

## Pay Compression

The number two problem in public sector compensation programs is the problem of pay compression. (I will let you know what we think the number one problem is at the end of the newsletter)

Pay compression goes by many definitions and these are some of them:

1. When a subordinate is paid, with or without overtime, more than his or her supervisor who does not get overtime.
2. When an employee in a lower graded job is paid more than an employee in a higher graded job is paid.
3. When a new employee is paid more than a longer term employee and they are in the same pay grade.
4. When a job that is less complex, difficult, or requires less effort, is paid more than a job that is more complex, difficult or requires more effort.
5. When employees in a new unit receive big increases and they aren't doing any different work than before the move.

There are probably other situations that can be called pay compression. We are going to try and describe what you can do in each of these situations.

First, however, recognize that regardless of how hard you try, as long as you have employees entering, leaving or moving in the system, you will have some degree

of pay compression. You should try to minimize it as much as possible, because once it gets out of control or its causes become institutionalized, the cost to get out of the problem will be large, the pain will be deep and the solution elusive.

### Here we go:

1. When a subordinate is paid, with overtime, more than his or her supervisor who does not get overtime.

The solution to this is easy, but employees probably won't buy it. One solution is to pay supervisors overtime at a straight time rate. This usually resolves the issues, although it can be expensive, especially if you cannot control the overtime hours that are worked. The second solution, is to make sure that you just count base wages. If the base wage of the higher level job is greater than the subordinate job, then you really don't have pay compression. Make sure that you measure this at the midpoint of the pay grade rather than at what employees are actually paid. The supervisor will eventually be paid more than all their subordinates at the base wage level even though a new supervisor may be paid less than a more senior subordinate.

2. When an employee in a lower graded job is paid more than an employee in a higher graded job is paid.

This is not too much different than the second part of the above issue. You want to make sure that the pay range opportunity (i.e., maximum of the

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pay range) is higher in the higher graded job than in the lower graded job. You may have employees that are paid less than long term lower graded employees, and that is to be expected in most pay systems because of range overlap, but you should make sure that your system of grades and ranges, or your pay movement procedures does not encourage this to happen. In addition, you want to make sure that range overlap does not exceed about 30%.

3. When a new employee is paid more than a longer term employee and they are in the same pay grade.

Now this is a problem. It may get worse in the near future as hiring picks up. It is normal to bring a new person in at a higher rate of pay than they were making in their previous job. Unless the move is a promotion, the new employee is going to want an increase just to make the move. That means that they may make more money than an existing employee. Existing employees get agitated when they find out that they have to train the new employee and they are making less money than the newbie.

Although most HR departments try to avoid this, unless you have a competitive pay structure and a hiring policy that limits the starting pay of new hires, you will likely have this problem to some extent. Existing employees still don't like it. But unless the problem is a total reversal of pay, this is a problem that may be managed by some pay adjustments and some education of current employees. Everyone has some of this type of compression.

4. When a job that is less complex, difficult, or requires less effort, is paid more than a job that is more complex, difficult or requires more effort.

This type of compression can be a serious issue, if it is true. Although employees will make this case quite frequently, if the facts bear out that lower complexity jobs are paid more than higher complexity jobs, and it is not a result of tenure in the job, then the problem is one where you need to

take some action. The serious potential danger you may have is if the pay is separated by racial or gender lines. But assuming it is not, and it is not a problem of seniority, then what you need to do is make sure that the basis of the assignment of job to pay grades is based on a defensible job evaluation system, good market data or a combination of the two. In short, your pay and classification system needs an overhaul.

5. When employees in a new unit receive big increases and they aren't doing any different work than before the move.

Ahh. Here is the tough one. We have heard this problem with general government jobs versus enterprise fund jobs, as well as new departments and functions. In order to get the "right" people, the argument is that they have to pay higher wages. They will also argue that they have higher expectations and/or there will be new procedures that people have to learn, and on and on and on. Most of it is spurious and should be dealt with by senior management. There may be issues of pay discrimination, as well as a clear definition of who the employer is. The ultimate outcome is either higher pay for everyone, or a slow exodus from the lower paid jobs to the higher paid jobs. Either way, the effect on government is a higher total payroll cost, either through higher pay or higher cost of recruiting and training.

And the number one pay problem in government? In our opinion, it is pay that is lower than the competitive market levels. Over time, this leads to the obvious problems of turnover, quality of work, morale issues and bureaucratic resistance to change. Eventually, this problem gets corrected because the market is a very powerful regulator of pay.