

# How to Establish Salary Ranges

Please note that all forms and policies should be reviewed by your legal counsel for compliance with applicable law, and should be modified to suit your organization's culture, industry, and practices.

Salary ranges help employers control their pay expenses and ensure pay equity among employees. It is critical that employers have rational explanations for why they pay their employees a certain rate, and defined salary ranges help accomplish that.

The purpose of this guide is to provide a basic set of steps for creating compensation grades and salary ranges. It is intended for general use and should be tailored to meet an organization's specific needs and goals. Employers and HR professionals without experience and knowledge of compensation design principles should consult with an expert for help as developing a compensation structure is a critical element within every organization.

## Step 1: Determine the Organization's Compensation Philosophy

Before creating salary ranges, the organization must first determine what its approach or philosophy is to compensation. What is the mindset that drives pay decisions? Determining the compensation philosophy requires an in-depth look at the company's beliefs regarding compensation. The key is to create a philosophy and be consistent in its application regarding pay practices.

An employer can choose to [lead, lag or match](#) the market when compensating employees. Being a market leader means that the organization pays more for jobs than its competitors. Typically, an organization does this to gain an advantage or attract talent away from its competitors. If an employer decides to match the market, it pays roughly the same as its competitors, and if an employer lags the market, it is paying less than market rates. Generally, an employer rarely chooses to lag the market as a conscious pay strategy. It is often either discovered after market research reveals the practice, or it may be the result of a limited compensation budget. In rare circumstances an employer's brand may be so attractive (e.g., Disney, Google) that the employer can pay lower-than-market wages without a negative impact on recruitment and retention.

A company's attitude toward compensation will drive its decisions through the rest of this process. Therefore, it is critical to know the employer's pay philosophy and have executive buy-in from the outset.

## Step 2: Conduct a Job Analysis

A job analysis is a process for gathering, documenting and analyzing information about a job to determine the activities and responsibilities it includes, its relative importance to other jobs, the qualifications necessary for performing the job and the conditions under which the work is

performed. This can be done by observing employees, conducting surveys or interviewing employees doing the job, or using a combination of these methods. The end result of a job analysis is a clearly defined job description. See [Performing Job Analysis](#)

### Step 3: Group into Job Families

Once an employer has developed current and accurate job descriptions, it should determine whether to group the jobs into separate job families or have one pay grade system for all positions throughout the organization. For example, an organization may have an administrative job family, technical job family, management job family and executive job family. It may have different job families based on geographic locations (different countries or regions) or different divisions.

### Step 4: Rank Positions Using a Job Evaluation Method

A job evaluation is the process of rank-ordering jobs—not the people in them—based on job content to demonstrate the relative worth and level of responsibility of all jobs to one another. There are several job evaluation methods; the two most common methods are explained below.

#### *Point method*

The content of jobs can be described in terms of factors. Factors are qualities of a job that are common to many kinds of jobs, such as skill, effort or working conditions. Each factor is assigned a weight, or points, according to how much of that particular factor is present in the job. Simply stated, the more points assigned to a job, the more worth the job has to the organization. Jobs with more worth are compensated more than jobs with lesser worth. There may be a group of factors to apply to all jobs or different factors for distinct functions or a combination of companywide and function-specific factors. One example is the Hay point method system, which uses only three factors and measures the degree that these three factors are required for each position. The Hay system factors are know-how, problem-solving ability and accountability.

Point Method Example:

Job Title:	Machine Operator I	Machine Operator II	Machine Operator III
<b>Factors</b>	<b>Points</b>	<b>Points</b>	<b>Points</b>
Skill (max pts 50)	10	30	50
Education (max pts 25)	5	5	10
Working conditions (max pts 10)	5	5	5
Independent judgment (max pts 15)	3	8	15
<b>Total Points (max 100)</b>	<b>23</b>	<b>48</b>	<b>80</b>

#### *Ranking method*

The ranking method is a much more simplistic approach to rank-ordering the value or worth of each job in comparison to other jobs within the same job family. Job ranking places jobs in a hierarchy of their value to the company. This method is an estimated approach rather than a formal calculation as described in the point factor method. The less-rigorous ranking method is often used in smaller organizations that have fewer jobs to compare.

### **Step 5: Conduct Market Research**

Conducting market research ensures that wages paid to employees are comparable to similar positions in the marketplace.

When conducting salary market research, employers should consider the following:

- Job titles vary between organizations. Employers should read the descriptions of the jobs surveyed to make sure that the related tasks, functions and levels of responsibility match the positions at their organizations.
- To obtain current, accurate salary information, employers will typically need to purchase salary data. A few resources, such as the U.S. Bureau of Labor Statistics (BLS), offer free data, but the data may be older and too broad in terms of industry, geography or other factors.
- Whenever possible, employers should try to obtain information from more than one market survey resource, at least for benchmark positions.
- Professional organizations sometimes offer data at a discounted price. For example, if an employer wants to hire a large group of engineers, it could check with the local engineering association to see if the association conducts salary research and offers price breaks to members.
- To avoid violating antitrust laws, employers should not contact other organizations directly for compensation information. Using information from a vendor that is in writing, that uses averaged pay rates and aggregate data received from various sources, and that does not directly identify survey participants is in the best interest of the organization.
- When collecting market data, employer-reported data are generally more reliable than employee-provided salary information. Avoid Internet searches for free salary data, which often contain compensation that has been self-reported by employees.
- Employers should realize from the outset that each organization has jobs that are unique and that it will be impossible to find exact matches for all jobs. Organizations may need to consider jobs that closely fit the principal aspects of a particular job and consider salary data for more than one type of job.

### **Step 6: Create Job Grades**

Job grades are groupings of positions with similar worth. Organizations can either use their job evaluation data to group positions into job grades or use their market data to band together positions based on similar salary survey data. This guide uses the market banding method.

An employer can have as many or as few pay grades as it wants. A startup or small organization may have only three or four pay grades. The federal government, by contrast, uses 15 pay grades based on the level of difficulty, responsibility and qualifications required. Individuals with a high school diploma and no additional experience typically qualify for GS-2 positions; those with a bachelor's degree for GS-5 positions; and those with a master's degree for GS-9 positions.

<b>Job Family</b>	<b>Job Category</b>	<b>Job Title</b>
Human Resources	Comp and Benefits	Total Rewards Manager Compensation Specialist Benefits Specialist
	Talent Acquisition	Talent Acquisition Manager Senior Recruiter
	Employee Relations	Employee Relations Manager Training Specialist Culture Specialist
	Support	Payroll Coordinator HR Systems Analyst HR Administrative Assistant

### **Step 7: Create a Salary Range Based on Research**

Employers should note the range of pay in the salary surveys and other information that may be relevant when establishing an average salary. For each pay grade, an organization will need to establish minimum, midpoint and maximum pay ranges. Often employers consider their midpoint of a salary range to be somewhere between the 25th percentile and the 75th percentile. Some employers will use the 50th percentile, the median, mean or mode if they want to meet the market. If a company's philosophy is to lead the market, the salary point will be above the 50th percentile for most positions. A simple way to establish a proposed midpoint is to average the market data between the different positions grouped in a grade. There is no hard and fast rule on creating salary ranges. In this guide, we use the midpoint as the base for developing the salary range. Other methods also are available, such as using the minimum salary as the base.

A traditional salary range is commonly 30 percent to 40 percent. It is common that top salary grades (i.e., for executives and top management) have a wider range (sometimes greater than a range of 40 percent) and that the lowest salary grades often have the narrowest range (sometimes smaller than 30 percent). Broadbanding occurs when employers decide to have very few salary grades and to make those ranges much wider.

The formulas for a 30 percent range using the midpoint as the base are:

Maximum = Midpoint x 1.15

Minimum = Midpoint x 0.85

The formulas for a 40 percent range when the midpoint is known are:

Maximum = Midpoint x 1.20

Minimum = Midpoint x 0.80

Pay grade ranges will usually overlap. The more overlap, the more cost-effective it will be for career progression; less overlap will require a larger pay increase for internal promotions. Each job family can have its own pay grades and pay ranges that are established independently from other job families.

Examples:

Proposed Ranges	Min	Mid	Max
<b>Grade I</b>	<b>\$11.48</b>	<b>\$13.50</b>	<b>\$15.53</b>
Maintenance I	(market salary = \$13.00)		
Administrative Asst.	(market salary = \$14.00)		
<b>Grade II</b>	<b>\$15.09</b>	<b>\$17.75</b>	<b>\$20.41</b>
Mechanic I	(market salary = \$17.50)		
Machinist	(market salary = \$18.00)		

### Step 8: Determine How to Deal with Salaries Not Within Range

At this stage in the process, an employer can look at what it is paying its employees in comparison to the data it has collected and the proposed salary grades and ranges for positions. The organization may need to make some adjustments, but overall the employer can rely on market data and its pay philosophy to set these ranges.

Grade I	
Maintenance I	Administrative Asst.
<b>\$11.00 (green circle rate)</b>	\$13.72
\$11.50	\$14.18
\$12.22	\$15.00
Grade II	
Mechanic I	Machinist
\$18.00	\$17.65
\$18.20	\$18.20
\$18.30	\$19.35
	\$19.60
	<b>\$20.45 (red circle rate)</b>

After the salaries for current employees have been placed into the range, several employees will inevitably not be in line with the guidelines and ranges the employer has established.

"Red circle rates" are salaries/wages that are above the maximum rate the organization has established for the position's salary range. Strategies to rectify red circle rates include the following:

- In lieu of base salary increases, offer star employees a bonus that is roughly the amount of what the pay increase would have been. This allows for recognition of an employee's outstanding performance without raising his or her base pay even more.
- Explore developmental opportunities to facilitate promotion into the next pay grade.
- Restrict further salary increases by freezing pay.
- Lower an employee's base pay to bring it in line with the range. This option will likely lower employee morale and may motivate an employee to start job hunting. For this reason, it is important to encourage valuable employees to seek developmental opportunities that could lead to promotion.

"Green circle rates" are salaries below the minimum rate the employer has established for the position's salary range. Green circle rates are equally as problematic as red circle rates in that they do not follow established guidelines. A solution is to provide pay increases up to at least the minimum in the range. An exception may be if an employee has been performing below expectations. In this case, the employer may want to consider requiring successful completion of a performance improvement plan prior to receiving a pay increase.

## **Step 9: Updating and Aging**

Compensation rarely remains static. The rate of pay is constantly changing with external market and economic activity.

Aging is the activity of increasing salary grades with the market without the cost of purchasing new salary survey data each year. One way to do this is by using the Employment Cost Index (ECI). The ECI is a component of the [National Compensation Survey](#), which is produced by the BLS. It measures changes in the cost of total compensation, which includes wages, salaries and the employer's cost of employee benefits. Another option is to use the annual [Cost of Living Adjustment](#), published each year by the Social Security Administration.

Ultimately, salary survey data should be gathered and reviewed every two to three years so that appropriate adjustments can be made to the organization's salary ranges.