

## Setting Up a Pay System

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Pay administration is a management tool that enables you to control personnel cost, increase employee morale, and reduce work force turnover. A formal pay system provides a means of rewarding individuals for their contributions to the success of your firm, while making sure that your organization receives a fair return on its investment in employee pay.

This publication provides time-tested concepts for determining competitive pay levels and for maintaining fair pay relationships among the jobs comprising a small company.

### Who Needs a Pay Administration Plan?

Pay administration may just be a fancy term for something you are already doing but haven't bothered to name. Or, perhaps your organization has not been paying employees according to any system, but waiting until unrest shows up to make pay adjustments - using payroll dollars to put out fires so to speak.

A formal pay plan, one that lets employees know where they stand and where they can go as far as take home dollars are concerned, won't solve all your employee relation problems. It will, however, remove one of those areas of doubt and rumour that may keep your work force anxious and unhappy - and less loyal and more mobile than you'd like them to be. What's in it for you? Let's face it, in business - particularly small business - it's good people who can make the difference between go and no go. Many people like a mystery, but not when it's about how their pay is set. Employees under a pay plan they know and understand can see that it's equitable (fair) and equable (uniform) - that pay isn't set by whim. They know what to expect and what they can hope to shoot for. In the long run, such a plan can help you:

- recruit employees;
- keep employees;
- motivate employees;
- it can help build a solid foundation for a successful business.

### Developing and Installing the Plan

A formal pay plan doesn't have to cost you a lot of time and money. Formal doesn't mean complex. In fact, the more elaborate the plan is, the more difficult it is to put into practice, communicate, and carry out.

The foremost concern in setting up a formal pay administration plan is to get the acceptance, understanding, and support of your management and supervisory employees. A well-defined, thoroughly-discussed, and properly-understood plan is a prerequisite for success.

The steps in setting up a pay plan are:

- define the jobs;
- evaluate the jobs;
- price the jobs;
- install the plan;
- communicate the plan to employees;
- appraise employee performance under the plan;
- encourage employee feedback with respect to the plan.

## **Defining the Jobs**

Unless you know each job's specifications and requirements, you can't compare them for pay purposes. It's no surprise, therefore, that the initial step in installing a formal plan is preparing a job description for each position.

You may be able to write these descriptions yourself, since in many small businesses the owner-manager at one time or another has worked at just about every job. However, the best and easiest way to put together such job information is simply to ask employees to describe their jobs. Supervisors should be asked to review these descriptions.

Your best bet here is to prepare a simple form to be filled out by the employee (or someone interviewing the employee). This is the time to begin explaining to employees what you are doing. They need to know that their help is needed to develop the pay plan - that you are not trying to find out how well they are doing their jobs - just what they do. The form should contain the following categories:

- job title;
- reporting relationship;
- specifications;
- primary function (What is the main responsibility of the job?).

Main duties - (List main duties in order of importance and estimate the percentage of time spent on each.)

Other duties - (List of duties not performed on a regular basis.)

Job requirements

- experience or background required;
- technical/administrative complexity;
- responsibility for dollar results;
- responsibility for supervision;
- unusual working conditions.

It will probably take some time to prepare job descriptions from the information you get from your employees, but what you learn may have other uses besides comparing jobs for pay purposes. For one thing, you may discover that some employees are not doing what you thought

they were, or what they were hired to do. You may find you want to make some changes in their work routines. The information may also be useful for:

- hiring, training and developing employees;
- realigning duties in the organization;
- comparing job data for salary surveys;
- assuring compliance with various employment practice and pay rate laws;
- evaluating job performance based on assigned duties.

## **Evaluating the Jobs**

Nobody knows a scientific, precise way of deciding exactly how much a particular job is worth to a company. Human judgment is the only way to put a dollar value on work. A good job evaluation method for firms with 100 or fewer employees is simple-ranking. It's a guess, too, but a pretty well controlled guess.

Under the simple-ranking system, job descriptions are compared against each other. They are ranked according to difficulty and responsibility. Using your judgment, you end up with an array of jobs that show the relative value of each position to the company.

After you have ranked the job descriptions by value to the firm, the next step is to group jobs that are similar in scope and responsibility into the same pay grade. Then you arrange these groups in a series of pay levels from the highest to lowest. The number of pay levels depends on the total number of jobs and types of work in your organization, but for a company with 100 or fewer jobs, 10 or 12 pay levels is usually about right.

## **Pricing the Jobs**

So far in establishing a pay system, you've had to look only inside the company itself. To put a dollar value on each of your pay levels, you should look outside at the going rates for similar work in your area. Since you have ranked and grouped jobs in pay levels, you won't have to survey each job. Survey those in each level that are easiest to describe and are most common in local industry. Do try, however, to survey those jobs that have more than one level, for example, junior and senior typists.

A survey of who's paying how much for what in your locality is the best way of finding out how much you ought to pay for each of your jobs. You probably have neither the time nor the money to spend on making such a survey yourself. That shouldn't be a problem; you should be able to get all the data you need from sources such as your local chamber of commerce, major firms located in your area, or from such national sources as Human Resources and Social Development Canada. If you belong to a trade association, you may be able to get its help to find out what the going rate is for one or more jobs in each pay level.

In studying pay in your area and applying what you learn to your own jobs, make sure you compare job descriptions, not just job titles. Job titles can be misleading; there can be great differences between what one organization and another call their jobs. One firm's janitor may be somebody else's environmental control engineer. After you are satisfied that you are comparing apples and apples, you can compute an average rate (the averages in the publications are purely arbitrary) for each job and enter it on a worksheet as follows:

<b>Pay Level</b>	<b>Position</b>	<b>Average Rate</b>
1	Clerk-Typist	\$574
2	Stenographer	\$635
3	Payroll Clerk	\$687
4	Secretary	\$723
5	Accounting Clerk	\$741
6	Computer Operator	\$815
		(and so on)

You may need to adjust the average rates somewhat to keep a sufficient difference between pay levels to separate them. The going rates you find for each pay level can then become the midpoints of your pay level ranges. (You can, of course, set your company's ability to pay, the length of your work week, and the type and value of your company's benefit programs.)

Typically, the minimum rate in a level is 85 percent of the midpoint rate, and the maximum rate is 115 percent of the midpoint. With the arrangement, a new employee can increase his or her earnings by 35 percent without a job change, thus having performance incentives even if he or she is not promoted.

You now have a pay range for each position in your organization. It will resemble the following example:

<b>Pay Range</b>	<b>Minimum</b>	<b>Midpoint</b>	<b>Maximum</b>
1	\$490	\$575	\$660
2	\$530	\$625	\$720
3	\$580	\$685	\$785
4	\$615	\$725	\$835
5	\$690	\$815	\$935
			(and so on)

Such a pay range will enable you to tell where your employees' pay and pay potential stand in relation to the market rates for their kinds of work. It should show you at a glance where you need to make changes to achieve rates that are fair within your organization and pay that's competitive with similar businesses in your community.

In general, with a planned pay structure you should be able to tie individual rates of pay to job performance and contribution to company goals. It should also provide enough flexibility to handle special situations.

### **Installing the Plan**

At this point you have the general plan, but you don't, of course, pay in general. You must pay each employee individually. You must now consider how the plan will be administered to provide for individual pay increases.

In administering the pay increase feature of the plan, you can use several approaches:

- merit increases, granted to recognize performance and contribution;
- promotion increases for employees assigned to different jobs in higher pay levels;

- progression to minimum for employees who are below the minimum or hiring rate for the pay level;
- probationary increases of newer employees who have attained the necessary skills and experience to function effectively;
- tenure increases for time with the company;
- general increases, granted employees to maintain real earnings as economic factors require and to keep pay competitive.

These approaches are the most common, but there are many variations. Most annual increases are made for cost of living, tenure, or employment market reasons. Obviously, you might use several, all, or combinations of the various increase methods.

You may find that a form for documenting salary increases and recording the reasons for them can be quite useful. You will probably find that records such as these are useful references for pay administration purposes.

### **Telling Employees about the Plan**

After you have set your pay administration plan into place, you have to consider how to tell employees about it. If setting up a good program is number one in importance, a close number two is explaining that plan to employees.

How to tell them is your decision. Some of the more successful methods include personal letters to each employee and meetings to explain the plan and answer questions.

However you tell employees, you must clearly, honestly, and openly explain the way the plan works. This is a prime opportunity for you to build goodwill and good relations with your employees. Be sure your supervisors understand and can explain the plan to their people. Explaining the plan to new employees is also essential, and it's a good idea to review the plan periodically with all employees.

### **Employee Performance Appraisal**

- The majority of employees in the Canadian labour force are under merit increase pay system, though most of their pay increases result from other factors. This approach involves periodic review and appraisal of how well employees perform their assigned duties. An effective employee appraisal plan:
  - achieves better two-way communications between the manager and the employee;
  - relates pay to work performance and results;
  - provides a standardized approach to evaluating performance;
  - helps employees see how they can improve by helping them understand job responsibilities and expectations;
  - sets targets for employees to aim towards.

Such a performance review helps not only the employee whose work is being appraised, but also helps the manager doing the appraising to gain insight into the organization. An open exchange between employee and manager can show the manager where improvements in equipment, procedures, or other factors might improve employee performance. Try to foster a climate in which employees can discuss progress and problems informally at any time throughout the year.

Again, to get the best results it's a good idea to use a form for appraisal. A typical form includes such job performance factors as:

- results achieved;
- quality of performance;
- volume of work;
- effectiveness in working with others in firm;
- effectiveness in dealing with customers, suppliers, etc;
- initiative;
- job knowledge;
- dependability.

You can design your own form, using examples you can find in books on personnel administration, if necessary. Your forms should be tailored to the jobs and should follow from your job analyses.

### **How Can the Plan Help You?**

The best pay plan in the world for employees won't be of any use if it doesn't help your business. What's in it for you?

Again, the answer is getting, keeping and encouraging good employees. Your pay plan will help you:

- Recruit - The pay ranges will provide competitive hiring rates for attracting high calibre employees.
- Retain - The performance appraisal plan and pay increase feature will encourage performance plus growth and development within your organization.
- Motivate - The pay plan will provide something to shoot for to keep employees interested in and enthusiastic about their present assignments and also provide the incentive to seek greater opportunity within your company.

Having capable employees who are interested and enthusiastic will help you win the battle for business survival and growth.

### **Updating the Plan**

To keep your pay administration plan in tune with the times, you should review it at least annually. Make adjustments where necessary and don't forget to retrain supervisory personnel. This isn't the kind of plan that can be set up and then forgotten.

During your annual review, ask yourself if the plan is working for you. That's the most important question. Are you getting the kind of employees you want or are you just making do? What's the turnover rate? Do employees seem to care about the business? In the last analysis, it's not how elegant the plan is or how beautiful the forms and administration. What matters is how the plan helps you to achieve the objectives of your business.

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