graphing questions with these annotations:</p> <ul style="list-style-type: none"> <li>• Difficulty level (1 for easy, 2 for moderate, 3 for difficult)</li> <li>• Type (Multiple-choice, true/false, short-answer, essay)</li> <li>• Topic (The term or concept the question supports)</li> <li>• Learning objective</li> <li>• AACSB learning standard (Written and Oral Communication, Ethical Understanding and Reasoning; Analytical Thinking; Information Technology; Diverse and Multicultural Work; Reflective Thinking; Application of Knowledge; Interpersonal Relations and Teamwork)</li> </ul>
<b>Computerized TestGen©</b>	<p>TestGen allows instructors to:</p> <ul style="list-style-type: none"> <li>• Customize, save, and generate classroom tests</li> <li>• Edit, add, or delete questions from the Test Item Files</li> <li>• Analyze test results</li> <li>• Organize a database of tests and student results.</li> </ul>
<b>PowerPoints</b> authored by Patricia Buhler	<p>Slides include many of the figures and tables in the textbook</p> <p>PowerPoints meet accessibility standards for students with disabilities. Features include, but are not limited to:</p> <ul style="list-style-type: none"> <li>• Keyboard and Screen Reader access</li> <li>• Alternative text for images</li> <li>• High color contrast between background and foreground colors</li> </ul>

## ACKNOWLEDGMENTS

I thank the multitude of course instructors and students who have used past editions of my book. Their invaluable insights and constructive feedback has helped me to improve both the instructor's teaching and students' learning experiences.

At Pearson, I wish to thank my editor, Neeraj Bhalla for championing this edition and providing support throughout the revision process. Many others at Pearson provided expert advice and project management oversight, including my content producers, Shweta Jain and Sugandh Juneja. At SPi Global, I thank Bhanuprakash Sherla and his colleagues for their expert oversight of the process and keen eye for details.

## ABOUT THE AUTHOR



### Joseph J. Martocchio

My interest in the human resource management field began while I was a junior at Babson College and in compensation, particularly, while I was a first-year graduate student at Michigan State University. I found myself wanting to practice in the field as well as to become a university professor and researcher. I pursued both professional desires starting with employment at Cameron and Colby (a reinsurance company) in Boston and General Electric's Aerospace business group in Valley Forge, Pennsylvania.

I advanced my education in the human resource management (HRM) field by earning a master's degree and Ph.D. degree at Michigan State University. My master's degree enabled me to build an even stronger foundation in practice and my doctoral degree provided me with the skills to conduct scholarly research and teach college-level courses. Since earning my graduate degrees, I have been a professor in the School of Labor and Employment Relations at the University of Illinois, Urbana–Champaign and assumed administrative roles as a Provost Fellow, Associate Dean for Academic Affairs, and Interim Dean. All the while, I have taught a variety of courses in the HRM field. These include compensation systems, employee benefits, employment systems (HRM and labor relations), HR planning and staffing, and statistics. I also teach the compensation and statistics courses online. For many years, I served as the faculty advisor to the student chapter of the Society for Human Resource Management at the University of Illinois during which time students earned Merit Awards and Superior Merit awards on multiple occasions.

As a researcher, I have studied a variety of topics that include employee absenteeism, employee training and development, compensation systems, employee benefits, and generational diversity. My work appears in leading scholarly journals such as *Academy of Management Journal*, *Academy of Management Review*, *Journal of Applied Psychology*, *Journal of Management*, and *Personnel Psychology*. I received the Ernest J. McCormick Award for Distinguished Early Career Contributions from the Society for Industrial and Organizational Psychology (SIOP), and I was subsequently elected as a Fellow in both the American Psychological Association and SIOP. Following the attainment of this recognition, I served as the Chair of the HR Division of the Academy of Management as well as in various other leadership roles within that organization.

In 2018, a study in the *Academy of Management Learning and Education* revealed that I am in the top one percent of the most influential HRM authors out of a total of 9,744. Besides writing scholarly articles and *Strategic Compensation: A Human Resource Management Approach*, I have two additional sole-authored textbooks: *Human Resource Management* (Pearson Higher Education), 15th edition, and *Employee Benefits: A Primer for Human Resource Professionals* (McGraw-Hill), 6th edition.

