EMPLOYEE COMPENSATION MANAGEMENT
(DMHR05)
(M.A. HRM)

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LESSON - 1

EMPLOYEE COMPENSATION MANAGEMENT - AN OVER VIEW

1.0 OBJECTIVE :

- After studying this lesson, the student is able to:
- Visualise the reasons for studying Employee Compensation Management
- Study the Principles of effective compensation plan
- Observe the significance of compensation
- Identify the various objectives of compensation management.

STRUCTURE:

1.1 Introduction

1.2 Meaning of Employee Compensation Management

1.3 Concept of Compensation.

1.4 Principles of effective Compensation.

1.5 Significance of Compensation.

1.6 Objectives of Compensation

1.7 Classification of Compensation System

1.8 Compensation Components

1.9 Designing Equitable Compensation System

1.10 Benefits of a Formal Compensation Program

1.11 Compensation Determinants

1.12 Summary

1.13 Keywords

1.14 Self Assessment Questions

1.15 Further Readings

1.1 INTRODUCTION:

'Compensation' refers to the establishment and implementation of wages and salaries of employees in an organisation. The organisation pays wages and salaries to the employees for the work rendered by them.

"According to Belcher' the term 'compensation' refers to all forms of payment going to employees of all levels and arising from employment. The soundness of compensation management depends on the amount of wage and salary paid to employees for a fair days work. Hence, formulation and administration of compensation is considered one of the important and complex managerial functions. Thus compensation is any form of payment given to the employees in exchange for work they perform.

The compensation function contributes to the organisational effectiveness in four basic ways :

1) Compensation can serve to attract qualified applicants to the organisation. An organisation offering a higher level pay can attract a large number of qualified persons than its competing units.

2) Compensation helps to retain competent employees in the organisation.

3) Compensation policies help by maintaining a fair internal pay structure and by providing attractive benefits.

4) Compensation serves as an incentive to motivate employees to put forth their best efforts.

Thus compensation is a reward for past service to the enterprise by the employees and stimulate to increase the employee performance in future.

Compensation function is one of the important functions of Human Resource Management. Human Resources engaged in a number of activities to facilitate compensation goals attracting, retaining and motivating employees for organisational effectiveness. The compensation function includes the human resource planning, job analysis, job evaluation, performance appraisal and employee relations.

1.2 MEANING OF EMPLOYEE COMPENSATION MANAGEMENT:

Employee compensation includes everything, an employed individual receives in return of his/her work. This concept encompasses all the employees, managers and professionals as well as rank and file, blue and white collar employees. Compensation includes wages or hourly rates of pay, salaries covering a longer period of time than wages, and incentives including extra pay. One of the most rapidly expanding areas of compensation is the fringe benefit area.

Compensation as a price involves economic considerations the allocation of scare human resources in the market and the determination of the value of employee services - but pay includes many elements in addition to economic value. Compensation, in an industrial society, often serves as a substitute for personal recognition. Furthermore, pay plays a major role in determining the workers way of life, including his social position.

1.3 CONCEPT OF COMPENSATION:

"Compensation which includes direct cash payments, indirect payments in the form of employee benefits and incentives to motivate employees to strive for higher levels of productivity is a critical component of the employment relationship. Compensation is affected by forces as diverse as labour market factors, collective bargaining, government legislations and top management's philosophy regarding pay and benefits."

— **Wayne F Cascio.**

"Compensation is what employee receives in exchange for their contribution to the organisation".

The productivity objective may be fostered through the compensation program of the organisation :

i) Helping the organisation to attract qualified employees who can be perform the assignments given to them,

ii) Motivating employees to perform it a consistently higher, at least satisfactory level, and

iii) Encouraging employees to improve their skills, abilities and knowledge so they can perform present or future jobs more effectively and efficiently.

1.4 PRINCIPLES OF EFFECTIVE COMPENSATION:

There are several principles of compensation plans, policies and procedures. The important among them are:

1) The compensation plans and policies should be sufficiently flexible.

2) Job evaluation must be done scientifically.

3) Compensation administration plans must always be consistent with overall organisational plans and programmes.

4) Compensation plans and programmes should be responsive to the changing local and national conditions.

5) Compensation management plans and programs should be conformity with the social and economic objectives of the country like attainment of equality in income distribution and controlling inflationary trends.

6) Compensation plans should simplify and expedite other administrative process.

1.4.1 Requisites of an effective compensation system:

a) Compensation plan should be an integral part of financial plan.

b) There should be an adequate data base for all compensation decisions.

c) In compensation policy formulation and implementation the management should be willing to associate workers / unions.

d) There should be proper organisation for compensation determination.

With a good compensation plan, employees are happier in their work, co-operation and loyalty are more pronounced, productive output is up, quality is better.

1.5 COMPENSATION ISSUES AND SIGNIFICANCE:

Compensation management, therefore, now plays a significant part along with the working style and environment, empowerment etc. in the organisation success strategy.

Paying employees' for their services appears at first glance to involve only a relatively straight forward economic problem. Setting a price for a factor of production, it includes psychological, sociological, legal, political and ethical as well as economic elements. Further price-setting process involves not only a market but a number of decision makers, employers, employees, unions, various levels of government and consuming public at large have their hands in decisions reached, in fact, our entire society insists upon compensation.

1.5.1 Compensation Considerations :

Compensation management is a broad and complex one. The purpose of compensation broadly stated, is to attempt to harmonise the various elements of wages. Compensation attempts to find solutions to wage problems, it must consider the interest of (i) employer, (ii) employees, (iii) unions, (iv) various publics and (v) government, and in arriving at specific wages.

There are many considerations concerning the economic, social, psychological, political and ethical at large that goes into solution of wage problems.

a) Economic elements in compensation:

Compensation as a price involves economic considerations.

Pay like a coin has two sides, one side consists of the cost to the employer, the other side income to the employee. To the employer, compensation is the price he must pay for the employment of a factor of production. In this sense, payment for employee services is an economic transaction governed by the same logic as any other purchase, in which the purchaser attempts to obtain the greatest quantity and the higher quality possible for his money.

b) Sociological aspects of compensation:

To the recipient, pay serves as a symbol of status as well as means to purchasable ends. Status of individuals is a product of many standards of judgement: family, friends, occupation, education, religious and political affiliations and so on.

c) Psychological aspects of Compensation :

Compensation provides a means for satisfying needs, needs motivate people. Therefore, to extent that pay becomes a means for satisfying needs, it may serve to motivate employees.

d) Legal aspects of Compensation :

The compensation administration follows the compensation laws. According to law, payments and benefits shall be provide to the employees, i.e. the Minimum Wages Act 1948, the Payment of Wages Act 1936, the Equal Remuneration Act 1966, the Payment of Bonus Act 1965.

e) Political aspects of compensation :

The determination of compensation involves matter of power and influence which are political consideration.

f) Ethical considerations in compensation :

Compensation is conducted with fairness, value based, ethical and systematic. Most people agree that compensation plan should be fair, and a fair days pay, the people agree that the just wages and gross inequities are common phrases.

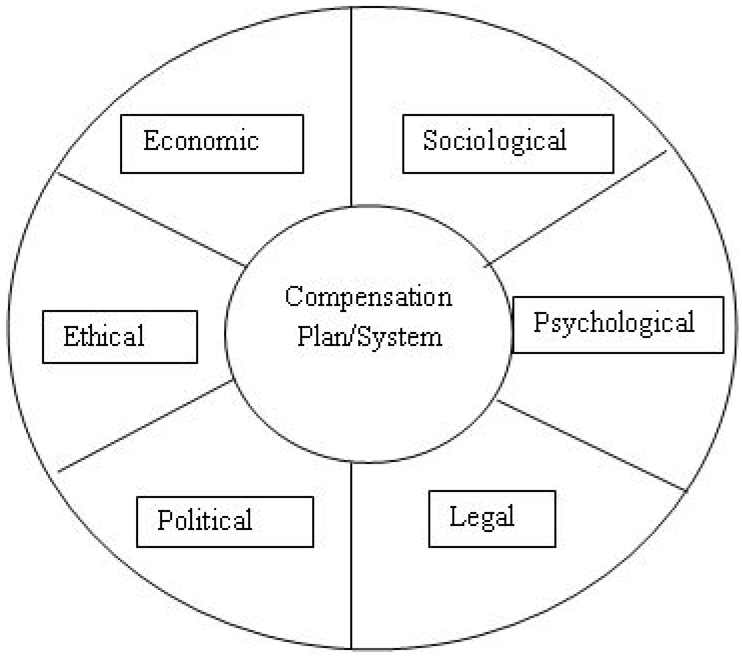


FIGURE 1.5.1 COMPENSATION ASPECTS AND SIGNIFICANCE

1.6 OBJECTIVES OF COMPENSATION MANAGEMENT :

The objectives of Compensation Management are numerous and sometimes conflict with each other. The important among them are :

1. To acquire qualified and competent personnel :

To attract qualified and competent personnel a sound compensation system is pre-requisite.

2. To retain the present employees :

Employees may quit when compensation levels are not competitive, in order to prevent such quits with the help of effective compensation plan.

3. To secure internal and external equity :

Internal equity mean payment of similar jobs within the organisation. External equity implies payment of similar wages to similar jobs in comparable organisations.

4. To ensure desired behaviour :

Good rewards reinforce desired behavior like performance, loyalty, accepting new responsibilities and change etc.

5. To keep labour and administrative costs in line with the ability of the organisation to pay.

6. To protect in public as progressive employer and to comply with the wage legislations.

7. To pay according to the content and difficulty of the job and in tune with the effort and merit of the employees.

8. To facilitate pay roll administration of budgeting and wage and salary controls.

9. To simplify collective bargaining procedure and negotiations.

10. To promote organisational feasibility.

The main object of compensation administration is to design a cost effective pay structure that will attract, motivate and retain competent employees and that will also be viewed as fair by these employees. Apart from meeting legal requirements, organisations have to take care of ever rising employee expectations and competitive pressures while designing an effective compensation plan.

1.6.1 Systems to achieve the objectives :

The above mentioned objectives are achieved by the use of the following systems.

a) Job Evaluation :

All jobs will be analysed and graded to establish the pattern of internal relationships. It is the process of determining relative worth of jobs. It includes selecting suitable job evaluation techniques, classifying jobs into various categories and determining relative value of jobs in various categories.

b) Wage and Salary ranges :

Overall salary ranges for all the jobs in an organisation is arranged. Each job grade will be assigned a salary range. These individual salary ranges will be fitted into an overall range.

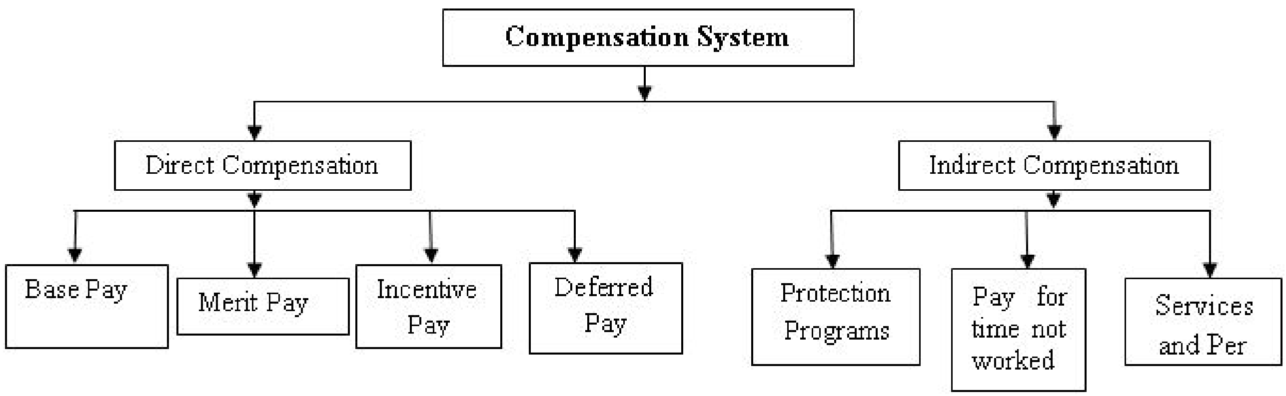
c) **Wage and Salary adjustments :**

Overall salary grades of the organisation may be adjusted abused on the data and information collected about the salary levels of similar organisations. Individual salary level may also be adjusted based on the performance of the individual employee.

1.7. CLASSIFICATION OF COMPENSATION SYSTEM :

In most organisations the compensation system involves a multifaceted package, not just pay for work and performance. The classification of compensation system can be divided into two types, i.e, direct (wages) and indirect (benefits) forms of compensation. Taken together, direct compensation and indirect compensation define total compensation (see chart 1.7.1)

Chart 1.7.1



a) Direct Compensation :

In this system the payment is getting by employee in the form of money. It includes, basic pay, wage incentives, bonus, H.R.A. CCA and other allowances, profit sharing etc.

b) Indirect Compensation :

It is necessary to consider the indirect compensation, employees receive that is not called wages. For example, employees receive rest periods, paid vacation, paid sick leaves, medical care, call-in and call-back pay, and down-time pay. Employers may contribute to insurance premiums, pensions and other benefits for employees. Then there are payments for holidays not worked, for time spent in grievance handling, night shift premiums and severance pay. The bonuses, attendance bonuses, length-of-service bonus etc.

The compensation plan is also classified into two types. a) Monetary Compensation b) Non-monetary Compensation.

The monetary compensation is an important function and plays crucial role in the organisation. It is classified into two types.

"The primary monetary compensation" is basic pay in the term wages or salaries. A sound primary compensation structure is a function of internal and external alignments. Internal alignments mean that there should be a proper relationship between the wages and salaries of various positions within the enterprise. This will depend on correct job evaluation. External alignments means that the company wage rates should be comparable with the rates of other companies. This will depend on the correct survey of wage rates prevailing in the country.

"Incentive compensation" is the device of increase workers' productivity. There are several types. All incentive plans can be classified into four categories.

a) Individual Incentive plans b) Group incentive plans

c) Factory wide incentive plansd) Payment by results.

'Non-Monetary compensation' is necessary to satisfy the social and self esteem or egoistic needs of employees.

1.8. COMPENSATION COMPONENTS :

Any organization's total compensation or reward package is comprised of three major components: direct monetary rewards, indirect monetary payments, and psychological satisfactions. In designing an effective compensation package, all three elements must be carefully considered.

1.8.1. Direct Monetary Rewards

Direct monetary rewards are the most obvious compensation component. Sometimes referred to as cash compensation, these rewards encompass all those items involving the payment of dollars to employees for work accomplished or effort expanded (e.g., a wage, a salary, a commission). Whether paid by the hour, by the month, or by another method, direct compensation is discretionary income to the employee. He or She is able to spend it in whatever way desired for the purchase of goods and services.

1.8.2. Indirect Monetary Payments

Indirect monetary payments include those items of financial value the organization provides to employees that do not result directly in employees' receiving spendable dollars. This compensation component is usually referred to as benefits. Included in this category are various forms of protection (health insurance, life insurance, disability insurance) and services (financial counseling, employer subsidized cafeterias, uniforms, free parking).

1.8.3. Psychological Satisfactions

The third compensation component consists of the psychological satisfactions-sometimes called psychic income-which a worker derives from the work he or she performs and the environment in which it is performed. This form of compensation includes opportunities to perform meaningful work, social interactions with others in the workplace, job training, advancement possibilities, recognition, and a host of similar factors.

An effective compensation system must carefully address all three compensation components: direct, indirect, and psychological. The three components are inextricably interrelated. Direct compensation influences an employee's perceptions of psychological satisfactions. Psychological rewards contribute to an employee's interpretation of direct and indirect compensation as adequate or inadequate. Feelings about indirect monetary rewards affect feelings about direct compensation and psychological satisfactions.

In other words, design of the total compensation package must consider all elements comprising the package and not simply focus on any one piece of the total system to the exclusion of the other two. An effective total compensation package must achieve proper balance between all three components.

1.9 DESIGNING EQUITABLE COMPENSATION SYSTEMS :

Employees want to be treated equally. Equity is the balance between the inputs an individual brings to a job and the outcomes he/she receives from it. Employee inputs include experience, education, special skills, efforts and time worked. Outcomes include pay, benefits, achievement, recognition and any other rewards.

It is a state-of-art practices in establishing equity, it have three elements : internal equity, external equity and individual equity.

Internal equity returns to the relationship among jobs within a single organisation. It exists when different pay for different jobs within the organisation.

External equity, refers to comparisons of similar jobs in different organisations.

The individual equity refers to comparisons among individuals in the same job within the same organisation.

1.10. BENEFITS OF A FORMAL COMPENSATION PROGRAM

Every organization has a compensation program. Whether that program is well thought out, written, and formalized, or whether it is arbitrary, unwritten, and informal, is another matter. Compensation issues are far too important and complex to be left to chance or caprice. Every organization-even those with only a handful of employees-should have a carefully formulated plan for compensating its workers fairly and accomplishing the tasks of attracting, retaining, and motivating employees.

1.10.1. Facilitate Recruitment

One of the primary benefits of a formalized compensation program is that it enables an organization to attract the right quantity and quality of employees needed to perform the work of organization. In the absence of a carefully thought-out and objective compensation program, organizations typically experience difficulty in attracting sufficient quantities of qualified workers.

Where compensation has not been formally considered and structured, it is often out of touch with what the labor market is paying; consequently, it is difficult for an organization to attract the workers it needs. An inequitable compensation program may, therefore, make constant recruiting necessary just to secure needed workers. On the other hand, keeping compensation rates in line with market rates makes attracting employees less difficult.

1.10.2. Enhance Retention

Organizations with inadequate compensation systems may succeed in recruiting sufficient employees, but may not be able to retain them for long because employees will typically leave for better paying jobs as soon as opportunities arise. Equitable pay, a sound benefits program, and a psychologically supportive organizational climate enable a firm to reduce employee turnover. In today's highly competitive environment, indirect monetary compensation plays a significant role in worker retention by creating "golden handcuffs" that tie an employee to a firm. Employees often stay with organizations because they know that other organizations cannot match the level of benefits the employees are currently receiving. Likewise, retention will be higher when the institution's rates are in accord with the labor market. Because turnover may cost an organization 1.5 to 2.5 times the annual salary of the person leaving the organization, retention of employees increases profitability.

1.10.3. Increase Motivation

Motivation, too, is difficult to accomplish in the absence of a formal compensation program. Where there is no rhyme or reason to an organization's pay system, employees tend to perceive the system as inequitable and respond accordingly as far as performance and productivity are concerned. A compensation system that rewards employees fairly according to efforts expended and results produced creates a motivating work environment. A formalized pay program also establishes lines of progression and promotion opportunities, thereby increasing the possibility of having a sufficiently motivated workforce to perform the work of the organization.

1.10.4. Control Costs

A formal compensation program enables an organization to establish and maintain control over the largest segment of its controllable costs: salaries and benefits. Informal approaches to compensation can lead to spending too much or too little money on compensation. A formal program sets pay ranges for each job and institutes a cost-control mechanism. Without an effective compensation system, salary and benefit costs may be too high or too low.

Salary budgets can also be prepared more easily and realistically when a formal program exists. Merit-increase amounts can be budgeted; staff replacement costs can be ascertained; the dollar impact of adding new positions can be determined. Formalization, in short, provides a basis for effective control of compensation expenditures. Without it there is little or no basis for systematic control of salaries and benefits.

1.10.5. Prevent Pay Discrimination

Without a formal compensation program an organization has no assurance that jobs requiring equal skills and effort are being compensated at equal rates of pay. In other words, an organization may be in violation of the Equal Pay Act of 1963 and Title VII of the Civil Rights Act of 1964 without even knowing it. Thus, a company using an informal approach to compensation matters may find itself open to charges of pay discrimination, a serious and potentially expensive situation. The risk of pay discrimination is minimized considerably with a formalized program because jobs that are essentially equal are compensated within the same range of pay. This one benefit alone may well be worth the effort and expense of installing a compensation system in many organizations.

1.10.6. Assure Equity

Equity consists of three separate issues. First , there is matter of the internal equity of the organization's pay structure itself. Internal equity simply means that jobs requiring greater amounts of skill, effort, and responsibility are compensated at higher rates of pay than jobs requiring lesser amounts of skills, effort, and responsibility. In other words, internal equity-fairness in rewarding jobs based on the degree of difficulty entailed in performing those jobs-is based on a hierarchical arrangements of jobs and compensation rates that recognizes as fairly as possible the differences inherent in jobs, and pays them accordingly. Without formalization and the concomitant analysis of jobs, an internally equitable ordering of jobs from the least difficult and responsible (the lowest paying) to the most difficult and responsible (the highest paying) is practically impossible to achieve. Under an informal approach to compensation, some jobs will always be compensated more and some jobs will always be compensated less than they should be when compared to other jobs in the organization. A formal compensation program recognizes the differences in jobs and structures a pay system that accurately reflects these differences-it establishes internal equity.

Second, there is the matter of external equity-the fairness of the organization's pay as compared to similar organizations in the labor market. External equity is said to exist when the pay rates of the organization are equal to or closely approximate market rates.

Finally, there is the matter of perceived equity-the apparent fairness of the pay system, either internally or externally, as seen through the eyes of employees. Because perception is the only reality that matters to many employees, perceived equity is an extremely important concept in compensation. When a compensation program is perceived as being fair, there are likely to be fewer complaints and problems related to pay. when a program is perceived as unfair, there are likely to be numerous complaints and problems. An informal program is rarely ever perceived as fair. Rather, it is usually seen as biased, arbitrary, or capricious because employees may feel that there is no logic or system attached to it. A formal compensation program, relying as it does on job analysis, systems, and logic, is more readily perceived by employees as fair or equitable. Formalization of compensation programs increases the likelihood of perceived equity on the part of employees.

1.10.7. Reward Performance

A formalized compensation program creates a mechanism whereby employees can be rewarded on the basis of how well they perform their jobs. These rewards, typically in the form of merit pay increases or performance bonuses, are based on actual accomplishments as determined through a periodic evaluation of results produced. A formalized program recognizes degrees of accomplishment and structures merit increase along the lines of job performance, thereby assuring that higher performers receive larger rewards than lower performers. Informal approaches to compensation do not usually define or take into consideration degrees of employee performance; periodic pay increase is apt to be based on factors unrelated to how well the job is carried out. Informal approaches often lead to de-motivation because employees sense-and rightly so-that accomplishment in the job bears little or no relationship to the size of the reward given. A formal program corrects this problem and reinforces motivation to do a good job by relating the amount of pay increase to actual performance. A formalized compensation system thereby allows a firm to pay fairly for the job, and also reward the individual for his or her performance in that job.

1.10.8. Establish Hierarchy of Jobs

The development and establishment of lines of progression- a job hierarchy-along which employees advance from lower-level jobs to higher-level jobs is a further benefit arising from a carefully constructed compensation program. Job sequences are defined so that promotional sequence, sometimes called career paths or career ladders, are developed and can be communicated to employees, thereby allowing employees to recognize and prepare themselves for jobs of greater responsibility and higher pay. Informal programs usually have no clearly identified job sequences or career paths; at best only a hazy concept of career progression may exist. What is regarded in management's eyes as a promotion often turns out to be nothing more than a transfer in the eyes as a promotion often turns out to be nothing more than a transfer in the eyes of the employee. The reverse may also be true.

Lines of progression contribute positively to employee motivation and morale. Employees are able to recognize promotional paths that are open to them and can take positive strides to move themselves forward along those paths.

1.10.9. Improve Morale

Morale refers to the general level of satisfaction that employees, either individually or as a group, have about their employer. A number of factors affect and shape morale: The work itself, quality of supervision, personnel policies, opportunities for advancement, coworkers, and pay are a few of the most prominent. Morale is based on perception; that is, how something appears to be when viewed through the mind's eye rather than how it is in reality. Pay plays a major role in shaping morale. When compensation in all its facets appears to be fair and equitable, other morale factors tend to take on the appearance of being satisfactory. Dissatisfaction with pay typically results in dissatisfaction with other aspects of the job and employment situation.

Inasmuch as a formal compensation program utilizes a logical, systematic approach to set pay rates and determine the appropriate configuration of benefits, its impact on morale is positive. A rational approach to setting compensation enhances an employee's perception of fairness relative to pay matters. Perceived fairness in this area tends to suggest fairness in other areas, thereby increasing the employee's general level of satisfaction with the work situation. Informal compensation determination carries with it the stigma of whim, capriciousness, or arbitrariness-unfairness, if you will-and colors an employee's view of other morale factors accordingly.

1.11. COMPENSATION DETERMINANTS

Why do organizations pay what they pay? Nine major forces influence the general level of compensation that an organization must pay if it is to be successful in acquiring and retaining the kinds of skilled and motivated employees it must have to operate effectively and profitably. These factors are the labor market, ability to pay, cost of living, productivity, bargaining power, job requirements, worker competencies, managerial attitudes, and legislation.

1.11.1 The Labor Market

One of the primary determinants of compensation is the supply of workers with particular skills and the need that employing organizations within a particular labor market have for hiring workers with those skills. Where there is an abundance of available workers in the labor market, employers will have no difficulty in obtaining sufficient employees. Consequently, the level of compensation will tend to be lower because employers do not have to pay higher salaries and benefits to attract employees. On the other hand, where there is a shortage of skilled workers and the demands of hiring institutions for the particular skills possessed by those workers is great, compensation levels will tend to escalate as employers bid against each other to secure the talent they need. In either instance, the economies of the marketplace are operating to establish or at least significantly influence the level of compensation.

For several years now we have observed the forces of supply and demand at work in many industries and have witnessed their impact on compensation. The supply of workers with technical skills has trailed the demand for workers with these skills. As a result, compensation in technical occupations has significantly increased as firms vigorously compete against each other for the talent they need. Likewise, the demand for workers in services industries has outstripped the supply of workers for positions in these industries. In a tight labor market compensation rates have been forced upward. In other industries the demand for workers has fallen and compensation rates have been lowered.

1.11.2. Ability to Pay

Organizational profitability is another factor that affects compensation levels. Put quite simply, the higher profitability of an organization, the more it can afford to pay; the lower the profitability, the less an organization can afford to offer in compensation. Profit margins allow some employers to pay more while they compel others to keep compensation as low as possible. Certainly no firm wants to pay more than is necessary to attract the quantity and quality of workers needed, but some firms do have a greater degree of latitude than others, based on profit margins, in establishing specific levels of compensation.

1.11.3. Cost of Living

Cost of living refers to the amount of direct monetary compensation required by workers to maintain an adequate standard of living for themselves and their families. Although colored by individual perceptions of what is an adequate standard of living, the concept of cost of living establishes a floor for compensation levels. Workers will not normally accept a job at a rate less than the one they consider to be the floor, assuming of course that all other conditions are equal. Compensation rates for employers, consequently, are controlled on the low side by the perceived cost of living.

Employers who conduct business at geographically dispersed locations can attest to the impact that cost of living has on compensation levels. Living costs are not uniform throughout the United States, and neither are compensation rates. In New York City- a high-cost area-one can expect to find higher pay levels than in El Paso, Texas- a low cost-of-living area.

1.11.4. Productivity

A fourth determinant of compensation is productivity, the ratio of output to personnel hours of input. While productivity is often a vague, elusive, and hard-to-measure concept, it does influence compensation. Generally speaking, the more a worker can produce, the higher his or her compensation will be. Productive workers produce more goods at a lower cost, allowing the company to make a greater profit on the sale of these goods. This basic generalization is the foundation for paying various types of incentive compensation-pay based directly on output. At the level of the individual job, worker performance may be measured and rewards given for increased productivity due to individual worker efforts. At the office or facility level, compensation may be increased for exceeding stipulated measures of performance. In either case, compensation is affected by the productivity of employees.

Even where productivity cannot be directly linked to measurable output, it still exerts and influence on compensation rates. The notion that those individuals, those positions, or those groups that produce more than others should be compensated at higher rates is a strong one.

1.11.5. Bargaining power

Bargaining power refers to the ability of groups of workers to exert pressure on an employer and thereby increase compensation levels. This power is typically gained by banding together in unions. Unions have been able to raise rates of pay in specific companies and in the economy in general. Both direct and indirect compensation levels have been pushed to higher and higher levels because of the power or threat of collective bargaining.

Compared to an employer, an individual employee normally has little or no bargaining power- certainly not enough to affect general compensation rates. But collectively through unions, employees can, by threatening to withhold the supply of labor if necessary, influence compensation amounts and practices. Although the influence of unions has waned as the percentage of union members in the total American workforce has declined (only 14.6 percent of the total U.S. workforce was represented by unions in 1996), unions still exert pressure on compensation rates.

Even those institutions that are not confronted by unions feel the impact on pay rates brought about by bargaining power. As collective bargaining increases compensation rates in specific companies and industries, other companies and industries periodically have to adjust compensation levels to stay competitive in attracting and retaining the workers they need. Thus, bargaining power affects, directly or indirectly, all labor market organizations.

1.11.6 Job Requirements

Another determinant of compensation rates is the requirements of performing a particular job. Where long training periods are required to learn the skills necessary for successful job performance, compensation rates tend to be higher than they are for jobs where the training period is short or nonexistent. Higher rates attract more people to the field, thereby assuring employers of an adequate pool of talent from which to select employees.

Where jobs involve dangerous, difficult, or unpleasant work, pay rates typically include a financial inducement to attract workers to those jobs. For example, second- or third-shift employees are usually paid more than their counterparts on the first shift in order to offset the inconvenience-even danger in some urban areas-imposed by the requirement of working unusual hours. Job requirements, as these examples point out, directly affect compensation rates for certain groups of positions.

1.11.7. Worker Competencies

Organizational downsizing and the rampant development of technology have created a new compensation determinant: worker competencies. In a world of scaled-down organizations or small companies that thrive on rapid shifts in products or technologies, workers may be called upon to perform a number of jobs. In these companies employees are compensated not on the basis of the job they are currently performing, but on the basis of the number of different jobs they can perform. Workers are paid for the knowledge and skills they have acquired, regardless of whether these skills are actually being used.

1.11.8. Managerial Attitudes

Pay structures vary widely across company lines because of managerial attitudes concerning pay. Management's feelings about compensation lead to an organization's adopting one of three possible wage and salary positions: (1) compensate workers at rates that are comparable to the rates being paid by other firms in the labor market, (2) compensate employees at rates below those paid by other labor market organizations, or (3) compensate workers at rates that are above those currently being paid in the labor market. Each of these positions reflects management attitudes and philosophies about pay. Paying market rates suggests that management is concerned with maintaining external equity in order to assure a sufficient supply of workers and to hold employee turnover to an acceptable level. Paying below market rates suggests that management views compensation largely as a cost. Paying above market rates suggests that management is interested in attracting and retaining the best workers possible and is willing to spend money to do so.

1.11.9. Legislation

Since the 1930s federal legislation has had a significant impact on compensation levels. The fair Labor Standards Act of 1938 established a minimum wage and specified requirements for the payment of overtime. The minimum wage set forth by this act, as of 1997, $5.15 per hour, creates a base compensation rate that covers most U.S. workers. Moreover, the base rate stipulated by the act functions as an index that leads to wage increases for many other workers who are well past the minimum compensation level. As the minimum wage is increased, other wages also tend to rise. The specified minimum wage has been raised a number of times since 1938, and will continue to be adjusted periodically in the future.

The Equal Pay Act of 1963, an amendment to the fair Labor Standards Act, requires equal pay for equal work for men and women performing the same work. Equal work is defined as work that requires the same skill, effort, and responsibility and is performed under similar working conditions. The result of this piece of legislation has been to raise the general level of compensation for female employees. Both the fair Labor Standards Act and the Equal Pay Act have significantly affected overall compensation levels.

These nine factors tend to work in concert with each other rather than independently to affect compensation levels. A knowledge of and appreciation for the influence they exert are important for understanding that compensation levels are products of forces existing outside as well as inside a specific organization. The determinants of compensation, in effect, reduce the degree of latitude that and organizations has in setting compensation rates.

1.12 SUMMARY :

Compensation is the process of providing equitable and fair remuneration to the employees. Compensation Management includes 1) Job evaluation, 2) Wage and Salary Administration 3) Incentives 4) Bonus 5) Fringe benefits and 6) Social security measures, etc.

One of the most important factors in Personnel / Human resource Management is Compensation Management. The soundness of compensation management depends upon the amount of wage and salary paid to the employee for a fair days work.

Formulation and administration of sound compensation policy to attract and retain personnel in right position is the prime responsibility of my organisation (right person for right job with fair remuneration).

The main objective of compensation management is to bring cost-effective structure which attract, motivate and retain competent employees.

Compensation System is classified into two types, Direct Compensation and Indirect Compensation. In other way monitory and non-monitory compensation.

1.13 KEY WORDS :

Compensation : The term compensation refers to all forms of payment going to employees of all levels and arising from employment.

Wage : Compensation for services rendered by the pension whose output is related to production.

Salary : Salary is compensation for services rendered by the person whose output is difficult to be measured.

Internal equity : Internal equity means payment of similar job within the organisation.

External equity : External equity is known as payment of similar wages to similar jobs in comparable organisations.

Job evaluation : Job evaluation is a process of determining the relative worth of a job.

1.14. SELF ASSESSMENT QUESTIONS :

1) Define compensation and discuss its importance.

2) What is meant by compensation system ? Explain its objectives ?

3) What are the objectives of compensation management ? Examine the significance of compensation.

4) Briefly describe the classification of compensation and discuss requisites of effective compensation plan.

5) What functions are assigned for compensation in our economic system ?

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LESSON - 2

WAGE CONCEPTS

2.0 OBJECTIVE :

- After studying this lesson the student is able to :
- Understand the various concepts of wages.
- Study the recommendations of the committees on wage concepts.
- Visualise the implementation of wage concepts in practice.
- Compare the development of wage concepts in India.

STRUCTURE :

2.1 **Introduction**

2.2 **Wage Concepts**

2.3 **Minimum Wage**

2.4 **Need-based Minimum Wage**

2.5 **Fair Wage**

2.6 **Living Wage**

2.7 **National Minimum Wage**

2.8 **Money and Real Wages**

2.9 **Summary**

2.10 **Keywords**

2.11 **Self Assessment Questions**

2.12 **Further Readings**

2.1 INTRODUCTION :

Various classifications of employees may receive different forms of compensation. For example, production employees may receive hourly rates, piece rates or production bonuses, profit sharing, various forms of indirect compensation and several nonfinancial rewards. Clerical employees may receive monthly salary profit sharing, various other benefits and nonfinancial rewards. Technical and professional employees are normally paid a salary and include bonus plan in addition to indirect and nonfinancial rewards.

Various types of rewards / pay or wage and salary concepts are implementing for the practice of compensation for employee satisfaction and motivation.

2.2 WAGE CONCEPTS :

Wage and salary concepts are commonly using in compensation system and are often used inter changeably; some important wage and salary concepts are :

2.2.1 Wage :

Wages in more restricted sense, refers to the pay hourly rated or other non clerical and non supervisory employees.

International Labour Organisation (ILO) defined the term ‘wage’ as the remuneration paid for services of hourly, daily, weekly and fortnightly to the employees.

It also means that remuneration paid to production and maintenance or blue collar employees.

Webester’s Comprehensive Dictionary defines wages as “pay given for labour, usually manual or mechanical, at short stated intervals”.

2.2.2 Salary :

The term ‘salary’ is defined as “the remuneration paid to the clerical and managerial personnel employed on monthly or annual basis”. A periodic payment to persons doing jobs other than mechanical has little relevance in the context of changing technology.

The terms wage and salary can be used interchangeably. As such the term wage and / or salary can be defined as direct remuneration paid to an employee compensating his services to an organisation. Salary is also known as basic pay.

2.2.3 Earnings :

Earnings are the total amount of remuneration received by an employee during a given period. These include salary (pay), dearness allowance, house rent allowance, city compensatory allowance, other allowances overtime payments etc.

2.2.4 Nominal Wage :

It is the wage paid or received in monetary terms. It is also known as money wage.

2.2.5 Real Wage :

Real wage is the amount of wage arrived after discounting nominal wage by the living cost. It represents the purchasing power of money wage.

2.2.6 Wage Rates :

Wage rates are payments per unit, time units or output units.

2.2.7 Time Rates :

Time rates are based on a time unit which is, most commonly, the working hour.

2.2.8 Piece Rate :

Piece Rate is a payment of so much per unit produced, but commonly refers to payments under other 'incentive wage' plans.

2.2.9 Commissions :

Which represent a common method of paying sales men, are similar to piece rates but are based on price or value rather than physical units.

2.2.10 Bonuses :

Bonuses are extra compensation and are two principal types. The production bonus is a regularly scheduled reward granted for extra performance. The non production bonus is the festival or year-end bonus, etc.

2.2.11 Take Home Salary :

It is an amount of salary left to the employee after making authorised deductions like contribution to the provident fund, life insurance premium, income tax and other charges.

The important wage concepts "minimum wage, fair wage and living wage" are discussed below :

2.3 MINIMUM WAGE :

The concept of minimum wage was first developed in New Zealand and Australia. Initially this concept was used to settle the Industrial Disputes in these countries. In India, some experiments in using minimum wage regulation to eliminate 'sweating' that are the payment of exceptionally low wages.

"Minimum wage is the amount of remuneration which could meet normal needs of the average employee regarded as a human being living in a civilised society".

It is defined as the amount of remuneration, "which may be sufficient to enable a worker to live in reasonable comfort, having regard to all obligations to which an average worker would ordinarily be subject to".

There can be three kinds of minimum wage :

i) A minimum wage notified by the government under the Minimum Wages Act, 1948 for different scheduled employments; or

ii) A minimum wage drawn by an unskilled worker in an organised industry as a result of a wage settlement which is purely the result of hard bargaining or even of coercive bargaining; or

iii) Need-based minimum wage determined as per the norms prescribed by the 15^{th} session of Indian Labour Conference held in July, 1957.

The basic minimum wage is the bare subsistence wage; above that is fair wage; and beyond the fair wage is the living wage. The content of minimum wage is not fixed and static. It is dynamic and is bound to vary from time to time and place to place. The International Labour Organisation (ILO) lists three criteria for fixing of minimum wage. These are (i) the needs of workers; (ii) the capacity to pay; and (iii) wages paid for comparable work elsewhere in the economy or more generally the standard living of other social groups.

The Committee on Fair Wages (1948) felt that different considerations arise so far as the minimum wages was concerned. It observed that in foreign countries the 'living wage formed the primary basis of the minimum wage'. However, the level of national income in India was so low that the country could not afford to fix by law, a minimum wage which would correspond the concept of living wage. The committee felt that the minimum wage must provide not merely for the bare sustenance of life but for the preservation of the efficiency of the worker. For this purpose, the minimum wage must also provide for some measures of education, medical requirements and amenities.

The courts and tribunals laid emphasis upon fulfillment of the needs of an industrial worker, irrespective of the capacity of the industry or of his employer to pay. For instance, in Hindustan Times Ltd. vs. Their workmen (1963-I LLJ 108), the Supreme Court held that at the bottom of the ladder, there is the minimum basic wage which the employer of any industrial labour must pay in order to be allowed to continue an industry.

The National Commission on Labour (NCL 1966-69) had expressed the view that a national minimum wage in the sense of uniform minimum monetary remuneration for the country as whole. It however thought that regional minimum could be fixed in different homogeneous regions in each state.

There is already in existence a Minimum Wages Act, 1948 it lays down norms and procedures for the determination and fixation of minimum wages in the industrial services and agricultural sectors.

The conception of minimum wages is based on the principles of equity and social justice. Its underlying idea is that "he who works is entitled to a fair remuneration which may enable him to live a life consistent with human dignity". Wages are not an economic abstraction but an important price in society. Economically speaking, wages may be the price of labor, just a interest is the price of capital and profit, the price of risk carrying but from social point of view they are unique in that they not only constitute payment for this effort but also provide the means of subsistence for those who supply the effort.

2.3.1 Problems of Minimum Wages :

The problem of minimum wages is not as simple as it appears to be on the face of it. It really consists of so many problems. The first of these problems is to know what minimum wage implies. Should it be subsistence wage which may enable a worker to stay alive and maintain his working capacity or should it be a living wage which may also provide for the maintenance of health and efficiency, a measure of frugal comfort and some insurance against the more important misfortunes, or should it be a fair wage somewhere between the levels of subsistence and living wage, as permitted by country's economy. In considering these questions, one can hardly overlook the fact that minimum wage is essentially a relative term and may mean differently in different countries according to their state of social and economic development. Again, it will also have to be considered whether there should be adopted a national system of minimum wages providing for a uniform wage for all covered workers subject only to regional variations, or a sectoral system of fixing different minimum wage rates for different sectors or industries, or a combination of both these systems.

After these questions are settled, another problem that will require serious considerations is as to what methods and machinery should be used for fixing minimum wages. The Government can use both direct and indirect methods. The indirect methods may take the form of extending existing collective agreements to third parties, and regulation of wages in public employment and public contracts by inserting fair wage clause in all public contracts. The direct methods may take the form of fixation of minimum wages by statute or by order, regulation or decree of the Government without any consultation with the interests concerned; or fixing minimum wages on the recommendations of wage boards and wage councils on which the workers and employers may be equally represented; or by the award of arbitration or industrial courts. In case wage boards or wage councils are to be set up, it will have to be decided what should be their composition, functions and powers.

Another important question that will have to be considered is whether the minimum wage fixing machinery should be required to follow any criteria in determining and recommending minimum wages. Criteria which are generally followed for minimum wage fixing are the needs of workers, capacity of the industry or employment to pay, wages paid for comparable work elsewhere in the economy, standards of living of other social groups and requirements of economic development. All these factors are too important to be overlooked by any minimum wage fixing machinery. It is their consideration in a coordinated manner that may help to work out an acceptable minimum wage. Minimum wage fixers will have to see that minimum wages determined by them are neither too high nor too low, as that will not serve the cause of economic growth. They will have to exercise their judgement on this question by weighing the gains to workers who will benefit from higher wages against the various kinds of costs which higher wages may impose on the industry and the economy on the whole. They will also have to bear in mind the fact that raising of minimum wages is more likely to benefit the workers, and will also avoid serious economic dislocation, if it proceeds rather gradually and experimentally, probing to see how far wages can be raised without adverse repercussion on markets and employment, and giving employers time to absorb the effects of higher wage costs through higher productivity, than if large increases in minimum wages are imposed suddenly.

Another important point closely connected with the minimum wage fixing machinery is whether it should be statutory or backed by any law, and if so, what should be the type of legislation or regulations that the Government may enact.

The last but not the least important problem is that of the administration and implementation of minimum wage regulation and enforcement of minimum rates of wages that might be fixed. Mere enactment of minimum wage legislation and fixation of statutory minimum wages will hardly serve any purpose unless they are implemented and enforced effectively. The need for strict enforcement is still greater in the case of minimum wage laws as these are largely applicable to small sweated employments and have works, which present problems of their own. The difficulties of enforcement are greater in the case of such establishments as generally they do not maintain any record or accounts. It is to these establishments that much attention has to be paid. Their employers will have to be trained and made to keep proper records.

2.3.2 MINIMUM WAGES AND ILO

The need for regulating minimum wages has been gaining increasing attention not only of the governments of developing and developed countries but also of the International Labor Organisation (ILO) at Geneva, which is formulating International Labor Standards for its member countries since its very inception after the First World War. The ILO attached much importance to the question of fixing minimum wages as far back as 1921, and the result of its enquiry led to the adoption of a Convention No. 20 and a Recommendation No. 30 on Minimum Wage Fixing Machinery, 1928, covering only non-agriculture sector of employments. After 23 years that is, 1951 the ILO Conference at its 34th Session adopted a Minimum Wage Fixing Convention No. 99 and a recommendation No. 83 for agricultural employments. Since then, a number of conventions and recommendations have been adopted, having important bearings on the question of minimum wages.

2.4 NEED-BASED MINIMUM WAGE:

It was the historic session of the Indian Labour Conference held in 1957 at Nainital which, for the first time, attempted to put content into the concept of minimum wage for all workers in Industry. Following are resolutions adopted by the conference are reproduced below :

"With regard to the minimum wage fixation, it was agreed that the minimum wage was 'need-based' and should ensure the minimum human needs of the industrial worker, irrespective of any other considerations. To calculate the minimum wage, the committee accepted the following six norms and recommended that they should guide all wage - fixing authorities, including minimum wage committees, wage boards and adjudicators.

i) In calculating the minimum wage, the standard working class family should be taken to consist of three consumption units for one earner; the earning of women, children, and adolescents should be disregarded;

ii) Minimum food requirements should be calculated on the basis of a net intake of 2,700 calories, as recommended by Dr. Aykroyd for an average Indian adult of moderate activity. (Recommended by National Nutrition Advisory Committee, (NNAC)).

iii) Clothing requirements should be estimated at a per capita consumption of 18 yards per annum which could give for the average workers family of four, a total of 72 yards;

iv) In respect of housing, the norm should be the minimum rent charged by government in any area for houses provided under the subsidised industrial housing scheme for low-income groups;

v) Fuel, lighting and other miscellaneous items of expenditure should constitute 20 per cent of the total minimum wage.

While agreeing to these guidelines for fixation of the minimum wage for industrial workers throughout the country, the committee recognised the existence where difficulties might be experienced in implementing these recommendations.

Keeping in view the socio-economic aspect of the wage structure, it is necessary to add the following additional component as a guide for fixing the minimum wage in the industry;

vi) "Children's education, medical requirement, minimum recreation including festivals / ceremonies and provision for old age, marriages, etc. should further constitute 25 per cent of the total minimum wage"

The wage structure which approximately answers the above six components is nothing more than a minimum wage at subsistence level. The employees are entitled to the minimum wage at all times and under all circumstances. An employer who cannot pay the minimum wage has no right to engage labour and no justification to run the industry.

2.5 FAIR WAGE :

The Encyclopedia of Social Sciences describes "a fair wage" as one equal to that received by workers performing work of equal skill, difficulty or unpleasantness.

According to Prof. Pigou, "a wage-rate is fair in the narrower sense when it is equal to the rate current for similar workmen in the same trade and neighbourhood and fair in the wider sense when it is equal to the predominant rate for similar work throughout the country and in the generality of trades". (quoted in Express Newspapers vs. Union of India, 1961, I LLJ 363).

A fair wage is in the opinion of the Indian National Trade Union Congress (INTUC) "a step towards the progressive realisation of a living wage." A fair wage is settled above the minimum wage and goes through the process of approximating towards a living wage.

The committee on Fair wages (1948) stated that "fair wage was something between a minimum wage and a living wage" (Report was submitted in 1949.)

Present economic position of industry and its future prospects the fixation of "fair wage is between minimum wage and living wage" should be considered the following factors.

i) The productivity of labour;

ii) The prevailing rates of wages in the same or similar occupations in the same or neighbouring localities;

iii) The level of the national income and its distribution; and

iv) The place of the industry in the economy of the country.

The fair wages committee recommended that "fair wage should be fixed on industry-cum-region basis. That the basis of a fair wage is according to the fair wages committee is the minimum wage within the capacity of the industry to pay" and also the 'fair wage should be related with the productivity of labour'. Based on the recommendations of the committee, a bill was introduced in the Parliament in August 1950 known as "Fair wages bill". Getting fair wage is a fundamental right of worker which must be granted.

2.6 LIVING WAGE :

According to the fair wages committee "the living wage is the highest level of the wage and naturally it would include all amenities".

The most expressive definition of the living wage is that of 'Justice Higgins' of the Australian Commonwealth Court of Conciliation in the Harvester case. He defined the living wage as one appropriate for "the normal needs of the average employee, regarded as a human being living in a civilised community".

According to Justice Higgins the living wage must provide not merely for absolute essentials such as food, clothing for "a condition of frugal comfort (Food expenditure) estimated by current human standards".

According to the South Australian Act, 1912 the living wage means "a sum sufficient for the normal and reasonable needs of the average employee living in a locality where work under consideration is done or is to be done".

There are three possible ways of obtaining some indication as to what constitutes a living wage :

1) It should be sufficient to purchase the minimum theoretical needs of a typical family, calculated in accordance with some or less scientific formula.

2) It should be sufficient to pay for a satisfactory basic budget, as revealed by a survey of actual family expenditures.

3) It should be comparable with a living wage already established in similar circumstances.

It is a difficult task to fix a living wage in terms of money as it differs from country to country and from time to time, according to national economy and social policies.

The Directive Principles of State Policy of the Constitution of India enumerates the concept of living wage and provides that the sate (government) shall endeavour to secure to all workers a living wage.

The Royal Commission on the Basic Wage for the Commonwealth of Australia expressed that "the living wage should enable the male earner to provide for himself and his family not merely the bare essentials of food, clothing and shelter but a measure of frugal comfort including education for the children, protection against ill-health, requirements of essential social needs and a measure of insurance against the more important misfortunes including the old age.

The Committee on Fair Wages set the living wage standard as the upper limit of wage fixation, and the lower limit being minimum wage.

2.7 NATIONAL MINIMUM WAGE :

There is also widespread demand among the trade union circles for a national minimum wage. The expectation is that such national minimum :

a) National Minimum Wage will be fixed sufficiently high to confer substantial benefit on a large number of low paid workers.

b) It would eliminate regional disparities in wages.

c) It would provide a basis for collective bargaining for higher wages in every industry or occupation and

d) It would be easily implemented.

It would be understood that national minimum wage is more a function of development and influence that of under development and poverty. If a realistic national minimum wage is to be fixed in India today, it would be so low not to benefit many. Again there is a danger that the minimum will be treated as maximum by many employers especially in the unorganised sector. It is fixed at unrealistically high, it will cause inflation or will not just be implemented. The U.S.A. has a national minimum wage, so have most developed economics of the Western Europe. No developing country has fixed a national minimum wage which would apply to all occupations, agricultural and industrial sectors.

The National Commission on Labour (NCL) has not supported the idea of national minimum wage to a country like us. Its recommendations are :

a) "......... a national minimum wage in the sense of a uniform minimum monetary remuneration for the country as a whole is neither feasible nor desirable"

b) "It may be possible, however, that in different homogenous regions in each state regional minimum could be notified".

c) " .... the widening of the area of fixation of minimum wage beyond a state may be impracticable and also not in the best interest of the workers".

At the existing stage of development of our economy this may be regarded as wise counsel.

2.8. MONEY (NOMINAL) AND REAL WAGES :

Wages earned by employees are normally expressed in terms of money. There are two aspects of wages; one is expressed by the term 'money wage' while the other by 'real wage'.

Money wages give to the workers command over goods and services. The actual goods and services for which wages can be exchanged constitute their 'real' value. Money wage only express the amount in terms of currency. Money wages can most appropriately be compared with changes in the average price of a 'market basket' of the goods and services.

Real wages are calculated by relating changes in money wages to changes in the consumer price index. Real wages, in contrast to money wages, depend on the level of production. It provides the real test as to whether or not a worker is improving his economic well - being. Real wage also serves an index for measuring charges in the economic welfare of workers over long period of time.

2.9. SUMMARY :

The institution and implementation of wage concepts in organisations is crucial and should take utmost care on concepts of wages. Minimum wage, Need based-minimum wage, Fair Wage, Living wage and Money and Real wages are regularly practicing by the Personnel/HR executives. The concept of wages includes economic, sociological, psychological and organisational elements. In an industrial society, wage concepts determine the worker's way of life, including his social position.

2.10 KEY WORDS :

Wage : The remuneration paid by the employer for the services of hourly, daily, weekly and fortnightly employees.

Salary : The remuneration paid to the clerical and managerial employees employed on monthly or annual basis.

Minimum Wage : Payment to a workman, which just sufficient to cover food, shelter and clothing for himself and his family.

Need - based minimum wage : The amount of remuneration fixed on the basis of norms accepted at the 15th session of the Indian Labour Conference (ILC) held at New Delhi in July 1957.

Fair Wage : It is something more than minimum wage. Minimum wage is lower limit and higher limit is fair wage. Between these two limits, actual wages should depend on considerations of such factor 1) Productivity of labour 2) Capacity to pay by the employer 3) National income and its distribution.

Living Wage : Living wage is the highest amount of remuneration and naturally it would include the amenities which a citizen living in modern civilised society.

Incentive Wage : Remuneration paid to the worker over and above the normal wage as an incentive for employee’s contribution to the increased production, saving in time, material, or quality.

2.11 SELF ASSESSMENT QUESTIONS :

1) Briefly illustrate various compensation / wage concepts.

2) What is concept of minimum wage ? and discuss the types of minimum wage.

3) What is fair wage ? How the employer can pay the fair wage, based on the skills of employees.

4) Define living wage ? and briefly discuss the necessity of living wage in modern civilised society.

5) Differentiate and compare the relevance and importance of minimum wage, fair wage and living wage.

2.12 FURTHER READINGS :

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LESSON - 3

COMPENSATION / WAGE THEORIES

3.0 OBJECTIVE :

After studying this lesson, the student is able to :

- Review the history of Wage Theory.
- Visualise the classification of Wage Theories.
- Understand and analyse different Classical Theories of Wages.
- Know about different Modern Theories of Wages.
- Know how the Wage Theories are helpful to determine the wages.

STRUCTURE :

3.1 Introduction

3.2 Why a separate Theory of Wages

3.3 Classification of Wage Theories.

3.4 Classical Theories of Wages.

- **a) Subsistence Theory**
- **b) Wage Fund Theory**
- **c) Residual – Claimant Theory**
- **d) Surplus Value Theory of Karl Marx.**

3.5 Neo - classical Theories

- **a) Marginal Productivity Theory.**

3.6 Modern Theories of Wages

- **a) Demand and Supply Theory**
- **b) Bargaining Theory**
- **c) Taussig's Theory of Wages**
- **d) Employment Theory**

3.7 Other Theories

3.8 Summary

3.9 Keywords

3.10. Self Assessment Questions

3.11. Further Readings

3.1 INTRODUCTION :

Wage Theory, a highly systematised body of knowledge began to emerge some two hundred years ago. Over the years a number of theories have made their mark on the contemporary economic thought.

A variety of new social ideas, institutional forces, egalitarian and ethical considerations, social, legal, political and economic factors, demands of social justice and equity are at work in the establishment of a wage level and a wage structure. There is an imperative need for an acceptable wage theory to guide the compensation policy of a country.

The activity of trade unions and positive interference of the state (government) in the regulation of wages for the benefit of wage-earners has brought to light the inadequate treatment to the supply side of the wage theory.

Various theories of wage determination may be necessary in the scientific study of the problems of wages. Wages when determined are subjected to several theories of wages.

3.2 WHY A SEPARATE THEORY OF WAGES :

It is the demand and supply relationship, or scarcity in relation to demand, which explains all values of commodities or values of services of the factors of production. Why should we then have a separate theory of wages ?

The ordinary theory of prices, i.e., the demand and supply theory, is not full applicable to the determination of wages for the following reasons :

i) The demand for goods depends on their utility to the purchaser, whereas the demand for labour services depends on their productivity to the employer. Hence demand for labour needs a special treatment.

ii) The human element in the labour market deserves special consideration. The labourer and labour services are inseparably tied-up; hence the importance of the human element.

iii) The peculiar institutional and behaviour factors affect bargains in the labour market. For instance, in the rural areas of backward economics, wages are fixed by custom instead of compensation.

iv) Certain peculiarities of labour, which distinguish it from a commodity, also necessitate a separate theory of wages. These peculiarities are :

a) Labour has weak bargaining power as against the powerful employer;

b) Labour is not perishable;

c) The changes in the price of labour react rather curiously on its supply;

d) Supply of labour cannot rapidly adjust itself to the changes in demand.

In view of the above peculiarities of labour; it becomes necessary to formulate several theories of wages.

3.3. CLASSIFICATION OF WAGE THEORIES :

The wage theories are classified into three periods based on the history of wage theories. Prof. John. T. Dunlop classified the Wage Theories on the basis of supply of labour.

According to Dunlop :

i) The (First) Period up to 1870 (dominated by wage fund theory)

ii) The (Second) Period up to 1914 (Marginal productivity theory held sway).

iii) The (Third) Period extending from the first world war to till the present day (Collective Bargaining)

Prof. N.N. Chatterjee has classified the theories of wages into three types.

i) Classical Theories of Wages

ii) Neo-classical Theories of Wages.

iii) Modern Theories of Wages.

3.4. CLASSICAL THEORIES OF WAGES: The Period upto 1870

a) Subsistence theory :

Several theories have been put forward to explain the general level of wages prevalent in a country. Take first the subsistence theory, this theory originated with the Physiocratic School of the French Economists and was developed by Adam Smith (1723-90) and the later economists of the Classical School.

According to this theory, wages tend to settle at all the levels just sufficient to maintain the worker and his family at the minimum subsistence level.

Adam Smith stated "the ordinary wages of even the lower species of labour" cannot be reduced and this limit is set by the cost of maintenance of labour. "A man must always live by his work and his wages must at least be sufficient maintain his family at the minimum subsistence level.

The subsistence theory by Ricardo in 1817 "the labourers are paid to enable them to subsist and perpetuate the race without increase".

The German economist 'Lassalle' called the subsistence theory as "Iron Law of wages or "Brazen Law of Wages".

Karl Marx made it the basis of his theory of exploitation.

Population was increased faster than the means of subsistence and mass of the workers were receiving wages that barely furnished subsistence. The subsistence theory evidently based upon "Malthus" law of population".

Criticism :

In backward countries, wages no doubt are to be found at or near subsistence level. But the theory does not apply to advanced countries like England and America.

Another criticism of the theory is that the subsistence level is more or less uniform for all working classes with certain expectations. The theory, thus does not explain differences of wages in different employments.

The main weakness of this theory lies in the fact that it does not accept the importance of productivity.

b) Wage Fund Theory :

This theory is associated with the name of J.S. Mill asserts that wages were paid from a fixed fund. It was held that the lump sum had been distributed equally among the workers obtained in the labour market.

'J.S. Mill' wrote the wages depend upon the demand and supply of labour, or as it is after expressed on the proportion between population and capital. He asserted, wages not only depend upon the relative amount of capital and population, but cannot under rule of competition.

According to this theory, therefore wages depended upon two quantities, viz.

i) The wage fund or the circulating capital set aside for the purchase of labour; and

ii) The number of labours seeking employment.

According to J.S. Mill the wages are determined on the basis of the relationship between the amount of fund allocated for the purpose of wage payment and number of workers in a country.

$$\text{Wage} = \frac{\text{Amount of fund allocated for wage payment}}{\text{No. of workers.}}$$

The wage are paid for fixed wage fund.

Criticism :

This theory has been widely criticised that wages were paid out of circulating capital alone. Whether the source of wages is capital the present product, has been the subject of a keen controversy.

According to this theory, wages can increase only at expense of profits. But this is not necessarily so. In times of business prosperity both wages and profits can go up.

Moreover, the wage fund theory does not explain why wages differ in different occupations.

c) Residual – Claimant Theory :

The Residual - Claimant theory has been advanced to American economist Francis A. Walker (1840-1897) the wages are determined on the basis of the amount left after the payment of rent, profits and interest to land, entrepreneur and capital respectively out of the production value.

The amount of wages = Production value - (Rent + Profits + Interest)

Thus, this theory can be applied more than one of the factories of distribution, is unsatisfactory. This theory was designed to emphasise the interest of the working class in continual process and accumulation.

Criticism :

This theory ignores that wages are first charge on an industry. It does not explain how trade unions are able to increase the wages.

This theory ignores other factors which influence wage determination. Further this theory did not consider the aspect of labour market and the role of labour in productivity.

d) The Surplus value theory of Karl Marx :

According to Marx, the simplest concept which related to man's activity of producing his means of livelihood was human labour. Wages were basically inadequate payment for the surplus value created by the workers for employer. He accepted the view of 'Ricardo' that the wages paid were nearly subsistence wages. Under the capitalist system labour was nearly a commodity and could get its subsistence. The capitalist was in a position to force the worker to spend more time on his job than was necessary to earn this subsistence.

According to Marx the price or exchange value of any product was determined by the amount of labour time "socially" necessary to create it. The employer shall provide full compensation for the time, the worker gave in creating goods and services. The excess product or surplus value, thus created, was taken partly, by the entrepreneur and the balance of 'surplus' went to pay rent, interest and profit. So this was the systematic exploitation of labour and made the rich richer and poor poorer.

3.5 NEO - CLASSICAL THEORIES :

II) THE PERIOD UPTO 1914 :

The modern period of wage theory commenced with the formation of the Austrian school of Economics and the development of the Neo-classical doctrine of marginalism.

a) The Marginal Productivity Theory :

This theory was most generally accepted theory of wages. This theory was first developed by 'Phillip Henry Wicksteed', England and 'John Beat Clark' in U.S.A. 1890. According to J.B. Clark the wages are determined on the basis of marginal contributions of the worker to production. The employer stops employing further workers where the contribution of the most recently employed workers are equal to his wages.

In 1930, John H. Robinson - England and Edward. H. Chamberlain, USA added refinements to the analysis of marginal productivity. This theory does not nearly deal with labour productivity but deals with factors of production.

In relation to the wages the theory holds that an employer will tend to his workers of a particular type of with a particular skill for a certain operation until the contribution made by the last worker (marginal worker) to the total value of the product is equal to the total cost caused by the hiring of one more worker. The theory relies on the prevailing market rate for wages of different categories of workers through the operation of the demand and supply mechanism. The theory assumes that the operation of competition will assure the worker that he will receive a wage at least equal to the marginal product.

Limitations :

1. It is a static theory, labour is not perfectly mobile. Workers of the same skill and efficiency may not receive the same wages at two different places.

2. The market for goods is in general characterised by imperfect competition.

3. The productivity of workers is also dependent on factor such as the quality of capital and efficiency management. These factors are outside the control of workers.

4. Finally, productivity is also a function of wages. Low productivity may cause low wages, which may tell on the efficiency of the worker, lower his standard of living and ultimately check the supply of labour. The theory takes the supply of labour for granted.

3.6 MODERN THEORIES OF WAGES :

III) THE PERIOD AFTER FIRST WORLD WAR TO TILL DATE.

a) Demand and Supply Theory of Wages :

Although labour has certain peculiarities and cannot be regarded as am ordinary commodity, still wages are largely determined by the interaction of demand and supply as in the case of ordinary commodity.

Demand for labour :

The demand for labour is a derived demand. It is derived from the demand for the commodities it helps to produce. An 'expected' increase in the demand for a commodity will increase the demand for the type of labour that produces this commodity.

- Elasticity of demand for labour depends on the elasticity demands for its output.

- Demand for labour depends on the prices of the operating factors. (Ex : Machines are costly, more labour will be employed or the demand for labour will increase).

- Demand for labour is technical progress. (Ex : The introduction of automatic looms reduces the demand for labour)

Thus the demand for labour is determined by :

a) The nature of demand for the product of labour.

b) The proportion of the cost of labour to the total cost of the product.

c) It is substitutability by other factors; and

d) Supply of capital as determined by the ability and willingness of investors to save and invest.

Supply of labour :

The supply of labour depends on :

a) The number of workers of a given type of labour which would offer themselves for employment at various wage rates; and

b) The number of hours per day or the number of days per week they are prepared to work;

c) Supply of labour to a firm;

d) Supply of labour to the industry; and

e) Supply of labour to the entire economy.

To a given firm, the supply of labour is perfectly elastic because the 'current wage rate, it can engage as many workers as it wants. Its own demand constitutes only a negligible fraction to the total supply of labour.

b) Bargaining Theory :

Bargaining theory of wages was propounded by John Davidson in 1889. According to him the wages are determined by the relative bargaining power between workers or trade unions and employers.

This theory has in recent years, especially since 1933, gained steadily at the expense of the weaknesses of the marginal productivity theory.

According to this theory the wages and other terms of employment are determined on the basis of the relative bargaining strength of the two parties, i.e.; employer and employees. 'Webbs' stated that the haggling of the market which under a system of free competition and individual bargaining determines the conditions of the employment.

This theory holds that wages are determined by the relative bargaining power of employees and employer.

c) Taussig's Theory of Wages :

According to American economist Taussig who gives a modified version of the marginal productivity theory. The wages are discounted the marginal of labour.

He thinks that the worker cannot get the full amount of the marginal output. This is because of production takes time and the final product of labour cannot be obtained immediately but the workers have to be supported in the mean time.

The employer does not pay full amount of the expected marginal product of labour. He deducts a certain percentage from the final output in order to compensate himself for the risk he takes in making the advance to support the workers.

Criticisms :

i) A dim and abstract one, remote from the problem of real life.

ii) That the joint product is discounted at the current rate of interest.

d) Contribution of Keynes to wage theory (Employment Theory).

John Maynard Keynes in General Theory of Employment, Interest and Money (1936) has developed a new approach. Keynes has rejected the classical theory of wages, in his theory of employment, he advocated wage rigidity in place of wage flexibility. "There is .... no ground for the belief that flexible wage policy is capable of maintaining a state of continuous full employment".

He stated that "a reduction of wages will mean some reduction in prices, with its main effect an redistribution of real income from wage earners to other members of the community who enjoy more stable earnings".

The three essential ideas in the Keynesian wage policy may be stated as a national wage policy, a stable (rigid) money wage level in the short run and a rising money wage level in the long run.

3.7. OTHER THEORIES :

a) Exploitation Theory:

In the Wages of Labor, Adam Smith suggested the basis for an exploitation theory. He referred to the original state of things in which the whole produce of labor belonged to the laborers and when there were no landlords or masters to share with them.

However, Karl Marx, a contemporary of Mill, drew more extensively from the writings of Ricardo and his followers. From Ricardo he adopted such ideas as the labor theory of value, the Ricardian theory of rent, and the notion that wages and profits increase only at the expense of one another.

Starting with Ricardo's notion that labor creates all value, Marx contended that profit, interest, and rent are unwarranted deductions from the product that labor alone creates. According to Marx, the capitalist compels his employees to work for more hours a day than is necessary in order to produce their subsistence. The difference between the exchange value of the workers' product and the subsistence wages they receive is the "surplus value" that is "expropriated" by the capitalists and distributed as profit, interest, and rent. In short, Marx assumes that laborers produce an "expropriated" amount in addition to their subsistence and that the capitalists, through superior bargaining power, can force the workers to perform that additional work.

b) Labor Theory of Value:

According to Marx (1893), the simplest concept which related to man's activity of producing his means of livelihood was human labor. He considered labor as an article of commerce which could be purchased on payment of subsistence price. The price of any product was determined by the labor time needed for producing it. But the laborer was not paid in proportion to the time spent on work but much less and the surplus went to the owner. His theory is also known as surplus value theory of wages. Labor might be viewed in its natural (universal) form and in its social (historical) quality. As such, 'labor is a natural condition of human existence; a condition of the metabolism of man and nature which is independent of all social forms'.

There were, according to Marx, two further aspects of labor in that form- particular labor, and the sum-total of the individual labor of all members of society which produced the sum-total of use-value which society required. In its second aspect, labor required a social significance. He further clarified that a commodity might have use-value without having any exchange-value at all, e.g., gifts of nature. But exchange-value presupposes a use-value. The qualities which gave a commodity use-value were, in the capitalist system, the material carriers of exchange-value. The exchange-value of a commodity was nothing but a function of abstract human labor; its measure, the amount of value-forming substance, i.e., labor, which it contains. The measure of the exchange-value of a commodity is the socially necessary labor time embodied in the production. He observed that socially necessary labor time is the labor time necessary to produce any use-value with the given normal conditions of social production and the social average degree of skill and intensity of labor. Marx's contention that all value is created by labor had popular appeal since the generation of surplus value in the form of rent, interest and profit was construed to mean that labor is exploited.

c) Competitive Theory:

The force on which economists have traditionally laid the greatest stress in wage determination is demand and supply. Adam Smith, an early English economist (1723-90), argued that if wages were fixed in accordance with demand and supply, workers would be attracted by high wages to industries, occupations and localities where they were most needed and would tend to leave industries and places where the supply of labor was greater than demand. More precisely, the basic assumption of competitive theories of pay is that employers compete among themselves by offering a higher wage to attract employees; while the employees compete with others for jobs by offering their services for a lower wage. Competition, then, is essentially a disequilibrium process by which excess demand and excess supply cause changes in wages.

The competitive theorists assume that neither employers nor employees combine together to influence demand or supply conditions and that markets are perfect. But these do not hold good in the case of a monopolistic world market. The most conspicuous type of labor market monopoly in modern capitalist economies is that which arises when employees combine together into trade unions, professional associations, and similar groupings, formal and informal. Further, social forces may restrict the effective adjustment of demand and supply; for example, when workers are unwilling to move away from their home localities in order to work for high wages elsewhere. Similarly, the forces of demand and supply may be affected by government intervention in the regulation of wages, the application of awards, and the statutory extension of the provision of collective agreement to employers and workers who were not parties to them.

d) Low-Wage Labor Market Theory:

There are several conceptual approaches which can be adopted for analyzing the behavior of low-income labor marker. One such theory is known as the Queue theory. Stated in its simplest form, the Queue theory asserts that workers are ranked according to the relationship between their potential productivity and their wage rates. The most preferred workers are selected from the queue first, leaving the less preferred to find work in the least desirable jobs on the fringes of the economy or to remain unemployed. The disadvantaged have limited access to the most preferred employment opportunities.

Another theory related to low-income labor market is the dual labor market theory. This theory argues that the labor market is divided into primary and secondary markets. Jobs in the primary market possess several characteristics, such as high wages, good working conditions, employment stability, chances of advancement, equity, and due process in the administration of work rules. On the contrary, the jobs in the secondary market tend to have low wages and fringe benefits, poor working conditions, high labor turnover, little chance of advancement, and often arbitrary and capricious supervision. The disadvantaged workers are confined to the secondary and capricious supervision. The disadvantaged workers are confined to the secondary market which is associated with a much higher level of frictional unemployment and high levels of turnover.

e) Purchasing Power Theory:

According to this theory, wage increase are desirable because they raise labor income and thereby stimulate consumption. Since wage earners spend a very large proportion of their incomes, it is held that higher wages will result in a rise in consumer spending and thus act to sustain or to stimulate the economy. This argument has been used by the unions in all periods, boom, recession, and recovery which is not sustainable. The under consumption theory used by the unions is not the only cause. Purchasing power and consumption are usually increasing just prior to recession; workers account for only part of total consumers spending; the assumption that general overproduction can be overcome by higher wages; are some of the basic limitations of this theory.

f) Micro-economic Wage Theory:

Many economists and institutions have tried to explain and weave out wage theories. After discussing the various wage theories, Jean Marchal advocated the necessity of evolving a truly micro-economic wage theory.

According to Jean Marchal, such a theory must have three essential requirements:

1. The usual concept of wages must be replaced by a wider concept.

2. General behavior of employers and workers affect the general price level only if there is sufficient compatibility between the structures of the groups and of production.

3. Integration of the theory of wages into a theory of national income distribution.

g) Multi-Disciplinary Theories:

A number of multi-disciplinary theories have emerged to encompass the increasing range of variables which empirical work provided. Lester (1952) has studied labor market behavior to explain wage differentials by contemplating what he calls competitive, anti-competitive and impeditive factors. Reder (1962) has considered economic, psychological and institutional factors in his theory of wage determination. Dunlop (1950) relates an organisation's internal wage structure to its milieu through a limited number of key job rates and key settlements determined by techno-logy, administrative practices, product market competition and source of labor supply.

Dunlop sought to identify job clusters by which he meant a stable group of jobs within a company linked together by technology, administrative organization, and social custom. Further, he conceived of wage contours- a stable group of firms linked together by a common product market, labor market or custom so that they have common wage-making characteristics. Such a wage contour was visualized to have three dimensions- occupational, industrial and geographic. The wage-making forces were hypothesized to be concentrating on key rates in job clusters. Indeed, the task of analyzing wage determination is not the problem of setting a single rate but rather the problem of setting and variation in the whole structure of complex of rates.

Livernash (1957) has developed Dunlop's concept of job clusters further to show that in an organization there are broad clusters containing narrower clusters. Ross (1956) has contended that wage contours were affected by customs in the shape of traditional or historical differentials and that inter-industry comparisons are the strongest force in wage determination.

Quite a number of economists have put forward wage-push theories of inflation which implicitly or explicitly involve the notion that the behavior of the general money wage level is influenced by ideas of fairness. The wage-price spiral theory maintain that unions have particular ideas about what would constitute a fair real wage, and that wage demands and settlements are dependent on the behavior of the general price level.

In sum, according to the subsistence theory, the sex instinct of the workers, by increasing the labor supply, is the chief factor in wage determination. The wage fund theory, although still retaining the notion that workers are responsible for the supply, placed the emphasis on the demand side, with the demand for labor depending largely upon the intention of the capitalist employers. The “exploitation” theory of Karl Marx places the responsibility for wages and the wage level upon the capitalist employer, emphasizing his power to exploit the workers. The residual-claimant and bargaining theories, in turn, place a part of the responsibility for wage determination upon the workers. The marginal productivity theory has been used to place the primary responsibility for employment and wages upon labor itself. A discussion of wage theories reveals that each theory contains some truth, but none of them alone covers the whole ground and explains all the facts.

3.8. SUMMARY

Wage theorists have given much thought and devoted much research to attempting to discover an acceptable general theory of wages that would explain in all circumstances the way in which the level of wages are determined. No such theory has been worked out because the factors affecting wages are very complex and are closely linked with the whole economic and industrial system and with social considerations. However, Prof John. Dunlop and N.N. Chatterjee classified the wage theories are i) classical ii) Neo-classical and iii) Modern theories of wages.

Ricardo’s Iron Law of wages; which postulates that there is a ‘natural wage’ for labour which is the ‘subsistence wage’, and which cannot be increase or decrease without adversely affecting the supply of labour.

Adam Smith’s ‘Wage Fund’ theory states that a predetermined fund of wealth, surplus to the personal needs of the employer, exists for paying labour.

‘Karl Max’s’ ‘Surplus value’ theory of wages, according to Marx the wages paid were an inadequate payment for the surplus value created by labour, and the labour was exhibited by the capitalist systematically.

The Bargaining theory is applicable is all free societies and partially in communist countries. However, state intervention restricts the area of collective bargaining.

Marginal productivity theory postulates that the last workman in a certain category employed would be the one who produces just about enough to cover the cost of living, and that those who were engaged earlier to produce more, and that by paying all at the rate the marginal worker is paid, the employer gains substantially.

The demand and supply theory explains how the interaction of demand and supply for labour influences the wage rate.

Keynes examined the impact of money wage cut on the determinants and concluded that they were not favourably influenced by such a general cut in money wages.

3.9. KEY WORDS :

Subsistence : Wages tend to settle at the level just sufficient to maintain the worker and his family.

Wage Fund : The wages are paid for fixed wage fund.

Residual Claimant : Wages are the residue left over, after the other factors of production have been paid.

Marginal Productivity : The wages received by the marginal labour determines the wages paid to all the other labourers in the same grade.

Surplus Value : Labour was not paid in preparation the time spent on work built much less and surplus went to the owner. This is known as surplus value.

3.10. SELF ASSESSMENT QUESTIONS :

1. Out line the 'Dunlops theoretical scheme, and discuss briefly.

2. Why are the classical theories of wages so different from the modern theories of wages?

3. Explain the marginal productivity theory of wages is inadequate and which modern theory that is useful to determine the wages effectively to the labour.

4. Elaborately discuss the modern theories of wages in the economy ?

5. How does the shape of demand and supply function and narrate its importance in the wage determination.

3.11. FURTHER READINGS :

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LESSON - 4

COMPENSATION / WAGE POLICY IN INDIA

4.0 OBJECTIVE :

After studying this lesson, the student is able to :

Know about the Compensation Plan and Programme in an Organisation.

* Discuss the Compensation Policy in an Organisation.
* Know the need for Compensation Policy.
* Understand the wage/compensation policy in India.

STRUCTURE :

4.1. **Introduction.**

4.2. **Compensation Plan in Organisations**

4.3. **Compensation Policy in Organisations**

4.4. **Objectives of Compensation Policy**

4.5. **Need for National Compensation Policy**

4.6. **Formulation of wage/compensation policy in India**

4.7. **Wage Policy in the Post-Independence Period**

4.8. **Policy enunciated in the Plans**

4.9. **Recommendations on Wage Policy**

4.10. **Summary**

4.11. **Key words**

4.12. **Self Assessment Questions**

4.13. **Further Readings.**

4.1.INTRODUCTION :

Wage / Compensation Policy forms a highly sensitive and complex dimension of labour policy in view of a widespread impact of wages on the relative status of workers, their commitment to industry, their level of motivation, morale, productivity and standard of living. It is not merely an economic phenomenon but also a multidimensional social issue which is of interest to the consumers, the state and the society as a whole. In this context the National Commission on Labour examines various issue of wage policy.

4.2. COMPENSATION PLAN IN ORGANISATION :

The actual payment of wage and salaries or compensation of employee consists of two basic elements. Viz. a) money wages or salaries and b) supplementary payment plans such as bonus, profit sharing and fringe benefits of economic value. In India the basic methods of industrial remuneration or wage payments are two types i.e. i) Time rate system and ii) Payments according to output. Both time and output (piece rate) basis of payments are interrelated and are not mutually exclusive to favourable impact upon employee productivity and morale in either case. Therefore to develop effective compensation, consider an ideal system or plan should fulfill certain characteristics such as.

1. The compensation plan should be satisfactory from the point of view of both the employees as well as the employer.

2. It should be capable of providing incentive or motivational effect to workers as may be necessary to accelerate productivity and raise employee's good will and morale.

3. Compensation plan should be fairly simple to calculate or understand as well as flexible so as to make adjustments in the event of conflicts or wage disputes in the organisation.

4. It should be devised in a manner which avoids / minimizes conflict or wage disputes as far as possible in organisations.

4.3. COMPENSATION POLICY IN ORGANISATIONS :

The compensation policy in all organisations is a complex and sensitive area of Personnel/Human Resource Management. The relative states of workers/employees in the society, their commitment to work and attitude towards management as well as their morale and motivation towards productivity etc., are all conditioned by the wages or salaries they get. All most all organisation/companies want their employees to be well paid and work hard, to be an accurate and reliable and show reasonable interest in the organisation they serve but they hope to get this kind of performance by paying them a fair wage or salary.

Employee's concept of fairness as suggested by Dalton. E and McFarland, depends on company's relative wage rates. Employees want to be paid in relation to the work and similar work should involve similar rates of pay. Since the general acceptance of the company's basic wage or pay structure is important. Statements on Personnel/HR Policies should include the general altitude of the company towards key wage and salary matters such as the level of wages and salaries, problems of manpower supply, labour market, factory, union, company relationships and approaches to the role of ability and seniority in selling particular rates.

In planning and developing a sound compensation policy/programme, compensation manager/wage and salary administrator keep in view the organisations guidelines of general policy on compensation. The company wages or compensation policy may seek to assure a competitive wage or salary or it may be higher than average level. Besides, the statements of policy on compensation may also seek to specify relationships within the wage and salary structure or compensation policy may propose to establish priorities among these and other intentions or it may outline differing intentions for various types and groups of employees, consider the principles of "equal pay for equal work and equal pay for the same job regardless of the gender.

The wage and salary structure should be flexible so as to permit necessary adjustment due to changes in conditions or circumstances. There should be a clearly defined procedure for minimizing and resolving wage disputes, if any as quickly and effectively possible. It is necessary that company wage/compensation policies ought to be seen as an internal part of the structure of Personnel/Human Resource function.

Compensation Policy should aim to achieve the following :

a) attract staff of the right caliber;

b) encourage staff to make full use of their abilities and develop their potentials and to strive to achieve the objectives of their jobs and of the organisation;

c) reward staff in accordance with the value of their contribution;

d) prevent loss of morale through dissatisfaction with levels of pay.

e) facilitate movement of staff across departmental, divisional or sectional boundaries;

f) achieve these aims at minimum cost affect into over payment must be avoided.

4.4. OBJECTIVES OF WAGE/COMPENSATION POLICY:

The real purpose of wage policy is to protect workers against exploitation or unduly low wages; improve workers efficiency and performance, encourage acquisition of new skills, provide an incentive to labour mobility, stabilise prices and acceleration of the nation's development process. As an instrument of economic policy, wage policy was considered as a means of promoting; (i) investment; (ii) internal price stability; (iii) worker efficiency; (iv) distribution of labour force; (v) the international competitiveness of economy, and (vi) influx of foreign capital. As instrument of social policy, it was widely known as

i) an alternative to social security systems

ii) a means of achieving industrial peace, and

iii) a vehicle for securing social justice.

The ILO Publication (Problems of wage policy in Asian countries, 1956, P.39) has enumerated the following objectives of a wage policy in developing countries. They are :

1) To abolish malpractices and abuse in wage payments.

2) To set minimum wage for workers whose bargaining position is weak.

3) To obtain for workers a just share in the fruits of economic development.

4) To bring about efficient allocation and utilisation of manpower through wage payment systems.

4.5. NEED FOR NATIONAL WAGE/COMPENSATION POLICY :

The formulation of a proper wage policy consistent with the requirements of a developing economy is best with numerous difficulties. There are innumerable obstacles in the way of evolving such a policy and these are further compounded by population pressure, growing inequalities of income, historical past, dualism in the economy, increasing unemployment, and low rate of growth. There is an urgent need in our country to guarantee a certain minimum living wage to the workers, so as to remove sweating and to improve productivity.

The International Labour Organisation (ILO) has defined the term 'wage policy' to mean "legislation or government action calculated to affect the level or structure of wages or both, for the purpose of attaining specific objectives of social and economic policy." Generally, a wage policy aims at imposing a discipline on all types of wage payments so that excessive, inadequate, or inappropriate wage payments may not stand in the way of fulfillment of the objectives, both economic and social, which any country sets for itself in the pursuit of continued progress and national development. A progressive and realistic wage policy is an instrument in attaining such social objectives as the elimination of exceptionally low wages, reduction in wage differentials and the protection of real wages.

National Wage Policy:

The Report of the committee on Fair Wages as far back as 1948, the entry of the legislation on minimum wages in the statute book the same year, the series of adjudication and judicial pronouncement, the tripartite conclusion of the 15th session of Indian Labor Conference on the need-base wage, the setting up of a number of wage boards for major industries, the five pay commissions for Central Government employees and the industry-wise or unit wise bipartite negotiating bodies all no doubt have done very useful work. But their work was not regulated by a coordinated national wage and income policy.

The need for evolving a national wage policy has been subjected to inconclusive national debates and studies sponsored both by the government and professional bodies for over two decades. However, certain piece-meal and ad hoc efforts have resulted in the formulation of a few components of wage policy, mostly at the micro level. At the macro level too, some guiding principles have come to stay in the case of organized sector. They are:

(i) A national minimum floor independent of capacity of industry to pay;

(ii) The concept of 'capacity of industry to pay' for arriving at a wage level above the minimum floor;

(iii) Instrumentality of the dearness allowances to protect the purchasing power;

(iv) The doctrine of deferred wage and profit sharing subject to the availability of re-allocable surpluses;

(v) The linking of increase in wages to the increase in production and/or productivity; and

(vi) A rational basis for determining the wage differentials taking into consideration the skills, physical efforts and working conditions, etc., required by different categories of jobs, within an industry and in relation to other other industries.

In India, the basic objectives of a national wage and income policy may be stated thus:

(a) To provide minimum wages to workers employed in sweated industries;

(b) To fix wage ceilings;

(c) To improve the existing wage structure;

(d) To control inflationary tendencies;

(e) To accelerate export promotion; and

(f) To improve the economic and social position of the working class.

Its specific objectives are:

(i) To distribute the national product equitably by enlarging the incomes of the poorer sections of the people and avoiding concentration of wealth;

(ii) To regulate the growth of the disposable income aiming at a level and pattern of domestic consumption so as to generate adequate saving for non-inflationary financing of required investment;

(iii) To prevent the owners of capital to take undue advantage of the imperfections in the labor market;

(iv) To ensure a fair comparability of wages between different industries, different regions, and between the public and the private sectors, keeping in view the national and social objective of an equitable distribution of national wealth; and

(v) To prevent inflationary tendencies and instability in price level in the national economy.

However, the wage policy evolved hitherto has failed to achieve the desired objectives. It is a well known fact that there are disparities and inequalities in wages and working conditions in the organized and unorganized sectors, and between public and private sector undertakings. Further, wage differentials and disparities exist for similar jobs from industry to industry, and within the industry between the public and private sectors. But in the present context, any national wage policy, howsoever comprehensive and rational it may be, will not be able to remove overnight the existing distortions that have taken place in the wage structure. Now what it can and should aim is to put an end to the continuing pathogenic distortions and inequities by providing a rational basis for wage determination in the future.

The major thrust of the policy should be towards:

(a) Arresting the progressive deterioration of the purchasing power of the pay packet of the workers;

(b) Effecting improvement in the distribution pattern of the national dividend among the different functional sectors;

(c) Bringing and improvement in the economic conditions of the working class in general and of the industrial workers in particular, giving them a share of productivity gains;

(d) Introducing and ideal productivity based wage policy linked to the weighted average of the rate of productivity increases at the national, sectorial, and firm levels; and

(e) Assigning due weight to two basic components-the skill component and productivity component-besides the components of minimum wage and the cost of living.

Though a national wage policy should aim at elimination inter industry wage difference for comparable type of work, such a policy has to keep in view appropriate occupational wage differences for encouraging skill formation or compensation for hazardous and/or arduous nature of the job. The inter-regional differences in wages have to be viewed in the context of differences in employee compensation in the same industry groups and between different regions. In addition, significance of the wage-earners' consumption basket should not be lost sight of.

Successive family budget surveys among wage earners in the different sectors have shown the predominance of agricultural products, and especially foodgrains, in the consumption basket of the wage-earners. Therefore, the effectiveness of any wage policy would largely be dependent on adequate increase of farm output combined with an effective public distribution system. In specific terms, the issue and problems of the wage policy are related to the elements like need-based minimum wage, protection of real wages through compensation for rise in the cost of living, incentives for increases in productivity, allowance for hazards in occupation, wage differentials for skills, responsibilities and other justifiable reasons, essential fringe benefits, bonus and such other ex-gratia payments.

Some suggestions for determining a national wage policy are:

1. It should lay down the criterion for fixation and revision of minimum wages and evolve a wage structure without impinging on the freedom of the parties to negotiate wage agreements.

2. A set of norms has to be evolved for a general minimum wage below which nobody should be paid.

3. The minimum needs of the workers may be determined on the basis of the criteria adopted by the Planning Commission for defining the poverty line.

4. A floor level general minimum wage may be fixed for all employments not included in the schedule to the Minimum Wages Act.

5. Minimum wage should comprise basic wage, fixed dearness allowance related to this wage at a fixed time limit and a variable dearness allowance formula which may be adjusted to a rise or fall of the consumer price index, local or all-India as may be appropriate.

6. The quantum of basic wage be reviewed, if necessary, at an internal of not less than five years or so as to amalgamate a part of dearness allowance to avoid distortion in the wage pattern.

7. If the minimum wage is not split up into a basic wage with a fixed dearness allowance or variable dearness allowance etc., and if it is fixed as a composite wage, how and to what interval this composite wage is required to be revised.

Every organization must frame its own policy keeping in mind the interests of the management, the employees, the consumers, and the community in general. In order to make the wage policy more effective, it should be carefully formulated, must be communicated not only to the managerial staff but also to the workers and their trade unions. It should be examined, evaluated and reviewed periodically to meet the changing needs of the organizations. Increasing emphasis has to be given for rationalization of the wage structure keeping in view the goal of higher productivity in the years to come. Further, a wage policy must be geared to achieving the best prices, the best wages, and the best profits.

Of course, the best prices are not the highest prices, but the prices that stimulate the largest volume of production and lead to the larger volume of sales. The best wages are not the highest wages, but the wages that lead to full employment and the largest possible pay-rolls. The best profits are not the lowest profits, but the profits that encourage most persons to become employers and to provide jobs. Prices, wages, and profits must be thought of together. Only when we have achieved the best balance among them can the economy function at its fullest. If we try to force one of these elements out of relationship to the others, we must reduce production and hurt everybody, and sometimes most of all the very groups we are most eager to help.

Income policy:

A wage policy cannot be conceived in a vacuum, and to be meaningful, it must be dovetailed with a proper income policy and price policy. The income policy generally refers to the composite measures undertaken by the government to regulate earnings, profits and prices, to achieve one or more objectives relating to price stability, balance of payments, fuller employment, faster economic growth and social justice.

The main objects of income policy are to prevent income rising at a higher rate than output, i.e., to fix a target of expansion in income and to secure correspondence between the aggregate income and expenditure in conformity with the flow of goods and services. The income policy is viewed as a tool to ensure better distribution of incomes. It is essentially an instrument to contain the evil effects of inflation on fixed income groups and weaker sections. It constitutes a close adjunct of fiscal and monetary policies and a cure for chronic inflation. By controlling incomes and thereby expenditure particularly on consumption, the income policy tries to maintain balance between aggregate demand and aggregate supply and saves the economy from the danger of too much money chasing less flow of goods. In addition, it tries to inject economic logic and an element of fairness and equity in wage bargaining. Also it restricts freedom in respect of collective bargaining in order to prevent inflationary wage settlements.

Income policy in the Indian context has got the dual task of fixing the wage norm and also price-freeze of wage goods. A system of productivity wage link-up (instead of a price wage link-up) needs to be an essential part of any income policy for India since only such an arrangement seeks to induce increase in productivity as well as higher increase in real wages of workers. Essentially an income policy is meant to arrest cost-push inflation, whereas in India, inflation is of demand-pull type which is the product of large budgetary deficits. In our country, where there is poverty, increasing unemployment, and a steep rise in the prices of essential commodities, an income policy is a crucial instrument in securing a redistribution of increasing prosperity in favor of the weaker and destitute sections of the community. However, if income policy is to succeed, it must be simple, rational, and economically feasible.

4.6. FORMULATION OF WAGE POLICY IN INDIA :

Policy in the Pre-Independence Period :

Before independence, Indian Government's attitude to labour problems was that of least interference. On occasions, it intervened to secure for labour, its fair dues. However, with the upsuring of organized labour movement and its alignment with the nationalist movement, the government began to take a positive interest in labour matters.

The provision of adequate living wage and recognition of the principle of equal remuneration for work of equal value figure prominently among the objectives of the ILO, set forth in the preamble to its constitution. In the Declaration of Philadelphia, the International Labour Conference recognises the solemn obligation of the organisation to further among the nations of the world a programme which will achieve the raising of standard of living, policies in regard to wages and earnings, hours and other conditions of work, calculated to ensure a just share of the fruits of progress to all, and minimum living wage to all employed and in need of such protection.

In 1928, the International Labour Conference adopted a convention urging the creation of a machinery for fixing minimum wages keeping in view a suitable standard of living for workers and related considerations. The enactment of the Trade Disputes Act, 1929 and the appointment of the Royal Commission on Labour in

1929 (Whitely Commission) where two important landmarks in the evolution of labour policy with reference to wages.

The Whitely Commission, for the first time, recommended setting up of a machinery for the fixation of minimum wages, in keeping with certain requirements so as to avoid sweating in Indian industries. It made a significant observation on the subject of minimum wages.

The Second World War imposed unusual burden and pressures on the Indian economy and caused a phenomenal rise in prices. The Fifth Indian Labour Conference (1943) and the Standing Labour Conference (1944) discussed the problem of minimum wage fixation. In order to neutralise the price rise and to sustain the real wages, the government initiated a system of dearness allowance, which has since become an important component of wages in the Indian economy. Since profits rose very high during the war, a system of payment of bonus to workers was initiated and continued for different reasons. In 1946, the government formulated a three-fold wage policy which recommended (a) statutory prescription of minimum wages in sweated industries and occupations and in agriculture; (b) promotion of fair wages agreements; and (c) steps to secure for workers in plantations a living wage.

4.7. WAGE POLICY IN THE POST-INDEPENDENCE PERIOD :

Soon after Independence, the government embarked upon a series of legislative and other measures for the amelioration of the pathetic conditions of the working class. The adjudication machinery, set up during the war, was suitably modified and incorporated in the Industrial Disputes Act, 1947, and since then it has played a significant role in the field of wage fixation. In India, evolution of wage policy started with the Industrial Truce Resolution unanimously adopted in a tripartite conference in December, 1947. The resolution stated the system remuneration to capital as well as labour must be so devised that while in the interest of the consumers and primary producers, excessive profit should be prevented by suitable measures of taxation and otherwise, both will share or product of their common effort after making provision for payment of fair wages of labour, a fair return on capital employed in the industry and reasonable reserves for the maintenance and expansion of the undertaking. The Resolution also recommended the setting up of a suitable machinery for the study and determination of fair wages and conditions of labour.

Subsequently, a number of committees and commissions, wage boards, tribunals, pay commissions were set up. The passing of the Minimum Wages Act, 1948, appointment of the Fair Wages Committee (1948) and the setting up of number of tribunals to settle wage demands of workers in several industries such as cotton textiles, jute and engineering are steps in this direction. Although these did not form a part of unified and well-designed wage policy, they provided evidence of the government's intention to raise the standard of living of the masses. The policy direction was also incorporated in Article 43 of the constitution which lays down that the state shall endeavour to secure by suitable legislation or economic organisation or any other way, to all workers, agricultural, industrial or otherwise, work a living wage, conditions of work, ensuing a decent standard of life and full enjoyment of issues and social and cultural opportunities. The principal of equal pay for equal work for both men & women has also been laid down as one of the Directive Principles of State Policy in Article 39 of the constitution.

4.8. POLICY ENUNCIATED IN THE PLANS :

The advent of the era of planning brought in its wake, a set of new problems as well as popular expectations. The inflationary potential inherent in the process of development called for a close check on the wage price spiral.

The First Five Year Plan (1951-56) contained some significant statements regarding wage movement and its repressions on economic stability of the country. It advocated wage increase for removing anomation or where the existing rates are abnormally low.

The Second Five Year Plan (1956-61) laid great emphasis on the fact that an improvement in wages could only come about as a result of increased productivity, and strongly recommended the system of payment by results. It suggested the setting up of a special wage commission to examine the relevant roles of wages, prices and profit in the economy, keeping in mind the social objective of the plan.

The Third Five Year Plan (1961-66) and the three Annual Plans (1966-68) did not offer anything specific in the area wage policy.

The Fourth Five Year Plan (1969-74) made there useful observations: first, the price stability is basic to wage policy; second, the need for linking wage increase with increases in productivity and third the necessity to extend the system of payment by results by agreement with workers and in the atmosphere of good industrial relations.

The Fifth Five Year Plan (1974-79) stated the reward structure of the industrial employees in terms of wage and non-wage benefits must be related to performance records in industrial enterprises.

The Sixth Five Year Plan (1980-85) trend on a wage policy stating : (i) to narrow down the existing inequalities and to eliminate malpractices in regard to wage rate and wage payment; (ii) to lay down criteria for fixation and revision of minimum wage and to evolve wage structure without impinging on the freedom of the parties to negotiate wage agreements; (iii) to raise the level of minimum wage in such a manner that soon the concept of a need based minimum wage becomes a reality; (iv) to make conscious efforts to remove the marked despairing in wage levels noticed between interstate and interregional, inter-industry occupations and also between the organised and unorganised, urban and rural sectors, (v) to extend the system of productivity linked bonus introduced in railways, posts and telegraph and some departmental undertakings, to other establishments where linkage with the profits is not a possible proposition.

The Seventh Five Year Plan (1985-90) observes that an important aspect of labour policy pertains to the formulation of an appropriate wage policy. Accordingly to the plan, the basic objective of wage policy is a rise in the levels of real incomes in consonance with increases in productivity, promotion of productive employment, improvement in skills, sectoral shifts in desired directions and reduction in disparities.

The Eight Five Year Plan (1992-1997) in its approach to labour welfare has suggested for adequate levels of earnings, safe and humane conditions of work and access to some minimum social security benefits for enhancing quality of life of workers and their productivity.

According to the Ninth Five Year Plan (1997-2002) the planning process attempt to create conditions for improvement in labour productivity and for provision of social security to supplement the operations of the labour market. The resources have been directed through the plan programmes towards skill formation and development, exchange of information on job opportunities, monitory of working conditions creation of industrial harmony and insurance against disease and unemployment for the workers and then families.

There is no uniform wage policy for all sectors of the economy. Wages in the organised sectors are determined through a process of collective bargaining. In the case of central public sector enterprises, the department of public enterprises issues guidelines and permits negotiations for wage revision.

4.9. RECOMMENDATION ON WAGE POLICY :

4.9.1. National Commission on Labour (1969) :

The commission did not go beyond recognising the need for a national wage policy in these words, “The wage policy has to be framed taking into account such factors as the price level which can be sustained, the employment level to be aimed at, requirement of social justice, and capital formation need for growth.”

The NCL has attempted to assess the general wage policy of the government since independence. For this purpose, it gave five indicators. They are : (i) the state of industrial harmony; (ii) changes in workers level of living; (iii) changes in productivity; (iv) impact of wages on prices and (v) share of wages in the value added by manufacture.

4.9.2. Chakraborty Committee (1974) :

Recognising the need for uniformity in wage payments across regions, industries and occupations the committee suggested that a National Wage Commission and a National Wage Board be set up to evaluate all jobs, work out a grade structure based on skill differentials and fix wages for each grade.

4.9.3. Bhoothalingam Study Group (1978) :

This Group opined that the determination of a homogeneous national wage structure is very difficult. Disparities, anomalies and irrationalities exist and have come to be regarded as right. Further, there is no reasonable method of determining what should be the absolute level of wage for each category of workers and what is a right differential between one category of workers and another. Even of a national wage structure is determined which is opposed or the historically determined structure accepted, which is improbable, several adjustment in wages as earnings are required from time to time.

The Study Group on Wages, Incomes and Prices (Bhoothalingam Panel) which submitted its report in 1978, proposed the concept of a national minimum wage, below which the wage of no category of worker will be allowed to fall. The committee has proposed a target of national minimum wage of Rs. 150 per month at 1978 prices, to be achieved in about seven years.

It should be revised every three years in relation to the increase in per capita national income. In arriving at this national minimum wage of Rs.150, the study group has attempted to balance the considerations of economic growth, on the one hand, and social and distributive justice on the other. The committee has underlined the need for a single national corrective formula to compensate for the rise in the cost of essential consumption basket. It recommended that future dearness allowance should be linked to the cost of living on a uniform basis.

4.10 SUMMARY:

The compensation policy in all organizations is a complex and sensitive area of personnel Management since the relative status of workers / employees in the society, their commitment of work and attitude towards productivity etc. are all conditioned by wages or salaries they get. In planning and developing a sound compensation programme, wage and salary administrators keep in view the organisation' guidelines of general policy on compensation. The company wage or compensation policy may seek to assure to a competitive wage or salary or it may seek to provide wages and salaries as an internationally higher than average level. Besides, the Statement of policy on compensation may intend to relate earnings to output or contribution or length of service. Such a policy may also seek to specify relationships with in the wage and salary structure or compensation policy may propose to establish priorities among these and other intentions or it may outline differing intentions for various types and groups of employees.

4.11. KEY WORDS

Wage policy: Wage policy names Legislation or government action calculated to affect the level or structure of wages or both, for the purpose of attaining specific objectives of social and economic policy.

4.12 SELF ASSESSMENT QUESTIONS

1. What is compensation plan and explain its importance in organisation?

2. What is Wage Policy? Discuss its necessity in the organisations?

3. Discuss different issues in Indian wage policy. What are the strengths and weaknesses of this policy?

4. Discuss the developments of Indian wage policy according to the five year plans.

5. Enumerate the various recommendations on wage policy in India.

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LESSON - 5

WAGE DETERMINATION

5.0 OBJECTIVE:

After reading this lesson, the student is able to:

* To know the importance of wage determination.
* To understand the principles of wage determination.
* To identify the considerations and constraints in wage determination.
* To analyse the factors influencing wage determination.

STRUCTURE:

5.1 Introduction

5.2 Meaning

5.3 Importance and Objectives of wage determination

5.4 Principles of Wage Determination

5.5 Basic Considerations and elements of Wage Determination

5.6 Constraints in Wage Determination

5.7 Factors influencing in Wage Determination

5.8 Systems for Wage Determination

5.9 Methods in Compensation/Wage Determination

5.10 Summary

5.11 Keywords

5.12 Self Assessment Questions

5.13 Further Readings

5.1 INTRODUCTION:

Wage/compensation are to design a cost effective pay structure that will attract, motivate and retain competent employees and that will also be viewed as fair by these employees. Apart from meeting legal requirements, organizations have to take care of ever-rising employee expectations and competitive pressures while designing an effective compensation plan. Throughout history, employers have been challenged with attracting, retaining and motivating employees. From the simplest barter systems of centuries past to the current complex incentive formulas of today, the organisational premise has been the same. Provide productivity and results to our enterprise and we will provide you with something of value. In their simplest forms, wage/ compensation and benefits have involved cash or commodities, and that still is true to a large degree today. The employee provides a service and the employer provides cash compensation/wage and/or a benefit of value to the employee. Today most organisations have realised that they must take a much broader look at the factors involved in attraction, retention and motivation. And they must deploy all of the factors – including compensation and benefits – to their strategic advantage. As ‘people’ are essential ingredients in the organisation’s success, it is incumbent upon the organisation to protect this asset / investment. As such, the organisation must pay employees what they are worth or else they may choose to work for another organisation.

5.2 MEANING:

Remuneration is the wage/compensation an employee receives in return for his or her contribution to the organisation. Remuneration occupies an important place in the life of an employee. His or her standard of living, status in the society, motivation, loyalty, and productivity depend upon the remuneration he or she receives. For the employer too, employee remuneration is significant because of its contribution to the cost of production. Besides, many battles (in the form of strikes and lockouts) are fought between the employer and the employees on issues relating to wages or bonus. Employee compensation may be classified into two types – base compensation and supplementary compensation. Base compensation refers to monetary payments to employees in the form of wages and salaries. The term ‘wages’ implies remuneration to workers doing manual work. The term ‘salaries’ is usually defined to mean compensation to office, managerial, technical and professional staff. The distinction, however, is rarely observed in actual practice.

Compensation/Wage Determination means “the fixation of compensation/wage rates through standard or structured procedure i.e.. Wage theories (Historical), wage surveys, job evaluation, legal enactments, policy making, appointment of committees, commissions, collective bargaining and with economical, political, social and psychological influences.

Compensation/wage determination is purely an economic problem it gives rise to various social, political, ethical, behavioural and economic problem. It is extremely essential to have specific consideration of factors which have some relationship to existing wage levels and thus influence wage and salary administration.

Generally large number of factors influences the salary levels in an organisation. But at the same time all the factors need not be considered in each and every organisation. A combination of factors will be considered at the organisation depending upon the capacity, conditions, traditions and beliefs.

Usually, wage determination having some common steps to determine/fix the wage in the organisations as: performing job analysis, wage surveys, analysis of relevant organisational problems forming wage structure, forming rules of compensation/wage administration, explaining these to employees, assigning grades and price to each job and paying the guaranteed wage.

5.3. IMPORTANCE AND OBJECTIVES OF WAGE DETERMINATION

5.3.1. Importance:

Wage/Compensation is an integral part of the management of the organisation. Compensation Management contributes to the overall success of the organisation in several ways. To be effective, the managers must appreciate the value of competitive pay, their human resources, and have an investment view of payroll costs.

Wage/ compensation mean different things to different people; it depends on a person's perspective. From employee's point of view, compensation may be considered as a return for their efforts or a reward for satisfactory or outstanding work. It may indicate the value the employer attaches to their skills and abilities-the return on their investment in education and training. In the case of most of the employees, their pay matters a lot in determining their socio-economic well-being. Wage can influence employee work behaviour and attitudes. It may affect their decision on various matters like 'to be or not to be' with the employer, whether or not to work more productively, or undertake training to be eligible for a higher –paying job. Inequity in pay matters may cause employees to diminish their efforts, to search for greener pastures elsewhere, and to form a union. Thus pay and wage matters have strong potential to influence employees' work behaviour and attitude.

5.3.2. Objectives:

- To establish a fair and equitable remuneration offering similar pay for similar work.
- To attract qualified and competent personnel.
- To retain the present employees by keeping wage levels in tune with competing units.
- To control labour and administrative costs in line with the ability of the organisation to pay.
- To improve motivation and morale of employees and to improve union management relations.
- To project a brand image of the company and to comply with legal needs relating to wages and salaries.

5.4. PRINCIPLES OF WAGE DETERMINATION:

To solve compensation / wage problems, a set of principles are pertaining for wage determination. A clear understanding of the aims of organisation in matters of pay having its own determination principles are as follows:

1) Wage and salary plan should be sufficiently flexible.

2) Job evaluation must be done scientifically.

3) Wage and salary plans must always be consistent with the overall organisations plans and programmes.

4) Wage and salary plans and programmes should be in conformity with the social and economic objectives of the country.

5) Ensure that the organisation's compensation policy is consistent with national/public policy.

6) Adjust wages and salaries to changes in the labour market.

7) Graduate wage and salary rates in accordance with the difficulty and importance of the jobs.

8) Maintain consistency by paying similar jobs to similar rates.

9) Provide for flexibility in compensation programs in response to changed conditions.

10) Provide incentives for development.

11) Protect the owners by seeing that pay is neither too high nor too low in terms of value received.

12) Provide not only fairness but employees conviction of fairness in all compensation programs.

13) Strive for simplicity in pay programs as an aid to employee understanding.

14) Provide all employees with full information on compensation policies and programs of the organisation.

5.5 BASIC CONSIDERATIONS AND ELEMENTS OF WAGE DETERMINATION

5.5.1. Basic Considerations for Wage Determination:

There are several considerations or criteria which help in determining wages in an organisation. These criteria include law of supply and demand, prevailing wages, ability to pay government role, standard and cost of living, productivity, bargaining power and job requirements.

5.5.2. Elements of Wage Determination:

Wage and salary systems should have a relationship with the performance, satisfaction and attainment of goals of individual. Henderson identified the following elements of a wage and salary system:

1. Identifying the available salary opportunities, their costs, estimating the worth of its members, of their salary opportunities and communicating them to employees.
2. Relating salary to needs and goals.
3. Developing quality, quantity and time standards related to work and goals.
4. Determine the efforts necessary to achieve standards.
5. Measuring the actual performance.
6. Comparing the performance with the salary received.
7. Measuring the job satisfaction of the employees.
8. Evaluating the unsatisfied wants and unrealized goals aspirations of the employees.
9. Finding out the dissatisfaction arising from unfulfilled needs and unattained goals.
10. Adjust the wage/salary levels accordingly with a view to enabling the employees to reach unreached goals and fulfil the unfulfilled needs and aspirations.

5.6. CONSTRAINTS IN WAGE DETERMINATION:

Constraints in wage determination can be classified as statutory and non-statutory, economic and technical.

i) The Statutory Constraints:

The Minimum Wages Act 1948, the Payment of Wages Act 1936, Equal Remuneration Act 1976, and the Payment of Bonus Act 1965, Adjudication, Tribunals and judgements are statutory constraints of wage determination.

ii) Non-statutory Constraints:

Non-statutory constraints exist varied from industry wide arrangements of wages standardisation at national level which lead to mass-scale governmental intervention. Those are wage boards, pay commissions, committee's recommendations, and collective bargaining operating in a democratic industrial society.

iii) Economic Constraints:

Inflation forms an economic constraint in the determination of wages in an enterprise. It causes divergence between the money or nominal wages of the worker and their real wages or the purchasing power of the money earned.

iv) Technological Constraints:

Technology forms a major constraint in the process of wage determination of an enterprise.

5.7. FACTORS INFLUENCING WAGE DETERMINATION:

On the basis of above discussions, we may summarise the factors affecting wage determination as under:

a) Demand and supply of labour:

Demand and supply conditions of labour have considerable influence on the determination of wage rates, like the price of a commodity is determined by the demand and supply of that commodity. The wage rates to the workers are also influenced by the demand and supply position of labourers in the labour market. If the labour is in short supply, and the demand for labour is more, the workers will offer their services only if they are paid well. On the other hand labour may be available at cheaper rates if their supply is in plenty and the demand for labour is comparatively less.

b) Firm's Capacity to Pay:

One of the principal considerations that weights with the management in fixing the wage rates is its capacity to pay. While fixing wage rates the firm must consider the capacity to pay, because if it pays beyond capacity it no longer survive for a longer period, it may lead to closure after some time.

When capacity to pay of an organisation is a part of profitability, various expenses that the industry bears, certain trends in prices of products/services that are to be charged by the industry should also be taken into account. In addition total cost of employees (salaries, allowances, cost of fringe benefits etc.) should be taken into consideration in determining the ability to pay.

Trade unions demand higher wages when the company's financial position is sound. But they may not accept wage reduction, when the company's financial position is in doldrums. Hence the management has to take decision judiciously. Further, certain incentives are linked to the profitability. Thus, whatever the influence of other factors may be, the organisation cannot pay more than its ability to pay in the long run.

c) Prevailing Wage Rates:

Prevailing rates of remuneration in comparable industries constituted an important factor in determining wage rates. The organisation in long run, must may at least equal to the prevailing rates for similar jobs in similar organisation. Further, the wage and salary rates for the similar jobs in the firms located in the same geographical region also influence the wage determination. The organisation has to pay wages equal to that paid for similar jobs in comparable industries in order to secure and retain the competent employees.

d) Cost of Living:

The cost of living is another important factor that influences the quantum of wage or salary. The employees expect that their purchasing power be maintained at least at the same level, if not increased by adjusting wages to changes in the cost of living. Progressive employers take into consideration the cost of living for their employees and try to fix their wages as to ensure at least the same standard of living as before. Where the employers do not show awareness, labour unions come out with a demand of wage adjustment according to the cost of living index number.

In recent years, in advanced countries, "numbers of labour agreements have 'escalator' clauses, providing for automatic wage and salary increase as cost of living index raises". However in some of the Asian countries the "Dearness Allowance" is an allowance granted to the employees with a view to combination the slaughts of so arising prices.

e) Labour Productivity:

An interesting development in wage determination has been the productivity standard. This is based on the fact that productivity increase is also the result of employee satisfaction and contribution to the organisation. But wage, productivity linkage does not appear to be so easy since many problems crop up in respect of the concept and measurement of productivity. Although, the wages are not linked directly to the productivity, in an organisation, changes in productivity have their impact on remuneration. These criteria received consideration of wage boards, not only, because it constituted a factor in the fixation of 'fair wage' but also because it is directly related to such question as desirability of extending the system of 'payment by result'.

f) Bargaining Power:

Wage also depends to a considerable extent on the relative bargaining power of labour/trade unions and employers. The stronger and more powerful trade unions bargain the higher wages. Their bargaining power is often measured in terms of their membership, the financial strength and the nature of leadership. Arther, M. Ross, concluded that 'real hourly earnings have advanced more sharply in highly organised collective bargaining strategies, political tactics and by organising strikes etc. Trade unions influence may be on the grounds that wages in comparable industries, firm's financial position, rising living cost, government regulations etc. Where the wage level is below that of other comparable industries.

g) Importance of the Industry in the Economy:

Wages are also influenced by the importance of the industry in the economy/country. For e.g. if we take the industries like Petroleum, Engineering, Ports and Docks, the wages are high because the profits are high and the bargaining power of unions is also high. The wages of the workers in these industries will be high when compared to the wages of workers in industries like jute, cotton textiles, and sugar etc.

h) Government Role:

Since the bargaining power of the workers has not ensured fair wages in all industries, the government has to interfere in regulating wage rates to guarantee minimum wage rates in order to cover the essentials in modern civilised society. The role of the government in this regard can be categorised into two; one is legislative and other in non-legislative.

Enactment of different legislations like Minimum Wages Act 1948, Payment of Wages Act 1936, Equal Remuneration Act 1976, and the Payment of Bonus Act 1965, are intended to protect the wages of employees.

The overall objectives of the above said legislations are well summarised as follows:

i) to abolish malpractices and abuses in wage payment,

ii) to set minimum wages for workers, whose bargaining position is weak because they are either unorganised or inefficiently organised.

The non-legislative body of the government in influencing wage rates is in the form of wage boards, pay commissions, recommendations of committees, and adjudication.

i) Good will of the Organisation:

A few organisations want to establish themselves as good employer in the society. For building such reputation, they fix higher wages for their workers. For E.g. ONGC, NTPC, BHEL, Ingresal-Rand, Wedia India Ltd., TELCO etc.

j) Job Requirements:

If a job requires higher skills, effort, greater responsibility and risk, the job holder will naturally get higher wages. Generally, the more difficult the job paid higher the wages.

k) Socio-Psychological Factors:

These factors determine to a great extent the importance of the job or the individual to the organisation. They also determine how hard an individual will work for the compensation received or what pressure he will exert to get his compensation increased. Whether the wage is adequate and equitable depends not only upon the amount that is paid but also the perceptions and the views of the recipients of the wage.

5.8 SYSTEMS OF WAGE DETERMINATION:

The following are the systems of wage determination evolved for effectiveness o f organisations:

i) The wages are determined based on clear definition of values / worth of all jobs in relation to each other within the company.

ii) Ensure fair and suitable earnings to the employees.

iii) Optimise the earning capacity of the employees.

iv) Provide employees, a share in the gains of productivity and follow the principles of internal and external consistency for wage determination.

5.9 COMPENSATION/WAGE DETERMINANT METHODS:

There are two widely practised methods for determining the compensation (i)Salary/wage surveys, and (ii) Job evaluation (iii) group similar jobs into pay grades (iv) Price each pay grade by using wage curves (v) Fine tune pay rates.

(i) Wage/Salary Surveys:

Wage/salary surveys are quick and less expensive way to determine compensation. It could be used to conduct a survey of what is being paid in similar industries for similar positions. This could be done two levels - organisational and professional consultant levels. As far as organisational level is concerned, the HRM department itself can undertake a study to find out comparable compensation packages in similar industries.

(ii) Job Evaluation:

Job evaluation is a technique to establish the relationship between contribution of an employee and compensation for this contribution. Although in reality it is very difficult to get a precise value of the contribution of an employee because of the large number of factors involved in the performance of a job. Job evaluation is the most suitable mechanism to the wage determination.

(iii) Group Similar Jobs into Pay Grades

Similar jobs (in terms of their ranking or number points as ascertained by the job evaluation committee) are grouped into grades for pay purposes. The organisation can now focus on, say 10 to 12 pay grades, instead of hundreds of pay rates. A pay grade consists of jobs of approximately equal difficulty or importance as determined by job evaluation. If the point method is used, the pay grade consists of jobs falling within a range of points. Ten to sixteen grades per job cluster (factory jobs, clerical jobs) is common.

(iv) Price each Pay Grade – Wage Curves

Pay rates are assigned to pay grades through a wage curve. The wage curve shows graphically the pay rates currently paid for jobs in each pay grade relative to the points or rankings given to each job or grade. A complete wage curve tells management the average relationship between the pay grade points and wage rates. It will show which pay is out of the trend line. If a job's pay rate is very high – where the current rates paid by the company fall well above or below the wage line – those wage rates are identified as 'red circles' rates. This only means that pay is frozen or below average increases are granted until the structure is adjusted upward to place the circled rate within a normal range.

(v) Fine Tune Pay Rates and Determine Wage Structure

The employees fix a pay range for each grade (Grade I, II and III, etc.,). The wage structure of a company is nothing but a pay scale showing ranges of pay within each grade.

5.10. SUMMARY:

Wage determination is one of the important areas of compensation management. A large number of factors are influencing in wage determination. Significant among them are, capacity of the employer to pay, i.e., the wages payable must be within the firm's ability to pay. The remuneration in comparable industries shall also be considered because if we pay wages unilaterally the wages may be either too low or too high, both are problems. Like the prices of a commodity are determined by the demand and supply of the commodity, here the wages are also determined by the demand and supply of labour. Government role in wage determination is in two ways, legislatively and non-legislatively. Whatever may be the factors which influence the wage determination, finally, the wages would be settled by agreements between the management and unions. So collective bargaining is one of the most important in wage determination. The other significant factors that influences wage determination process are; cost of living, labour productivity, importance of industry in the economy, good will of the organisation, job requirements and socio-psychological factors.

5.11 KEYWORDS:

Wage Determination: Wage determination is fixing the wage/salary rates with a systematic procedure.
Capacity to pay: Management foxing the wages based on organisation's ability or capacity.

Collective Bargaining: The negotiations between employees and employer are known as collective bargaining.

Cost of Living: Cost of living means expenditures of normal employee in the modern society. That can be measured with consumer price index.

5.12 SELF ASSESSMENT QUESTIONS:

1.Define wage determination, explain its principles.

2. What are principles of wage determination? Discuss its considerations.

3. Various factors influence the wage determination, briefly discuss some important factors

4. In the globalisation, every organisation shall follow the factors to fix their organisation's compensation/wage rates, discuss.

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LESSON - 6

JOB EVALUATION

6.0 OBJECTIVE:

After reading this lesson, the student is able to:

- Know the concept of Job Evaluation
- Analyse the role of Job Evaluation in Wage Determination
- Understand the Characteristics, objectives and steps in Job Evaluation
- Comprehended the Techniques/Methods of Job Evaluation.

STRUCTURE:

6.1 Introduction

6.2 Meaning and Concept of Job Evaluation

6.3 Role of Job Evaluation in Wage Determination

6.4 Characteristics and Purpose of Job Evaluation

6.5 Objectives and Principles of Job Evaluation

6.6 Procedure/ Steps in Job Evaluation

6.7 Techniques / Methods of Job Evaluation

6.8 Advantages and Problems of Job Evaluation

6.9 Establishing the Pay Structure

6.10 Merit Rating

6.11 Summary

6.12 Keywords

6.13 Self Assessment Questions

6.14] Further Readings

6.1 INTRODUCTION:

Job evaluation is a systematic method of appraising the value of each job in relation to other jobs in the organisation. It provides a consistent procedure that sets up and maintains a hierarchy of jobs, attaching to each job a pay rate commensurate with status in the hierarchy

Job evaluation is a method used to describe, analyse, compare and evaluate jobs within a unit, or an industry on the basis of the work content and the job requirements in order to place them under particular wage or salary grades.

Job Evaluation is a technique of job analysis, assessment and comparison in order to determine the demands of the job, such as the experience and the responsibility required for carrying out the job effectively. It is a dynamic tool for rationale comparison of the relative worth of jobs in an organisation essentially for purpose of establishing compensation systems.

6.2 MEANING AND CONCEPT OF JOB EVALUATION:

Job evaluation as a part of compensation system relates to the systematic procedure for creating a wage structure with a view to determining a proper value relationship between several productions or clerical jobs in an enterprise to attract motivate and maintain effective human resources by adequately compensating them for work performed.

The International Labour organisation (ILO) defined job evaluation as an "attempt to determine and compare demands which the normal performance of a particular job makes on normal workers without taking into account the individual abilities or performance of the workers concerned".

Windell L.French defined job evaluation as "a process of determining the relative worth of the various jobs within the organisation, So that differential wages may be paid to jobs of different worth".

British Institute of Management (1970) defined job evaluation as "the process of analysing and assessing the content of jobs, in order to place them in an acceptable rank order which can be used as a basis for a remuneration system. Job evaluation, therefore, is simply a techniques designed to assist in the development of new pay structures by defining relatives between jobs on a consistent and systematic basis".

Thus job evaluation may be defined as a process of determining the relative worth of jobs, ranking and grading them by comparing the duties, responsibilities, requirements like skills, knowledge of a job with other jobs with a view to fix compensation payable to the concerned job holder.

6.3 ROLE OF JOB EVALUATION IN WAGE DETERMINATION:

Job evaluation is the cornerstone of a formal wage and salary and compensation administration. Specifically the job evaluation process plays a key role in compensation management in the following ways:

1. It is the most effective means of determining internal pay relationships.
2. It can be used as an instrument for affecting the company's basic pay policies.
3. Equitable base-pay relationships set by job evaluation serve as a foundation for incentive of bonus plans or merit increase programmes.
4. Job evaluation provides a reasonable basis for personnel moves like transfer, promotion, or demotion.
5. Useful controls over wage and salary costs can be greatly aided by job evaluation.
6. Job evaluation provides a foundation for gearing company pay scales to the wages paid by competing companies.
7. Job evaluation assists management in meeting day-to-day problems. This is turn contributes to the reduction of employee grievances, improves employee productivity through higher morale, and helps to reduce turnover.

6.4 CHARACTERISTICS AND PURPOSE OF JOB EVALUATION:

6.4.1 CHARACTERISTICS OF JOB EVALUATION

1. Job evaluation is a method with a systematic approach
2. It is an attempt to determine the requirements of the work involved for any incumbent.
3. It is a process by which jobs in an organisation are appraised.
4. It is a process of analysing and describing positions, grouping them, and determining their relative value by comparing the duties of different positions in terms of their different responsibilities and other requirements.
5. It is a system to deal exclusively with assessment of the job and not concerned with employees assigned to the job.

6.4.2 PURPOSE OF JOB EVALUATION:

1. Job evaluation can provide a more workable internal wage structure.
2. Job evaluation fixes wage rates for new or changed jobs
3. Job evaluation reduces the grievances over wage and salary rates.
4. Job evaluation can provide incentive values to employees
5. Job evaluation provide the facts for wage negotiations

6. Provide the facts on job relationships for use in selection, training, transfers and promotions.

6.5 OBJECTIVES AND PRINCIPLES OF JOB EVALUATION:

6.5.1. OBJECTIVES OF JOB EVALUATION

The following objectives are derived from the analysis of the above mentioned definitions.

(i) To establish an orderly, rational, systematic structure of jobs based on their worth to the organization.

(ii) To justify an existing pay rate structure or to develop one that provides for internal equity.

(iii) To assist in setting pay rates that are comparable to those of in similar jobs in other organizations to compete in market place for best talent.

(iv) To provide a rational basis for negotiating pay rates when bargaining collectively with a recognized union.

(v) To ensure the fair and equitable compensation of employees in relation to their duties.

(vi) To ensure equity in pay for jobs of similar skill, effort, responsibility and working conditions by using a system that consistently and accurately assesses differences in relative value among jobs and

(vii) To establish a framework of procedures to determine the grade levels and the consequent salary range for new jobs or jobs which have evolved and changed.

(viii) To identify a ladder of progression for future movement to all employees interested in improving their compensation.

(ix) To comply with equal pay legislation and regulations determining pay differences according to job content.

(x) To develop a base for merit or pay-for-performance.

(xi) To gather data and information relating to job description, job specification and employee specification of various jobs in an organisation.

(xii) To compare the duties responsibilities and demands of a job with that of other jobs.

(xiii) To determine the ranks or grades of various jobs.

(xiv) To minimise wage discrimination based on sex, age, caste, religion, region etc.

6.5.2. PRINCIPLES OF JOB EVALUATION:

Job evaluation is not truly a scientific process as there is no way of scientifically measuring jobs. It is rather a process of judgement. The 'correctness' of the results it provides can only be assessed in terms of their acceptability to the vast majority of personnel to whom it applies.

Since job evaluation is a process of finding out the relative worth of a job as compared to other jobs, it is based on the following principles:

i) Rate the job but not employee. Rate the elements on the basis of job demands.

ii) The elements selected for rating should be easily understood

iii) The elements should be defined clearly and properly selected.

iv) Employees concerned and the supervisors should be educated and convinced about the programme.

v) Supervisors should be encouraged to participating in rating the jobs.

vi) Secure employee co-operation by encouraging them to participate in the rating programme.

vii) Discuss with the supervisors and employees about rating but not about assigning money values to the points.

viii) Do not establish too many occupational wages.

6.6. PROCEDURE/STEPS IN JOB EVALUATION:

National Institute of Personnel Management has evolved the following steps for evaluating jobs.

i) Analyse and prepare job description:

Job evaluation is the outcome of job analysis. Job analysis provides information necessary for appraising jobs like skills, knowledge, abilities and aptitudes.

ii) Select and prepare job evaluation plan:

Job should be divided into detailed tasks and positions. It also includes selection factors, elements needed for the performance of the jobs, determining the money value of each factor and element and writing instructions for evaluation.

iii) Evaluation and Classification of jobs:

Classify the jobs in a sequential order based on their significance and contribution to the organisation. This includes assigning money values to each class.

iv) Install the Job evaluation programme:

Educate the employees, with their confidence and then put the programme into operation.

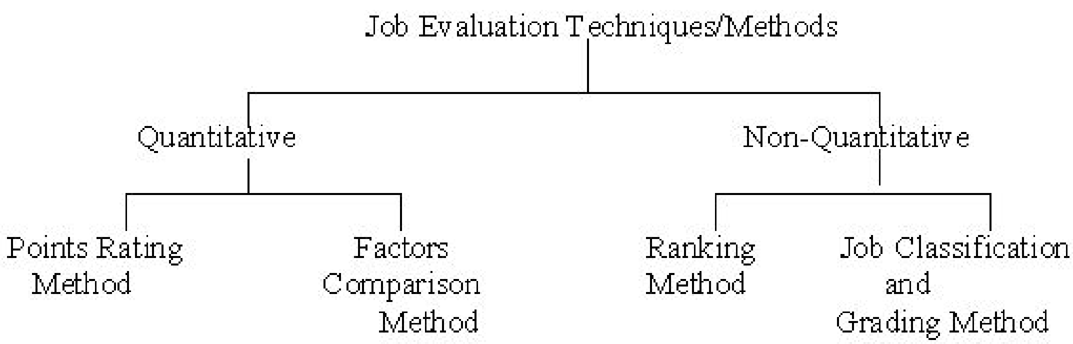
v) Maintain the job evaluation programme:

This step involves updating the job evaluation programme, bring modifications based on the changes in the conditions and situations. Make sure from time to time that programme runs smoothly and perfectly.

6.7 TECHNIQUES/METHODS OF JOB EVALUATION:

Jobs are evaluated on the basis of various techniques. These techniques are grouped into two classes, viz., 'quantitative and non-quantitative' techniques. Non-quantitative techniques include ranking, (simple ranking and paired comparison ranking), job classification and grading methods. Quantitative techniques include points rating and factor comparison methods (see fig. 6.1).

Figure. 6.1



6.7.1 NON-QUANTITATIVE TECHNIQUES OR METHODS:

Conventionally, non-quantitative, simple and crude techniques were developed. They are ranking and job classification methods.

(i) Ranking Method:

This is a simplest method of job evaluation, in this method four stages or steps are there.

(a) Simple Ranking: This is the simplest and administratively the easiest technique. The evaluator compares one job with other jobs based on duties, responsibilities and demands made by the jobs on the incumbent and the degree of importance of the job to the organisation and rank all the jobs from the most important to the least important. The evaluator has to appraise and rank the jobs but not the job incumbents.

(b) Ranking the Key jobs: Ranking all the jobs at a stretch under simple ranking methods is difficult. The evaluator, in order to minimise this problem, has to identify the key or representative jobs at the first stage, rank the key jobs at the second stage, identify and rank all other jobs at the third stage.

(c) Paired Comparison: In this method the evaluator ranks each job in turn against all other jobs to be appraised, so that a series of paired rankings is produced. This method is more comprehensive, logical and reliable compared to the simple ranking method.

(d) Single Factor Ranking Method: 'Goldenberg' has suggested a single factor ranking scheme. The single factor considered is the discretionary contents present in each job related to other jobs. The single most important task to be performed in a job is identified and compared with the single most important task to be performed in other jobs. Thus, pure ranking does not cover these refinements.

The jobs are to be priced after they are ranked. In other words, money value should be assigned to each job. Key jobs with known monetary values will be used as the basis to determine the money value of jobs. Generally, there is agreement about the rates of key jobs.

Advantages:

(i) This method is the simplest, quickest and least costly from the viewpoint of time and money, (ii) This method is most appropriate in small organisations, (iii) It is also appropriate for ranking the top managerial personnel in large organisations and (iv) It is useful as a first and basic step of job evaluation.

Disadvantages:

(i) This method provides no yardstick for measuring the relative worth of one job against the other, (ii) Job requirements, job specifications and employee specifications are not considered in evaluation, (iii) It does not indicate the extent or degree to which one job is worthy than the other and (iv) It is not a comprehensive and systematic technique.

(ii) Job Classification and Grading Method:

Class and grade are used differently in this method. A grade is a group of different jobs of similar difficulty or requiring similar knowledge and skill to perform. A class is a subdivision of a given occupation. For example, Class I Clerk, Class II Clerk, Class III Clerk, Class IV Clerk and Class V Clerk. The jobs within a class have fairly similar tasks to be performed whilst the jobs within a grade may be different as far as tasks are concerned. However, classes and grades are designed for the similar jobs and thus receive similar pay.

Under this method, jobs at different levels in the organisational hierarchy are divided into various grades with a clear cut definition of each grade. Grades are formulated on the basis of nature of tasks, requirements of skill, knowledge, responsibilities and authority of various jobs. There are several steps in the mechanism of this method. The important among them are:

(i) Determine the shape and size of organisational structure, i.e. tall or flat organisation, geographical or functional organisation etc.

(ii) Preparation of job descriptions,

(iii) Preparation of grade descriptions based on various components.

(iv) Establishment of a number of job grades and division of the organisation into various grades like Grade-I, Grade-II . . . Grade-VI.

(v) Discussion and negotiation with trade union representatives regarding the number of grades, grade descriptions.

(vi) Selection of key jobs and grading them.

(vii) Grading the entire jobs.

(viii) Classifying the jobs of each grade and

(ix) Assigning the money value to the key grades first and then to all other grades.

Advantages:

(i) It is simple and easy to understand and operate, (ii) It provides an opportunity for a systematic organisation structure, (iii) Pay grades are better and appropriate for comparison with those of other organisations. (iv) It is more elaborate than ranking method.

Limitations :

(i) It sometimes seems to be arbitrary though it takes the view of the representation of the trade unions. (ii) Writing grade descriptions is not easy in this method. However, classification and gradation represent a link in the historical development of job evaluation between ranking and points system.

6.7.2 QUANTITATIVE TECHNIQUES OR METHODS:

These are two methods under conventional quantitative techniques, viz., points rating and factor comparison system.

(i) Points Rating Method :

This method was introduced by Merrill R. Lott . This was one of the earliest approaches for evaluating jobs based on quantitative values. This method is analytical in the sense that jobs are broken into components for purposes of comparison. This method is quantitative as each component of the job is assigned a numerical value. Thus, characteristics of factors considered to have a bearing on all jobs in the programme like skill, knowledge, responsibility, working conditions etc., are selected under this method. Each factor is divided into degrees or levels and point value is assigned to each level. The total of point values assigned to each factor given the total point values for each job which can be compared.

This method of job evaluation should be developed systematically and applied methodically in order to avoid the anomalies. The important steps in the process of developing this technique are:

(i) Constituting a representative committee of members from various departments for job evaluation.

(ii) Selecting a sample of jobs and preparing job descriptions, job specifications and employee specifications.

(iii) Selecting and defining those factors which are related to all jobs and are considered to be most critical in determining the relative degrees of difficulty and responsibility between jobs.

(a) **Skill:** Education, Training, judgement, analysis, mental complexity, mental dexterity, adaptability etc.

(b) **Effort:** Physical demand, visuals effort, concentration, mental effort, alertness etc.

(c) **Responsibility:** For preventing monetary loss, machines, materials, safety, policy etc.

(d) **Job Conditions:** Working conditions, hazards etc.

(iv) Determining the weight of each factor according to its relative importance.

(v) Defining each factor, specifying the scope and elements of each factor.

(vi) Dividing each factor into levels and defining each level.

(vii) Determining relative value of each level within factors. Factors can be divided into point values by arithmetic of geometric or geometric progression.

(viii) **Testing the mechanism:** Get the total points for a few sample jobs and compare them with the results obtained through other methods. Proceed further, if the system produces acceptable results.

(ix) Appraise all the jobs and arrive at a composite numerical value for each job.

(x) Price the points in order to arrive at the wage structure with the help of organisational hierarchy of jobs and salary policy.

Advantages :

(i) Almost the same pay scale can be arrived at for the same jobs because agreement among rates on the same is very close.

(ii) Definitions are written in applicable terms to the jobs.

(iii) Assigning monetary values is very easy.

(iv) Prejudice, bias and error of human judgement are minimised in this technique.

(v) Once the score is assigned to a particular job, it is long standing.

(vi) Wage differentials would be systematic and according to the content of the job under this method.

Disadvantages:

(i) It is difficult to determine factor levels and assign point values.

(ii) It would be somewhat difficult to explain the mechanism and operation of this method to employees, supervisors and trade union leaders.

(iii) Operation of this method involves heavy expenditure, spending of much time and clerical work.

(ii) The Point Factor or Factor Comparison Method

This method is based both on the principles of points rating and principle of ranking. This method is analytical as jobs are broken into sub-factors and components. Under this method, first the components and sub-factors are ranked under various factors headings. The next step is assigning the monetary values to the components or sub-factors of each job. Thus, each job is ranked a number of times (i.e., number of compensable components of sub-factors).

The mechanism or modus operandi of this method involves the following steps:

(i) Developing job descriptions, job specifications of job requirements covering physical requirements covering physical requirements, skill requirements, training and experience, responsibility and authority, working conditions etc.

(ii) Selecting a number of key jobs: This step is more critical and useful from the point of final evaluation as the other jobs are assigned monetary values based on the fixed wage rates arrived for the key jobs on the basis of negotiations, A key job must be clearly divisible into sub-factors and components. This step also involves dividing the job into sub-factors and components.

(iii) Ranking key jobs**:** The sub-factors of each key job must be given relative ranks based on their individual contribution to the total job.

(iv) The fourth step involves valuing the sub-factors of each of the key jobs. This steps is known as factor evaluation. Money worth of each sub-factors of the key jobs is ascertained in order to known the royal money value (or salary) of each or the key jobs.

(v) The fifth step integrating the monetary value of sub-factors arrived though factor evaluation with those of ranking of factors . It is to find out whether the difference among factors as per the ranking and factor evaluation is one and the same or not.

(vi) The sixth step is comparing all the jobs (factor by factor) of the same grade or level with related key job and establishing monetary value to the sub-factor of various jobs based on the monetary value of sub-factors of key jobs. There are certain advantages to this technique over others.

Advantages:

(i) It is analytical and quantitative method.

(ii) This method is a combination of two techniques, i.e., ranking and factor comparison.

(iii) Since the modus operandi of this system is relatively easy to understand, it can be operated and explained to supervisors, employees and trade union leaders.

(iv) This technique is more reliable and valid compared to other techniques as each is compared with all other jobs from respects, i.e., factor rank order comparison.

(v) This technique assigns money value more or less fairly and objectively as there is cross checking of money value with rank order.

Disadvantages

(i) It is costly and difficult to operate compared to the conventional non-quantitative techniques.

(ii) Factors evaluation in this method is not that much objective as that of point rating technique.

(iii) This technique does not consider all the sub-factors as the operation of the system.

6.8 ADVANTAGES AND PROBLEMS OF JOB EVALUATION:

6.8.1 ADVANTAGES OF JOB EVALUATION

Job evaluation is a process of determining the relative worth of a job. It is a process which is helpful even for framing compensation plans by the personnel manager. Job evaluation as a process is advantageous to a company in many ways:

1. **Reduction in inequalities in salary structure -** It is found that people and their motivation is dependent upon how well they are being paid. Therefore the main objective of job evaluation is to have external and internal consistency in salary structure so that inequalities in salaries are reduced.

2. **Specialization -** Because of division of labour and thereby specialization, a large number of enterprises have got hundred jobs and many employees to perform them. Therefore, an attempt should be made to define a job and thereby fix salaries for it. This is possible only through job evaluation.

3. **Helps in selection of employees -** The job evaluation information can be helpful at the time of selection of candidates. The factors that are determined for job evaluation can be taken into account while selecting the employees.

4. **Harmonious relationship between employees and manager -** Through job evaluation, harmonious and congenial relations can be maintained between employees and management, so that all kinds of salaries controversies can be minimized.

5. **Standardization -** The process of determining the salary differentials for different jobs become standardized through job evaluation. This helps in bringing uniformity into salary structure.

6. **Relevance of new jobs -** Through job evaluation, one can understand the relative value of new jobs in a concern.

7. It is logical and to a certain extent an objective method of ranking and grading the jobs.

8. It helps to fit the newly created jobs in the existing structure.

9. Employee grievances, doubts and complaints would be at the lower ebb as it is a systematic and objective method of wage fixation.

10. It eliminates some undesirable factors like capacities of employee and employers, fluctuations in market rates etc.

11. It satisfies the principles of fair wage, wage equity, uniformity in wages etc.

12. It helps to redesign the jobs for minimising wide wage differentials.

13. It ensures employee satisfaction about wage level and wage equity.

14. It also helps to redesign the jobs by reallocating the easy and difficult tasks equally among various jobs.

6.8.2 PROBLEMS OF JOB EVALUATION

Though there are certain advantages of job evaluation, it suffers from some problems. They are:

i. Job evaluations are not exactly scientific.

ii. Modus operandi of most of the techniques is difficult to understand even to the supervisors.

iii. The factor taken by the programme is not exhaustive.

iv. There may be wide fluctuations in compensable factor in view of changes in technology, values and aspirations of employers etc.

v. Employees, trade union leaders, management and the programme operators may perceive differently in selecting the compensable factors, in giving weightages or degrees etc.

vi. The results of job evaluation may not exactly coincide with social evaluations which in turn result in employee dissatisfaction.

vii. Job evaluation is only one among several factors in determining the wage level. Sometimes, other factors like government policy may dominate the job evaluation.

viii. Job of equal contact or grade may not attract the workers equally.

ix. Job evaluation programme once structured may not be useful for the next time. Despite these limitations or problems, job evaluations is the most appropriate technique for fixing and revising the wages as it is a systematic and objective method of wage fixation.

6.9 ESTABLISHING PAY STRUCTURE:

Once the job evaluation is complete, its data become the nuclear for the development of the organisations pay structure. This means establishing pay rates or ranges that are compatible with the ranks, classifications, or points arrived through job evaluation.

(i) Wage/Salary Surveys:

Wage/salary surveys are quick and less expensive way to determine compensation. It could be used to conduct a survey of what is being paid in similar industries for similar positions. This could be done two levels - organisational and professional consultant levels. As far as organisational level is concerned, the HRM department itself can undertake a study to find out comparable compensation packages in similar industries.

(ii) Job Evaluation:

Job evaluation is a technique to establish the relationship between contribution of an employee and compensation for this contribution. Although in reality it is very difficult to get a precise value of the contribution of an employee because of the large number of factors involved in the performance of a job. Job evaluation is the most suitable mechanism to the wage determination.

(iii) Group Similar Jobs into Pay Grades

Similar jobs (in terms of their ranking or number points as ascertained by the job evaluation committee) are grouped into grades for pay purposes. The organisation can now focus on, say 10 to 12 pay grades, instead of hundreds of pay rates. A pay grade consists of jobs of approximately equal difficulty or importance as determined by job evaluation. If the point method is used, the pay grade consists of jobs falling within a range of points. Ten to sixteen grades per job cluster (factory jobs, clerical jobs) is common.

(iv) Price each Pay Grade – Wage Curves

Pay rates are assigned to pay grades through a wage curve. The wage curve shows graphically the pay rates currently paid for jobs in each pay grade relative to the points or rankings given to each job or grade. A complete wage curve tells management the average relationship between the pay grade points and wage rates. It will show which pay is out of the trend line. If a job's pay rate is very high – where the current rates paid by the company fall well above or below the wage line – those wage rates are identified as 'red circles' rates. This only means that pay is frozen or below average increases are granted until the structure is adjusted upward to place the circled rate within a normal range.

(v) Fine Tune Pay Rates and Determine Wage Structure

The employees fix a pay range for each grade (Grade I, II and III, etc.,). The wage structure of a company is nothing but a pay scale showing ranges of pay within each grade.

6.10 MERIT RATING:

James Lundy defines merit ratings as "the process of evaluating an employee's performance on the job" Merit rating is concerned with employee appraisal. It is a systematic and impartial procedure for determining the excellence with which an individual is performing a job.

Kimball and Kimball define merit rating as "the evaluation of any given worker as to his fitness for given terms of assigned factors by which he may be intelligently appraised."

Objectives of Merit Rating:

i. to furnish a periodic record of the relative value of each employee as judged by his superiors.

ii. to determine and justify wage differentials existing for the same job.

iii. to provide more accurate information for the purpose of promotions, transfers and demotions.

iv. to provide a means of evaluating the selection and training techniques.

v. to ensure congenial superior-subordinate relationship.

Job evaluation and merit rating are not one and the same. These two are different. The differences between job evaluation and merit rating are presented in exhibit 6.1.

Exhibit 6.1

DIFFERENCES BETWEEN JOB EVALUATION AND MERIT RATING

	Job Evaluation	*Merit Rating*
1.	Job evaluation is determining the relative worth of jobs,	Merit rating is appraising/ evaluating the employee against the job description.
2.	Job evaluation is the basis for designing a satisfactory wage structure,	Merit rating is used for determining promotions/transfers.
3.	Job evaluation explains the relative wage rates of the jobs,	Merit rating provides guidelines to employees for better performance/ Promotions.

6.11. SUMMARY:

Job evaluation is a systematic attempt which provides a basis of comparing jobs and determines the relevant worth of different jobs in an organisation. It has two basic objectives: (1) to compare jobs and determine their level within each occupational group; and (2) to compare jobs between occupational groups. Achieving the first objectives is important for promotions, career planning and personnel development. Achieving the second objective is of interest because of wage comparisons. Job evaluation attempts to achieve both objectives by determining the rank order of all the jobs. It is thus a systematic and orderly process of determining the value of each job in relation to other jobs in the organisation. It is the job that is be rated and not the man. It is an important tool of personnel administration and has an important role to play in wage decisions. It provides a systematic framework which may serve as the basis for wage determination, but does not entirely solve the problem.

6.12 KEY WORDS:

Job Analysis: It is the process of a study and collection of information relating to the operations and responsibilities of a specific job.

Job Evaluation: It is the process of determining relative worth of jobs.

6.13 SELF ASSESSMENT QUESTIONS:

1. What is job evaluation? Explain the objective of job evaluation. How do you prepare the ground for evaluating jobs?

2. What are the conventional and non-conventional techniques of job evaluation? What type of technique do you adopt to evaluate the jobs of an Engineer (Maintenance), Engineer (Operations), Engineer (Marketing), and Chief Engineer in a large Machine Tools Industry?

3. What are the quantitative and non-quantitative techniques of job evaluation? Which type of techniques do you adopt to evaluate jobs of an officer (Ag Officer (Small Scale Industry), Economic Officer and General Officer in a large Commercial Bank.

4. "Job evaluation does not usually price jobs" Discuss.

5. Explain the advantages and limitations of job evaluation as a basis for fixing and revising wages and salaries.

6. Explain different techniques of job evaluation. What are the advantages and disadvantages of each technique?

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LESSON - 7

WAGE DIFFERENTIALS

7.0 OBJECTIVE:

After reading this lesson, the student is able to :

- Know why the Wage Differentials in an Industry.
- Study various factors influence the Wage Differentials.
- Study the different types of Wage Differentials.
- Understand Recommendations or Opinions of various Committees in India.

STRUCTURE:

7.1 Introduction

7.2 Importance of Wage Differentials

7.3 Reasons causing Wage Differentials

7.4 Types of Wage Differentials

7.5 Geographical Wage differentials in India

7.6 Desirability of Wage Differentials

7.7 Wage Differentials in India

7.8 Public Sector vs. Private Sector

7.9 Summary

7.10 Keywords

7.11 Self Assessment Questions

7.12 Further Readings.

7.1 INTRODUCTION:

Payment of wages differs in different occupations, localities and grades. One therefore comes across such terms as occupational wage differentials, inter-industry, inter-firm, inter - area or geographical differentials and personal differentials.

The causes of difference in wages in different occupations, localities and grades of employment needed to be analysed. Wages everywhere tend to approximate to the marginal productivity of labour which is different in different occupations and grades. It varies with the degree of scarcity of labour in relation to the demand for it, or ultimately in relation to the demand for the products produced by labour.

The wage differentials that can be attributed to imperfections in the employment markets, such as the limited knowledge of workers in regard to alternative job opportunities available elsewhere, obstacles to geographical, occupational or inter-firm mobility of workers; or time lags in the adjustment of resources distribution and changes in the scope and structure of economic activities. Examples of such wage differential are inter industry, inter-firm, and geographical wage differentials.

The wage differentials which originate due to social values, and prejudices which are deeper and more persistent than economic factors. Wage differentials by age, sex, status or ethnic origin. The occupational wage differentials, which would exist even if employment markets were perfect and social prejudices, were absent.

7.2 FRAMEWORK OF WAGE DIFFERENTIALS:

The importance of proper wage differentials has been stressed by 'Harry Ober' in his book "Occupational wage differentials in Industry".

The study of wage differentials is important both from academic as well as practical point of view. Wage differentials are a necessary concomitant of the wage system in the modern industrial organisation and have been recognised as such in all countries, irrespective of their political and economic background. Wage differentials are directly related to the allocation of the economic resources of a country - including manpower, growth of national income, and the pace of economic development. Economic and social welfare activity depends, in a large measure on such wage differentials.

Wage differentials have a great economic and social significance, for they are directly related to the allocation of the economic resources of a country.

Wage differentials reflect differences in physical and mental abilities of workers, in productivity and efficiency of management, and consumer preferences. By providing an important incentive for labour mobility, they bring about a reallocation of the labour force under changing circumstances. Wage differentials act as an incentive to work hard, to develop requisite stalls and improve productivity. Different levels of wages exist mainly to fulfil the objectives of efficiency and justice in wage payment.

The wage differentials must be based on certain sound principles and rationalism, namely:

a) Wages should be commensurate with work.

b) Equal wages should be paid for equal work.

c) Differentials should be such as to provide a sufficient incentive for acquiring skill and improving productivity; and

d) Wage differentials should be sufficient to attract workers to jobs in industries in which there is a shortage of labour.

7.3 REASONS FOR WAGE DIFFERENTIALS:

7.3.1. Considerations to Wage Differentials:

The Committee on Fair Wages recommended that wage differentials should be established on the basis of certain considerations.

i) The degree of skill.

ii) The strain of work.

iii) The experience involved.

iv) The training required.

v) The responsibility undertaken.

vi) The mental and physical requirements.

vii) The disagreeableness of the task.

viii) The hazard attendant on the work.

ix) The fatigue involved.

According to the Planning Commission, wage differentials for various jobs should be maintained at the minimum levels justified by the criteria which had been suggested by the Fair Wages Committee.

7.3.2 Factors influence the Wage Differentials:

Robert E. Sibson has presented a useful list of factors to explain wage diversity:

1) The wide difference in the earning of employees.

2) The personnel policy of employees.

3) Imperfections of the labour market.

4) Job security.

5) Regularity of employment.

6) The relative bargaining strength of individual employers and local unions.

7) The value of labour to an individual employer.

8) The proposition of total costs represented by labour costs.

9) The market conditions of the employers product.

10) Variation in individual performance.

11) The growing importance of fringe benefits in employee compensation.

12) Job disutilities connected with the work and with specific jobs and hazards inherent in the occupation.

Wage differentials may be due to any one or combination of factors such as :

a) Degree of skill and training period needed for discharging and assigned job.

b) State and nature of the work to be performed.

c) Mental and physical exertions and risk in doing job.

d) Disagreeableness or unpleasantness of the assigned task.

e) Differences in the efficiency of labour, which may be due to in born quality, education and conditions of work.

f) Demand and supply of particular type of labour service.

g) Existence of non-competing groups due to difficulties in the way of labour mobility from low paid to high paid employment.

h) Differences in agreeableness or social esteem of employment.

7.4 TYPES OF WAGE DIFFERENTIALS:

The common types of prevalent wage differentials are occupational or still differentials, inter-plant wage differentials inter-industry wage differentials, regional or geographic wage differentials and differentials based on the age or sex.

7.4.1 Occupational Wage Differentials:

These indicate that different occupations require different qualifications; different wages of skill and carry different degrees of responsibility, wages are usually fixed on the basis of the differences in occupations and various degrees of skills. The basic functions of such differentials are:

a) to include workers of undertake “more demanding more agreeable or dangerous” jobs, or those involving a great chance of unemployment or wide uncertainty of earnings.

b) to provide an incentive to young person’s to incur the cost of training and education and encourage workers to develop skills in anticipation of higher earnings in future.

c) to perform a social function by way of determining the social status of workers.

In countries adopting a course of planned economic development, skill differentials play an important role in manpower and employment programmes, for they considerably help in bringing about an adequate supply of labour with skills corresponding to the requirements of product plans.

Inter - Occupational Differentials:

Inter-occupational differentials may comprise skilled, unskilled and manual wage differentials; non-manual and manual (white and blue collar); and general skill differentials occupational wage differentials generally follow the changes in the relative supplied of labour to various occupations.

7.4.2. Inter-firm differentials:

Inter-firm differentials reflect the relative wage levels of workers in different plants in the same area and occupation. The main cause of inter-firm wage differentials is:

a) Differences in the quality of labour employed by different firms;

b) Imperfections in the labour market; and

c) Differences in the efficiency of equipment, supervision and other Non - labour factors.

Differences in technological advance, managerial efficiency, financial capacity, age and size of the firm, relative advantages and disadvantages of supply of raw materials, power and availability of transport facilities these also account for considerable disparities in inter firm wage rates. Lack of co-ordination among adjudication authorities, too, is responsible for such anomalies.

7.4.3. Inter - area or Regional Differentials:

Inter area or regional wage differentials are arise when workers in the same industry and the same occupational group, but living in different geographical areas, are paid different wages. Regional wage differentials may be conceived in two senses. In the first sense, they are nearly a part of inter-industry differentials in a particular region. “The industry mix varies from one area to another, and for this reason alone, the general average of wages would be expected to vary. In the second sense, they may represent real geographical differentials, resulting in the payment of different rates for the same type of work. In both cases, regional differentials affect the supply of manpower for various plants in different regions.

Such differentials are the result of living and working conditions, such as unsatisfactory or irksome climate, isolation, sub-standard housing, disparities in the cost of living and the availability of manpower. In some cases, regional differentials are also used to encourage planned mobility of labour.

7.4.4 Inter - industry Differentials:

Inter - industry wage differentials arise when workers in the same occupation and the same area but in different industries are paid different wages. Inter - industry differentials skill differentials. The industries paying higher wages have mostly been industries with a large number of skilled workers.

While those paying less have been industries with a large proportion of unskilled and semi skilled workers. Other factors influencing inter - industry differentials are the extent of unionisation, the structure of product markets, the ability to pay, labour - capital ratio and the stage of development of an industry.

7.4.5. Sector Differentials:

Wage differentials between agricultural sector and industrial sector are generally a characteristic of developing economies like India. The main reason for such sectoral differences in wage rates are the nature of the workers groups whether they are an organised group or unorganised group, and the level of economic development of sector.

7.4.6 Sex or Gender Differentials:

Personal wage differentials arise because of differences in the personal characteristics (age or sex) of worker who work in the same plant and the same occupation. “Equal pay for equal work” has been recommended by the I.C.O. convention (No. 100), as also by Industrial courts, labour tribunals, the minimum wages committee, and fair wages committee. But in practice this principle has not been fully implemented because in occupation which involves strenuous muscular work, women workers, if employed are paid less than women employees, less mobility among them, their lower subsistence and their weak constitution are other reasons which bring them lower wages than their male counterparts receive.

To give effect of article 39 of India constitution, the Government of India passed the Equal Remuneration Act, 1976. The act provides for the payment of equal remuneration for men and women workers and for the prevention of discrimination on the ground of sex against women in the matter of employment and for other incidental matters connected herewith. It also seeks to provide for increasing opportunities for women in the specified employments.

7.5 GEOGRAPHICAL WAGE DIFFERENTIALS IN INDIA:

All India average wages do not reflect the level of variation in wage levels across regions. In general it has been argued that wages are highly suppressed in the poorer regions, while the developed regions have fairly high wage levels. Apart from the fact that general wage levels (particularly rural casual wages) are very low in the poorer states, the rural-urban and casual-regular dualisms are stark in most of the poorer states in

India. Rural casual wages vary from a high level of Rs 120 per day in Kerala to a low of Rs 34 in Chhattisgarh, followed closely by Rs 36 in Madhya Pradesh and Rs 38 in Orissa and Maharashtra. Most of the developed states, such as Punjab, Haryana, Gujarat, Himachal Pradesh, and Tamil Nadu, have higher casual wages in both rural and urban areas as compared with those in the poorer states and the all India average Although two poorer states, Chhattisgarh and Madhya Pradesh, have very low casual and regular wages, most of the poorer states such as Assam, Bihar, Jharkhand, Karnataka Orissa, and Jammu and Kashmir have high urban regular wages.

In most of the less developed states such as Orissa, Karnataka, Chhattisgarh, Madhya Pradesh, and Andhra Pradesh, the ratios are approximately similar, with the rural casual wage being approximately one-fifth of the urban regular wage. In other less developed states such as Assam, West Bengal, and Uttar Pradesh, the ratios are little better than the all India average. In contrast, most of the developed state shows a comparatively lower disparity across casual and regular wages and also across rural and urban areas. The least disparity in this regard is in Kerala, where the rural and casual wages are almost equal and the rural casual wages are approximately two-thirds of the urban regular wages.

7.6 DESIRABILITY OF WAGE DIFFERENTIALS:

Wage differentials perform a very important and useful economic function in that "they provide an important incentive for labour - mobility and bring about a reallocation of labour force under changed conditions, however imperfect the market mechanism may be". In a communist society there is a forcible direction of labour in accordance with the needs of the society but in a capitalist society the same objective is achieved on a voluntary basis through the instrumentality of wage differentials. In a planned economy where wage cannot and should not be determined by the market faces of demand and supply, wage differentials have an important role to play in the regulation of wages and development of a national wages policy. An under developed or a developing economy requires the development of new skills and creation of new occupations. Shortage of workers skilled as well as unskilled in the basic and key industries and is backward and underdeveloped regions may create serious bottlenecks that might impair the efficiency of planning and check the growth of the economy. The maintenance of proper wage differentials therefore, becomes an essential aspect of the national wage policy.

Further, wage differentials are desirable within certain limitations to provide a strong incentive to the low paid workers to work hard and produce more with a view to enhance their earnings. This is the specific advantage of piece rates. Though the workers may exert themselves for noneconomic motives as well, the economic motive - reward in terms of money is very important.

7.7 WAGE DIFFERENTIALS IN INDIA:

Due to the paucity of relevant data on wage differentials, it is not possible to analyse them in India; yet the main features of the Indian wage structure may be stated thus: "As a characteristic the unorganised labour market, personal differentials because of job selling, individual bargaining and wage discrimination have tended to persist in India, especially in the unorganised sector of the economy, and even in the organised and unorganised sections in industry.

The tendency appears to be towards the elimination of wage differentials because of government interference through the fixation of the minimum wages and of late, through the appointment of wage Boards and pressures from trade unions. Wage differentials by sex are more in India. Both economic and social reasons account for this phenomenon. Despite the fact the constitution of India enjoins upon the state to direct its policy towards securing "equal pay for equal work for men and women, awards of some Industrial Tribunals provide for "different wages for men and women workers, not one the ground that the wages of women workers support a smaller family that the cost of employing women workers is higher".

As regards inter-firm and inter-industry differentials in Indian, the former were quite important and frequent in the post, particularly in the jute industry. Of late, however, there has been a tendency towards the elimination of inter-firm differentials. The forces which tend to eliminate n workers inter-personal differentials in the country operate in this case as well.

India witnessed a mere 1% hike in wages against a 5% growth in productivity during the last two decades to employees, according to a recent study by International Labour Organisation (ILO).The country ranked ninth in the list of countries offering highest disparity in wage and productivity growth between 1990 and 2007. Altogether 32 countries were surveyed by the ILO. China had offered among the best wages to its workers with its productivity to wage growth ratio standing at 9:10.While Brazil was the worst, with its productivity to wage growth ratio standing at a dismal 3.5:-3.5.The report, titled 'World of Work Report 2008: Income inequalities in the age of financial globalisation' produced by the ILO's International Institute for Labour Studies, concluded that the gap between richer and poorer households widened since the 1990s, despite rapid globalisation and boom in economic.

7.8 PUBLIC SECTOR Vs. PRIVATE SECTOR:

Examination of wages in public, formal-private and informal-casual sectors shows that differences in wages between workers in the public and private-formal and informal sectors are positive and high. The average real wage in the public sector was about 2.1 times that in the organized private sector. The difference in real wages between the public and private-informal sector is even larger at 3.8 times. The public sector tends to employ workers with more human capital. Since the labour market places a premium on more education and experience, adjusting for these differences in characteristics between public and private sector workers reduces the size of the wage differential. The public sector wage premium remains, ranging from 62% to 102%, over private-formal, and from 164% to 259% over casual-informal sectors, The wage differentials tend to be higher in rural as compared to urban areas The wage differential also tends to be higher for low-skilled workers.

The paucity of evidence on the magnitude of the wage differentials for the Indian labour market as a whole is usually blamed on the scarcity of suitable data. Even though many agencies collect some information on employment and wages, the comparability of public and private sector wages is complicated because wage data are rarely collected in conjunction with information on the qualifications of workers. Thus, the notion of alternative wages is rarely used. Yet, some data from formal sources exist and several authors have analyzed wages and wage differentials using individual-level data. Overall, the information on the differences in wages is limited to the factory sector, to the segment of the labour market, which employs highly skilled workers, and to some geographic areas. Data on wages from the 1997-98 Annual Survey of Industries (Central Statistical Organization, Government of India), which covers the factory sector, suggest that the public sector offers higher remuneration for workers compared to the private sector. There are substantial variations in pay within the public sector. Workers employed in units owned by the Central government receive wages that are nearly twice as high as the sector average; followed by workers in units owned jointly in the public sector. Workers in "wholly" private enterprises appear to receive the lowest wages among all considered categories Most of these studies used the survey of Degree Holders and Technical Personnel (DHTP) conducted, along with the 1981 Census of India, on behalf of the Division of Scientific and Technical Personnel of the Council for Scientific and Industrial Research. Data were collected on the basis of a 20% Census sample in 12 states and using the complete enumeration samples in other states and union territories.

7.9 SUMMARY:

Wage differentials are inevitable in any type of economy. Whether capitalist or socialist. They are necessary both in the interests of efficiency and in the interests of justice. But wide disparities in wage levels and consequent exploitation of low wage earners belonging to a particular section of society are not to be justified under any circumstance. Wage differentials for various jobs should be maintained at the minimum levels justified by the criteria which had been suggested by the committee on fair wages. It is heartening to note that over a period time, various influences such as trade unionism, government intervention by compulsory adjudication, minimum wage enactments and the process of standardisation of occupation, have helped to reduce the wage differentials in our country. There is no doubt that workers' expectations are such that the Indian society of the future will move towards much lower disparities in income than is at present keeping this in view, there is a general need to evolve a policy on wage differentials.

7.10. KEY WORDS:

Wage Differentials: Wage is differentiating with several factors i.e. skill, occupation, industry, and region.

Inter - Industry Wage Differentials: Inter - industry wage differentials arise when workers in the same occupation and the same area abut in different industries are paid different wages.

Regional Wage Differentials: Inter - area or geographical wage differential arise when works in the same industry and in the same occupational group, but living in different geographical areas, are paid different wages.

7.11. SELF ASSESSMENT QUESTIONS:

1. Wage differentials are essential, discuss.

2. Wage differentials have considerable economic and social significance for an industry discuss.

3. Briefly discuss the principals of wage differentials and write various factors causing wage differentials.

4. What do you mean by wage differentials? Explain briefly the various types of wage differentials.

5. Indicate an account of disparity in wage rates in different industries in India.

6. Examine the principle of "Equal pay for Equal work" in the context of its implementation in India.

7.12. FURTHER READINGS:

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LESSON - 8

METHODS OF WAGE FIXATION IN INDIA

8.0 OBJECTIVE:

After reading this lesson, the student is able to:

- Know the Need for Wage Fixation.
- Study the Principles of Wage Fixation.
- Understand the Methods of Wage Fixation.
- Visualise the Wage Fixation Practices in Indian Industries.

STRUCTURE:

8.1 Introduction

8.2 Need for Wage Fixation

8.3 Principles of Wage Fixation

8.4 Norms and Procedures for the Fixation of Wages

8.5 Institutions / Methods for Wage Fixation.

- **8.5.1 Statutory Fixation / Legislations**
- **8.5.2 Collective Bargaining**
- **8.5.3 Wage Boards**
- **8.5.4 Pay Commissions**
- **8.5.5 Adjudication**

8.6 Wage Fixation Practices in Public Sector

8.7 Summary

8.8 Keywords.

8.9 Self Assessment Questions

8.10 Further Readings.

8.1 INTRODUCTION:

The history of wage fixation in India is of a recent phenomenon. There was practically no effective machinery until the Second World War for the settlement of disputes for the fixation of wages. Under the Industrial Disputes Act 1947, various tribunals have passed awards resulting wages in a number of important industries. Immediately after attainment of Independence, industrial relations in our country started deteriorating rapidly. There was a phenomenal increase in the number of industrial disputes, mostly over wages, leading to a substantial loss of production. Realising that industrial peace was a sine-qua-non for progress on the industrial as well as economic front, the Central Government convened in 1947 a tripartiate conference consisting of the representatives of the employers, labour and government.

8.2 NEED FOR WAGE FIXATION:

The spirit of truce was incorporated by the Government of India in its declaration of Industrial Policy Resolution of 1948. In the statement embodied in the Resolution, the Government included two items which have bearing on wages namely;

i) Statutory fixation of minimum wages in sweated industries; and

ii) Promotion of fair wages agreement in more organised industries.

To fulfil the first objective, the Minimum Wages Act, 1948 was passed to lay down certain norms and procedures for the determination and fixation of wages by the Central and State Governments in sweated scheduled employments.

To fulfil the second objective, the Government of India appointed in 1949 a tripartiate committee on fair wages to determine the principles on which fair wage should be fixed and to suggest lines on which these principles should applied.

8.3 PRINCIPLES OF WAGE FIXATION:

A set of principles of wage fixation have emerged over the last few years as guidelines for the adjudicating authorities on wage demands. The fair wage committee in its report observed that “any attempt to evolve principles for governing the fixation of wages must be made against the background of general economic conditions of the country and the level of national income”.

The principles laid down by the Fair wage committee were discussed at length by the Supreme Court in the case of Crown Aluminium Works v/s their workmen (1958 I LLJ I), and were expounded in detail in the case of Express Newspapers v/s Union of India and others (1961-I LLJ 339). In the case of Crown Aluminium works, the Supreme Court made the following well known and off quoted observation: "There is, however, one principle which admits of no exceptions. No industry has a right to exist unless it is able to pay its workmen at least a bare minimum wage. It is quite likely that in developing countries, where unemployment prevails on a very large scale, unorganised labour may be available on starvation wages. but the employment of labour on starvation wage cannot be encouraged or favoured in a modern democratic welfare state. If an employer cannot maintain his enterprise without cutting down the wages of his employees below even a bare subsistence or minimum wage, he would have no right to conduct his enterprise on such terms".

In the case of express News papers, it was held that the upper limit of wages must be set by capacity to pay, not of a particular unit then of but on an industry - cum - region basis. Another principle which the Supreme Court has stressed is that, while fixing the wage - scales the total emoluments, including the basic wages and dearness allowance, have to be taken into consideration.

8.4 NORMS AND PROCEDURES FOR THE FIXATION OF WAGES:

The wage fixation policy should ensure prevention of exploitation of labour through the payments of unduly low wages, particularly in those employments where sweated conditions exist and where the workers are vulnerable because of lack of organisation. It is a step in the direction of realising the objectives of wage in the direction of realising the objectives of wage policy in a developing country like India; namely, the abolition of malpractices and abuses in wage payment, and fixation of minimum wage for workers whose bargaining position is weak because they are unorganised wages cannot be left to be determined entirely by the market faces and the government has a positive role play in ameliorating the conditions of the low paid workers. The following norms shall be followed while fixation of wages.

1. The wages have to be fixed on an industry-cum-region basis.

2. Uniformity shall be maintained in the wage levels of different concerns of the same industry working in the same region.

3. Wages prevailing in an establishment must be comparable with those given to workmen on similar grade and scale by similar establishment in the same industry.

4. Employees getting the same wages should get the same dearness allowance, irrespective of whether they are working as clerks or members of subordinate staff of factory workmen.

8.5 INSTITUTIONS/METHODS OF WAGE FIXATION IN INDIA:

Wage and salary incomes in India determined through several institutions. There are five methods of wage fixation in India: 1) Statutory Fixation, 2) Collective Bargaining, 3) Wage Boards, 4) Government Appointed Pay Commissions, 5) Adjudication and Tribunals.

8.5.1 STATUTORY FIXATION / LEGISLATIONS:

The major wage laws include the Payment of Wages Act, 1936 and its subsequent amendments, the Minimum Wages Act, 1948 and the Equal Remuneration Act, 1976.

1) The Payment of Wages Act, 1936:

Except Sikkim, The Payment of Wages Act, 1936, extends to the whole of India and applies to persons employed in any factory as defined in the Factories Act, 1948 and in the railways, receiving wages and salaries below Rs. 1,600 a month. Neither employers can withhold the wages earned by workers nor can they make any unauthorised deductions. Payments must be made prior to the expiry of a specified day after the last day of the wage period. While there is a provision to impose fines for only those acts of omission which have been approved by the appropriate government, the fines cannot exceed an amount equal to three paise in a rupee of the wage payable. If the payment of wages is delayed or wrongful deductions are made, the workers or their trade unions can file a claim.

2) The Minimum Wages Act, 1948:

The Minimum Wages Act, 1948 relates to the employment situations embodied in part I and II of the Schedule to the Act. The appropriate governments are empowered to include other employment situations in the schedule and fix or revise the minimum wage rates. It is obligatory on the part of the employer to pay the minimum rates of wages fixed in terms of the procedures prescribed by law, irrespective of employer's capacity to pay. The Act provides for fixing minimum wages in certain employment situations where sweated labour prevails or where there exists possibility of exploitation of labour. However, minimum wages are not to be fixed in an industry which employs less than 1,000 employees in the entire state, although this condition has been relaxed in a subsequent amendment of the Act. Thus, the Act empowers the central and state governments to fix minimum rates of wages in woolen, carpet-making or shawl-weaving establishments, rice, flour or dall mills, tobacco or bidi-making industry, plantations, oil mills, road shed or insufficiently organised. In a developing economy, with severe unemployment, construction or building operations, stone breaking or stone crushing, lac manufactories, mica works, public motor transport, tanneries and leather manufactories and agriculture. The Act provides for the fixation of a minimum time-rate, a minimum piece-rate, a guaranteed time-rate, and an overtime rate suitable for various occupations and classes of workers. A minimum wage rate incorporates a basic rate of wage and a cost of living allowance or a basic rate with or without a cost of living allowance, and the cash value of the concessions regarding supplies of essential commodities at normal rates. The Act further prescribes for the payment of wages in cash, although the appropriate government is empowered to pay in wholly or partly in kind. The Act further provides for the appointment of committees, subcommittees, advisory board for assisting the appropriate government in fixing and revising the wages. The Act also provides for revision of minimum rates fixing at suitable intervals, not exceeding five years. Accordingly, wage revisions are done by different state governments and union territory authorities. The facts taken into account for initial fixation of wages as well as for the subsequent revisions under the Act include minimum wage rates fixed by other states in similar industries, prevailing wage rates in adjacent areas/industries, increases in the cost of living since the last fixation, etc.

The Act, however, does not provide any guidance to the wage fixation authorities with respect to the content of minimum wages, factors to be taken into account while fixing the minimum rates of wages, size of the family unit for which minimum wage rates have to be fixed, weightage to be assigned to different factors such as cost of living, needs of workers, etc. Therefore, it is left to the individual committee or the government to determine their own standards and arrive at conclusions. Historically, the first to lay down the guidelines for fixation of minimum wages was the fifteenth session of the Indian Labour Conference held in July 1957. It passed a resolution stressing that the minimum wage should be need-based to meet the minimum requirements of the workers. The resolution embodies several norms for the fixation of such wages in industry.

The one-man committee headed by K.I. Vidysagar, in his report dated 19th December 1966, suggested a number of norms which must be taken into account while fixing/revising minimum wages. Likewise, the National Commission on Labour (1969) provided a number of recommendations with regard to the statutory minimum wage. A committee of secretaries belonging to six states with additional secretary of the Ministry of Labour as chairman was formed in 1981. The committee made a number of recommendations with respect to the criteria for fixation of minimum wages and evolve a formula for variable dearness allowance to be attached thereto.

Although the Minimum Wages Act originally included 13 industries/employments, the minimum rates of wages have been fixed in 197 employments till 30 June 1985. During July 1995 to June 1996, minimum wages were revised in 426 employments.

Viewpoint of National Labour Law Association on the Minimum Wages Act, 1948:

In the opinion of National Labour Law Association, while significant progress has been made in extending the coverage of the Act, the effort has neither been systematic nor uniform. There is also no means to verify or to ensure that all the employments for which minimum wages need to be fixed are actually included in the schedule, and minimum wage have been fixed in respect of all of them.

Fixation of minimum wages is a kind of "safety net" to protect workers from exploitation by payment of unduly low wages. This protection should be available to every worker who needs it. There is no justification to deny this protection to those employed in employments which are not included in the schedule to the Act unless there is proper arrangement for regulation of their wages by collective agreement or otherwise. It is, therefore, proposed to make law applicable to all employees with the provision that where the minimum was fixed or revised under this code is less than the wage fixed through collective bargaining, arbitration, adjudication, wage board or otherwise the employee shall be entitled to be paid the wages at the higher rate applicable to him.

Finally, there is limitation in the Act as it does not define the term minimum wages. While several states consider that the concept of minimum wage as currently applied to sweated industries needs no change, trade unions have urged that to avoid differences in interpretation by wage fixing authorities, "minimum wage" should be spelt out in precise terms. Accordingly, the minimum wages vary from region to region and even within the same region from time to time depending upon particular situations. It has been recommended by the National Labour Law Association that the minimum wage be defined as "a wage which is fixed with reference to the basic needs of an employee so as to provide him and his family consisting of his spouse and two children adequate means of livelihood and a decent standard of living".

3) The Equal Remuneration Act, 1976:

The Equal Remuneration Act, 1976 provides for payment of equal remuneration to men and women workers for the same work or work of similar nature. It prevents discrimination on the ground of sex against women in the matter of employment and for matter connected therewith except where the employment of women in such work is prohibited or restricted by under any law for the time being in force. The Act has been enforced in several spheres such as plantations, local authorities, central and state governments, banks, educational institutions, mines, hospitals, hotels and restaurants, manufacture or textiles and textile products, wholesale and retail trade, construction, agriculture and air transport industry. In June 1978, it was extended to community, social and personal services.

8.5.2 COLLECTIVE BARGAINING:

The phrase ‘Collective Bargaining’ originated in the writings of ‘Sydney’ and ‘Beatrice Webb’. This term relates to those arrangements under which ways and condition of employment generally are decided by agreements negotiated between the parties.

Collective bargaining is a process of joint decision - making and basically represents a democratic way of life in industry. It establishes a culture of bipartism and joint consultation in industry and a flexible method of adjustment to economic and technical changes in an industry. It helps in establishing industrial peace without disrupting either the existing arrangements or the production activities.

Bargaining may also take place at enterprise level and plant level. It may be conducted through a union (or a group unions) and an association representing wages, hours at work and other conditions of employment. Broadly speaking the following factors affect the wage determination by collective bargaining process:

1. Alternate choice and demands;

2. Institutional necessities, e.g. if ratification of an agreement requires a majority vote of employees, the character of wage settlement would have to be such as would be acceptable to major 3. The right and capacity to strike.

‘Joseph Shister has opined that collective bargaining can best be analysed by listing its principles characteristics. He lists five characteristics: 1) Collective bargaining involves group relationships; 2) it is both continuous and evolutionary; 3) it interacts with the socioeconomic climate; 4) it is private, but at times involves government action; and 5) it varies from setting to setting.

‘John Dunlop and Derek Bok’ have listed five important function of collective bargaining : i) establishing the rules of the work place; ii) determining the form of compensation; iii) standardising compensation; iv) determining priorities on each side; and v) redesigning the machinery of bargaining.

Employer's federation of India shows that collective bargaining system has been adopted in almost all industries.

The Bureau of public enterprise has increasingly exerted unifying influence on collective bargaining in public sector undertakings.

In a modern democratic society wages are determined by collective bargaining in contrast to individual bargaining by workers in the part. When wages are determined by individual worker bargaining separately with his employer.

8.5.3 WAGE BOARDS:

The establishment of tripartite (non statutory) wage boards was recommended by the Fair Wages Committee with a view to determining wages on an industry-cum-region wise basis. In March 1957 the first Wage Board was established for the textile industry (followed by the second formed in 1964). Thereafter, several wage boards were established for sugar (1957, 1965, 1985), cement (158, 1964), jute (1960), tea plantations (1960), rubber plantations (1961), coffee plantations (1961), iron and steel (1962), iron ore mining (1962), limestone and dolomite mining (1963), coal mining (1962), working journalists (1963, 1985), nonworking journalists (1964, 1985), ports and docks (1964), engineering (1964), heavy chemicals and fertilizer (1964), leather and leather goods (1966), electricity undertaking (1966) and road transport (1966). The composition of wage boards is tripartite in character and thus, involves the representatives of employees and workers and an independent chairman. An equal number of representatives of the employers and workers are appointed by the government in consultation with them. The chairman and two other independent members (including consumers' representative) are nominated by the government. Usually, the chairman is a judge serving or retired, while the consumers' representative is a Member of Parliament. The total number of members of the wage boards formed hitherto varies from seven to nine. Although the wage structure recommended by a wage board remains in operation for five years, it may not be necessarily implemented by the management.

Working of Wage Boards:

The objectives of wage boards include more durable results, improved climate for industrial relations, promotion of interests of consumers and the community, standardisation of wage structure and support to social and economic policies of the government. Explicitly, wage boards have not succeeded in accomplishing these objectives largely. Specifically they have failed to tackle the problem of wage differentials and payment by results. There are several drawbacks in the system of wage structures. Despite several inadequacies, it is admitted that the system has provided a rity; machinery to pay for bipartite collective bargaining on wages and allied issues on an industry wise basis at the national level. It has been suggested that wage boards should be provided statutory support to make them effective. However, as Subramanian observes, if wage boards are made statutory and their recommendations made legal binding, they will be inseparable from industrial tribunals and lose whatever advantage they have under a voluntary system of being a convenient forum for collective bargaining. Moreover, wage determination on all India bases is inconsistent with the requirements of a developing country involving uneven levels of development in various regions and industries. Indeed, collective bargaining of wage claims is likely to be effective when limited to an industry in a small area or region than when embracing the national level.

Viewpoint of National Labour Law Association:

Although India has a long experience of Wage Boards, observes National Labour Law Association, the spirit of cooperation among parties evaporated and each started mistrusting the other. Accordingly, there was inordinate delay in completing the work and even when completed the recommendations came to be challenged in the courts stalling their implementation. The practice of setting up wage boards has, therefore, gradually been discontinued. Currently, the law requires wage boards to be set up for the newspaper industry under the Working Journalists and other Newspaper Employees (conditions of services) and Miscellaneous Provisions Act, 1955 The only other wage board set up recently was for the sugar industry. In order to minimise litigation on the awards of the wage boards, the Association proposed to make them final and binding subject only to an appeal to National Labour Relations Commission. It is also proposed to keep the awards in operation for a minimum of three years which may extended by mutual agreement between the parties. It is also suggested that there should be an enabling provision in the law for setting up wage boards for any activity when necessary in consultation with the most representative organisations of employees and employers concerned.

8.5.4 PAY COMMISSIONS:

The First Central Pay Commission:

The First Central Pay Commission (1947) Justice Varadachariar asserts that “the state must now take some steps forward in the direction of giving effect to the living wage principle”. Thus, the commission stresses that the “living wage” should form the basis for determining the minimum wage which should not be too low to cause under nourishment. Accordingly, the minimum wage was fixed at Rs. 30 per month in the lowest grade of class IV employees. It asserted that a state should not attempt to be a model employer and accordingly “it will not be fair to the country to encourage a claim by civil servants to be treated better than their fellow countrymen”. However, the commission recognises that” the lower grades of Government servants with fixed incomes of small amounts have been hard hit, they must be relieved, at least to some persisting”. Notwithstanding this observation, it did not limit its recommendations regarding dearness allowance to “the most vulnerable section” of the employees but also allowed it to higher salaried employees. Obviously, it allowed more than 100 per cent neutralisation in instances where the basic salary was below Rs. 46.25. Thus, it considered Rs. 55 as an appropriate minimum wage for January 1947 at consumer price index of 80.

The Second Central Pay Commission:

The Second Central Pay Commission was constituted in August 1957 and submitted its report in August 1959. Regarding principles of pay fixation, the commission observed, “We have reached the conclusion that the minimum wage or salary not be determined merely on economic considerations, but should satisfy also a social test–both because of its intrinsic validity and because of its bearing on efficiency”. It recommended that minimum wage should be fixed at Rs. 80 per month corresponding to consumer price index of 115 obtained at the time of reporting. The commission visualised dearness allowance as “ a device to protect to a greater or lesser extent, the real income of wage earners and salaried employees allowance to those drawing a salary of less than Rs. 300 per month. Accordingly, for others it asserts, “As it is, we consider that it would be appropriate to fix the entire remuneration for such staff in the form of salaries which appear reasonable in the present conditions”. The commission further states, “If the Government were to function as a model employer in the sense that they paid higher wages and salaries than other good employers for comparable work... the community would be required to pay a price which the efficiency of the public service did not demand and which should not in fairness, be asked of the community. The Government cannot, therefore, in our opinion be a model employer in this sense".

The Third Central Pay Commission:

The Third Central Pay Commission submitted its report in 1973. It stressed on the reduction of prevailing numerous pay scales by compiling the posts of several different categories and occupational groups in one single grade. Regarding the fixation of the minimum wage, the commission observes, "we are, therefore, of the view that the starting salary need not be fixed higher than Rs. 185 per month". Accordingly, the minimum scale devised by the commission was Rs. 185-2-193-3-220 based on the consumer piece index of 200 obtained in 1972. It asserts, "we not consider it practicable to recommend more than one level for the semiskilled category within the pay range available" and thus, six scales were board-banded into one scale of Rs. 200-280 incorporating dearness allowance and interim relief. Likewise, 13 existing scales for skilled categories of working staff were board were broad banded into three new scales of Rs. 260-350, Rs. 260-400 and Rs. 320-400. Again the grades of highly skilled workers were devised as Rs. 330-480 and Rs. 380-560, while that of master craftsman as Rs. 425-640. The grades of lower division clerks and upper division clerks were revised to be Rs. 260-400 and Rs. 330-560, respectively. The commission recommended payment of dearness allowance to all employees drawing pay not exceeding Rs. 2,250 per month. However, the report of the commission recommended by the commission raising the minimum wage for the lowest category of class IV from Rs. 185 to Rs. 196. The commission denied the role of the model employer to the government. It observes, "We would be labouring under a delusion if we were to suggest that the Central Governments should now take upon itself the responsibility of being a pace-setter, and of bettering the wages paid by reputable concerns in the private sector".

The Fourth Central Pay Commission:

The Fourth Central Pay Commission, appointed under the chairmanship of Justice P N Singhal on September 1, 1983, submitted its report on June 30, 1986. It was specifically asked to examine the variety of allowances and benefits in kind which are currently available to the employees in addition to pay and to suggest their rationalisation and simplification to promote efficiency in administration. The commission's report is divided into two parts.

Part I relates to structure of emoluments, conditions of service of central government employees including union territories, members of all India services and personnel belonging to armed forces.
Part II deals with the pension structure for pensioners including both past and future and the death-cum-retirement benefits for all categories of employees.

It has been felt with the pension structure for pensioners including both past and employees with those of public sector undertakings were not based on sound reasoning. There is also need to rationalise transfer / travelling allowance rules to resolve various problems and hardships which the transferred employee is subjected to. The commission has been appreciated for providing a new dearness allowance formula, liberalisation of HRA and withdrawal of overtime allowance for nonindustrial employees.

The Fifth Central Pay Commission:

The Fifth pay Commission was formed on April 9, 1994 under the Chairmanship of S R Pandian, a retired Supreme Court Judge, The other members was Suresh Tendulkar and M K Kaw. The Commission's report has caused immense contradictions and resentment. It has proposed a total annual increase of Rs. 9,500 crore (as compared to Rs. 5,000 crore provision in the current year) in the central government's expenses towards:

		Rs. (in crore)
Transport allowance	:	522
Housing	:	2,000
Salaries (civil and defence)	:	2,333
Exemption of allowances from income tax	:	132
Increase in pension	:	9,000
Other expenses (servant allowance, LTA, entertainment allowances, medical cover, etc.)	:	3,646

There is recommendation for increasing the pay of lower level employees by 20 to 40 percent and that of senior level bureaucrats by almost 130 per cent. There is also proposal to reduce hiring, abolish currently vacant posts, and restructure government department. It has made several recommendations to improve productivity. These include:

A six-day week instead for five, which will increase the number of working days by 40. the number of gazetted holidays be reduced from 17 to three (Republic Day, Independence Day and Mahatma Gandhi's Birthday); a holiday be declared only on the death of an incumbent Prime Minister or President and on no other deaths.

All payment of overtime allowance to employees should be discontinued. Instead, staff deployed on weekly off-days may be given compensatory leave.

The payment of a time-punching machine, to ensure punctuality in every office-applicable even to the Cabinet Secretary.

Top executives (secretary-level officers) should be entitled to T class or AC first class train travel; senior executives (above the post of deputy secretaries) be entitled to 'Y' class air travel and AC first class train-travel; executives (below the level of deputy secretary) be entitled to economy class air travel and AC second class train travel; and supervisory staff be entitled to AC second class train travel.

Government should phase out staff cars by attaching such cars only to top executives. beginning common pool of private vehicles; freezing the cadre of staff car drivers; and abolishing vacant posts of drivers.

Increase timings of government-run service institutions like banks, hospitals, dispensaries and shopping centres by introducing a shift-system in these places.

All adhoc bonus schemes should be made productivity-related and a performance-related increment scheme should be introduced.

SIXTH CENTRAL PAY COMMISSION

In July 2006, the Cabinet approved setting up of the sixth pay commission. This commission has been set up under Justice B.N.Srikrishna with a timeframe of 18 months. The cost of hikes in salaries is anticipated to be about Rs. 20,000 crore for a total of 5.5 million government employees as per media speculation on the 6th Pay Commission, the report of which is expected to be handed over in late March/early April 2008. The employees had threatened to go on a nationwide strike if the government failed to hike their salaries. Reasons for the demand of hikes include rising inflation and rising pay in the private sector due to the forces of Globalization. The Class 1 officers in India are grossly underpaid with an IAS officer with 25 years of work experience earning just Rs.55,000 as his take home pay. Pay arrears are due from January 2006 till September 2008. Almost all the Government employees received 40% of the pay arrears in 2008 and balance 60% arrears (as promised by Government) has also been credited in Government employees account in 2009. The Sixth Pay Commission mainly focused on removing ambiguity in respect of various pay scales and mainly focused on reducing number of pay scales and bring the idea of pay bands. It recommended for removal of Group-D cadre.

SEVENTH CENTRAL PAY COMISSION

The Government of India has initiated the process to constitute the 7th Central Pay Commission along with finalization of its Terms of Reference, the composition and the possible timeframe for submission of its Report On September 25, 2013 the finance minister P Chidambaram announced that the Prime Minister Manmohan Singh has approved the constitution of the 7th Pay Commission. Its recommendations are likely to be implemented with effect from January 1, 2016. Justice A.K Mathur will be heading the Seventh Pay commission, announcement of which was done on 4 February 2014

8.5.5 ADJUDICATION:

Since, Independence, adjudication has become one of the main instruments for settlement of wage disputes, improvement in wage scales, standardisation of wages and allowances. Though Courts and tribunals were primarily intended to deal with the settlement of industrial disputes, in practice, wage fixation has become an important element in their working and functioning. This is because of a large number of disputes concerning wages and allowances. The Industrial Disputes Act 1947 which replaced the Trade Disputes Act 1929, enables the government to intervenes in matters involving disputes between workers and employers. The act also provides the compulsory adjudication in the case of failure of conciliation proceedings. Numerous wage disputes in many industries have been guided by the reference for adjudication to labour courts and tribunals during the past four decades. In this exercise they have been guided by the Fair Wages Committee. The High Courts and Supreme Court have also adjudicated upon such disputes. The awards given by these authorities not only helped in the formulation of a body of principle governing wage fixation but laid down the foundation for the present wage structure in many of the major industries.

8.6 WAGE FIXATION PRACTICES IN PUBLIC SECTOR:

In the beginning, compensation plans for the public enterprises were mainly borrowed from the Government. In some organisations these were based on a comparison of similar industries in private enterprises. In case of public sector steel plants, the pay scales and allowances were a mixture of Government, TISCO, IISCO and Railways. In 1962, the minimum wage and wage structure was suitably modified in line with the recommendations of the Second Pay Commission for Central Government employees. For the first time, a composite Central Wage Board for Iron and Steel Industry was set up in January, 1962 which finalised its report in 1965. This was, as it were, the foundation for determination of wages on industry basis both for public, private as well as joint enterprise. The Wage Board produced an extensive document describing the history of Iron and Steel Industry and the Wage Fixation machinery therein besides dealing with the question of principles of Wage Fixation and allied matters.

The experiment of bipartism which thus started successfully in 1970 in steel was emulated throughout the country. In BHEL, it started in 1973, Coal India Ltd. in 1974 and in other public enterprises later. The history of wage settlements in other enterprises is much the same. In most of the central public sector undertakings today, bilateral committees consisting of representatives of labour and management determine wages and allied fringe benefits, on an industry basis or even enterprise basis, through a process of collective bargaining.

The department of public enterprises issued guidelines for new wage settlements. Under the guidelines, managements are free to negotiate wage structure consistent with generation of resources / profits by individual enterprises / units. Wage increases are to be met from internal resource generation. The period of wage settlements is to be normally five years and there should be no increase in labour cost per unit of output.

8.7 SUMMARY:

The methods generally followed in India with regard to wage determination are collective bargaining, wage boards, governments appointed pay commissions and adjudication by courts and tribunals. Collective bargaining is one of the important methods of wage determination process in India. Its practices very in accordance with such factors as the economic characteristics of the industry. Single plant or company bargaining is more widespread as compared to industry - wide bargaining.

The minimum wages Act was passes in 1948 to provide for machinery for statutory fixation and revision of minimum wages in the scheduled employments,; including plantations and agriculture it is a piece of social legislation which provides protection to workers in employments are to exploitated on account of the lack of organisation and bargaining power. The main object of the Act is to prevent the payment of unduly low wage to workers employed in scheduled employments and to secure certain basic conditions of work and employment. The setting up of tripartiate wage boards for the fixation of fair wages on an industry - cum - region basis was one of the recommendations made by the Fair Wages Committee. The fifteenth session of Indian Labour Conference reiterated that wage boards should be appropriate machinery for the fixation of wage rates. One more institution which is giving recommendations for the fixation and revision of wages and allowances of Government employees is the Pay commissions. Adjudication has become one of the main instruments for settling wage disputes, improvement in wage scales and standardisation of wages and allowances. Though courts and tribunals were primarily intended to deal with the settlement of industrial disputes, in practice, wage fixation has become an important element in their working and functioning.

8.8 KEY WORDS:

Wage Fixation: Wage and Salaries are determined through several institutions i.e. collective bargaining, legislations, wage boards, pay commission and adjudication.

Wage Boards: The term "Wage Board" covers (i) a voluntary body set up by discussions between organised employers and workers to regulate wages, working hours and related conditions of employment by collect the bargaining. (ii) a body set up by law or with legal authority to establish minimum wages and other standards of employment which are then legally enforceable in the particular trade or industry to which the Board's decision relate.

Pay Commission: The Commission appointed by the Central / State Government for the fixation and recommendation on ages, salaries, Dearness allowance, H.R.A. and benefits.

Adjudication: Adjudication is one of the main instruments for settlement of disputes on wages allowances etc.

Tribunals: The Government shall constitute or setup the tribunals where the dispute or problem is for a state or whole.

8.9. SELF ASSESSMENT QUESTIONS:

1) What are the principles of wage fixation?

2) What are the mechanisms of wage and salary fixation in Industrial Sectors?

3) Any system of wage fixation must be judged by how it works in practice, Discuss.

4) Elaborately discuss the statutory methods of wage fixation.

5) Enumerate the role of pay Commissions and wage boards for the fixation of wage and salaries.

6) Define collective bargaining and explain its importance in wage fixation.

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LESSON 9

COLLECTIVE BARGAINING

9.0 OBJECTIVE

After going through this unit, you should be able to:

- Familiarise yourself with approaches and emerging issues in collective bargaining;
- Examine collective bargaining in Indian context;
- Discern the recent trend and special provisions in collective bargaining.

STRUCTURE

9.1 Introduction

9.2 Approaches to Collective Bargaining

9.3 Emerging Issues in Collective Bargaining

9.4 Collective Bargaining in Indian Context

9.5 Productivity Bargaining

9.6 Collective Bargaining in Public Sector

9.7 Special Provisions in Collective Bargaining

9.8 Summary

9.9 Key Words

9.10 Self-Assessment Questions

9.11 Further Readings

9.1 INTRODUCTION

Collective bargaining is concerned with the relations between management representatives and union representatives. Collective bargaining has been characterised as a form of industrial democracy and industrial government. It involves the process of negotiation, administration, and interpretation of collective agreements covering wages, hours of work, and other conditions of employment for a specific period of time. For some issues, collective bargaining occurs when one party's goals conflict with those of the other party. The style and substance of the negotiations are affected by the legal requirement to bargain in good faith. The final product of negotiation process is a collective bargaining agreement. Effective administration of collective agreement is vital to the health of the union-management relationship. Successful administration of an agreement depends on mutual respect among employees, management and union. Collective bargaining today faces a crisis. Severe environmental pressures, particularly competition and technological change make it increasingly difficult for the parties to reach a mutually satisfactory settlement.

9.2 APPROACHES TO COLLECTIVE BARGAINING

Collective Bargaining

The World Labour Report of ILO (1997-98) mentions that the collective bargaining is

weak as the state intervention plays a crucial role. The system of social dialogue is centralised at the industry or national level and leaves little discretion at the enterprise level. However, a new pattern of unionisation has appeared due to the shift from organising workers in a region/industry to the formation of independent trade unions at the enterprise level. Accordingly, the focus of collective bargaining has shifted from the region/industry level to the enterprise or even plant level.

Industry Bargaining

The industry level collective bargaining is common in the case of core industries in public sector like coal, steel, cement, ports, banks and insurance. The collective bargaining on industry basis is practiced by traditional industry groups like textiles, plantations and engineering in the private sector. The recent trend in the field of collective bargaining in India has been a gradual shift from national/industry level to local level leadership; and enterprise/job level bargaining.

Enterprise Bargaining

The importance of enterprise is growing as a bargaining level as the industry-wide bargaining is losing ground. Even in case of industry-wide bargaining, sufficient scope is offered for enterprise level negotiations. Enterprise level agreements are steadily increasing in number and becoming a point of decision-making. In the industrialised countries, the trend is towards increasing autonomy of enterprises and individualisation of labour relations.

Concession Bargaining

Concession bargaining originated in U.S.A. as a temporary measure to save jobs in the period of economic depression. Concession bargaining was undertaken by the employers to face increased competition and cope up with higher productivity requirements. The trade unions preferred wage cuts or wage moderation to that of job losses and displacement. The trade unions indicated their readiness to accept other options to avoid labour redundancies. Apart from accepting wage reduction, other options considered under concession bargaining were: (a) shorter working hours; (b) freeze on fresh recruitment; (c) restriction on overtime; and (d) training and retraining of workers. In U.S.A. the concession bargaining agreements included wage cuts in case of newly hired workers, curbing the cost of health insurance, and increased compensation for voluntary separation. In India, it has taken the form of downsizing of employees and offering of voluntary retirement schemes.

Composite Bargaining

The contents of conventional bargaining are mainly wages, allowances and benefits, and conditions of work and employment. The composite bargaining calls for a strategic shift from conventional bargaining to include issues like quality of work life, productivity improvement, enhancing of market share or even financial matters. Composite bargaining reflects a change in strategy from confrontation to coordination between management and labour for the promotion of their common interest of survival and progress of enterprises.

9.3 EMERGING ISSUES IN COLLECTIVE BARGAINING

Union and management are going to face many substantive and procedural issues in collective bargaining. Some of the issues can probably be handled at the bargaining table by using existing structures and strategies. Some of the traditionally handled issues are as follows:

Wage Bargaining

Wages will remain at the centre stage of future contract negotiations because the size and security of income will continue to be of vital importance to workers.

Women's Issues

The explosive growth in the number of women employees may give rise to fresh challenges to both employers and unions to squarely face the particular concerns and problems of females on-the-job. That process has been going on for some time now but will probably accelerate in the future as women become firmly and permanently entrenched in the labour force and in the unions. Women issues are going to figure more and more in future collective bargaining.

Job Security

The potential loss of jobs due to technological change has always been a major concern for the unions. Use of automation and computers will expand as Indian companies attempt to increase productivity and remain competitive in domestic and international markets. This will continue in the future and may even accelerate the collective bargaining process.

Productivity

Time has come, according to many economists, for the unions to be vitally concerned with productivity and to realise that employee welfare is tied directly to the success of the enterprise and industry. At the same time, management must recognise that to obtain an increase in productivity, it must seek the co-operation of the employees and the union. In short, what is needed in collective bargaining is re-approachment between union and management that recognises the necessity of co-operating to raise productivity.

Technological Change

Management cannot expect workers and their unions to moderate their wage demands and attitude toward technological change unilaterally. As in every constructive collective bargaining situation, there must be a give and take. Further, the society cannot expect labour to bear the full cost of technological change. It is true that workers will ultimately benefit from a competitive product, but so will management, stockholders, and the consumer. It seems only equitable that all parties bear some of the cost. In Japan and some European countries, technological change is not normally opposed because jobs are guaranteed.

Quality of Work Life (QWL)

The issue of quality of work life is related to the need for organised labour and management to work co-operatively toward the goal of greater productivity. The attention now being paid to the QWL reflects the growing importance being attached to it. It is apparent that a substantial number of employees are unhappy with their jobs and are demanding more meaningful work. Employees are beginning to demand improvements in both economic and non-economic benefits from their jobs. The importance of non-economic rewards is increasing relative to the importance of economic ones, especially among white-collar and highly educated employees. People are demanding greater control and involvement in the jobs. They do not want to be treated as a cog in a wheel. QWL experiments will continue in the years ahead and may eventually provide some impetus to the collective bargaining across countries.

9.4 COLLECTIVE BARGAINING IN INDIAN CONTEXT

Like many other countries, in India, collective bargaining got some impetus from various statutory and voluntary provisions. The Trade Disputes Act 1929, the Bombay Industrial Relations Act 1946, the Industrial Disputes Act 1947, and the Madhya Pradesh Industrial Relations Act 1960, provided machinery for consultation and paved the way for collective bargaining. Among the voluntary measures, mention may be made to the different tripartite conferences, joint consultative machineries, code of discipline, and Central and State Implementation and Evaluation Units. In India, collective bargaining was not very popular till the end of the Second World War. However, there had been a few instances where wages and working conditions were regulated by collective agreements even earlier. The collective bargaining agreements have been concluded at three levels – at plant level, industry level, and national level.

Collective bargaining was traditionally conducted at the plant level as in the case of TISCO, Indian Aluminium Company, and Bata Shoe Company. In some industrial units, detailed grievance procedures have been laid down by mutual agreements. The collective agreement signed between the TISCO and the Tata Workers' Union in 1956 embodies a provision for grievance procedure and closer association of employees with management. The Belur Report of 1958, which is a study by Subbiah, Kannappan and his associates in the Indian Aluminium Company, is one of the best published case studies on collective bargaining in India. It throws light on the factors responsible for creating a favourable bargaining relationship between the management and the union.

The best example of an industry level agreement is offered by the textile industry of Bombay and Ahmedabad. The agreement between the Ahmedabad Millowners' Association and the Ahmedabad Textile

Labour Association, which were signed on June 1955, laid down the procedure to be followed for the grant of bonus and the voluntary settlement of industrial disputes. The practice of industry-wise bargaining continues to prevail in the cotton textile industry in Maharashtra, Gujarat, and Tamil Nadu; in Jute Textiles and in the plantation industry in Karnataka, Tamil Nadu, and West Bengal. In most other industries, particularly in modern industry groups, collective agreements are entered into at the plant or enterprise level. The agreements at the national level are generally bipartite agreements and are finalised at conferences of labour and management convened by the Government of India. The bonus agreement for plantation workers was concluded in January 1956 between the representatives of the Indian Tea Association and the India Tea Planters' Association on the one hand, and the Hind Mazdoor Sabha (HMS) and the Indian National Trade Union Congress (INTUC) on the other. The agreement was about the payment of bonus to about one million plantation workers.

The Employer's Federation of India (EFI) in a study of collective bargaining in its member organisations in the late sixties (published in a monograph in 1970) classified collective agreements into three categories: (i) agreements which have been drawn up after direct negotiations between the parties and are purely voluntary in character for the purpose of their implementation; (ii) agreements which combine the elements of voluntarism and compulsion, i.e., those negotiated by the parties and registered before a conciliator as settlements; and (iii) agreements which acquire legal status because of successful discussion between the parties when the matters in disputes were under reference to industrial tribunal/courts and could be considered sub judice, the agreements reached being recorded by the tribunals/courts as consent awards.

The EFI study covered 109 collective agreements, relating to 77 companies and 11 industrial associations. Results of the study show that the collective agreements have included all levels. Industry-wide agreements were concluded in engineering, textiles, and tea plantations, and plant-wide or company-wide agreements were the norm in most other industries. The EFI study found "two categories of subjects (which) appear to have figured prominently in the collective agreements, one having a direct bearing on the pay packet and the other relating to leisure and leave." Wages, dearness allowance, retirement benefits and bonus (appearing in a majority of agreements) are illustrations of the first category, and annual leave, paid holidays, and casual leave are (included in a smaller but substantial number of agreements) of the second. Out of the 109 agreements analysed, 96 dealt with wages and 50 with bonus. As for the duration of the agreements as many as 49 (i.e. 45 percent) were for a period of 3 years, 18 were for a period of 5 years and only a small number were for a period of less than 2 years. There are 31 agreements, which dealt with the whole range of topics comprising wages, conditions of employment, and fringe benefits. The rest of them covered one or more specific subjects. The study makes the following concluding observations:

"Another notable feature of the agreements under reference, which is of considerable importance for the development and maintenance of harmonious industrial relations, is the recognition of their mutual rights and responsibilities by the representatives of management and employees. Under a number of agreements, the unions have recognised the right of the management among other things, to introduce new or improved methods of production, establish production schedules and standards, and make rules for maintaining discipline and securing effective operation of the plant. The right of the management to discharge workers for just cause, including inefficiency and lack of work, has also been conceded. The managements on their part have recognised the unions as bargaining agents and pledged to desist from unfair labour practices such as interference with the right of the workman to organise and join a union and discrimination against them because of their membership of a union. In the same manner, the trade unions have agreed to follow the constitutional methods as laid down in the grievance procedure to redress the grievances of their members and to desist from indulging in or encouraging unfair labour practices."

A significant development of the 1970s is the emergence of bipartite national industrial committees in certain key industrial sectors such as coalmining, textile, sugar, electrical machinery, steel and cement. These committees comprise representatives of all major trade unions and employers in a given industry, and operate under broad terms of reference, which include a revision of wage structure and conditions of employment. These negotiating committees have covered both public and private sectors. The development of joint negotiating committees is a clear indication of the preference of the parties for collective bargaining over other methods. Although a variety of industries have been covered under this approach, we would confine our examination to two of the most important ones, namely, steel and coal mine.

The new experiment, in the form of bipartite negotiating committees was first pioneered in the iron and steel industry in 1970. Early in that year a Joint Steel Wage Negotiating Committee [later on re-christened as National Joint Committee for the Steel Industry (NJCS)] was formed. The NJCS is composed of representatives of employers and employees. The employers' side is represented by Indian Iron and Steel Company (IISCO) and Tata Iron and Steel Company (TISCO), and from all the public sector steel plants. On the employees' side, there are three members each from the central trade union organisations, namely, the All India Trade Union Congress (AITUC), the Indian National Trade Union Congress (INTUC), Centre of Indian Trade Unions (CITU), and the Hind Mazdoor Sabha (HMS). Till now, the Committee has signed six agreements.

The coalmines in India were nationalised in 1973. There were agitations by the unions prior to 1973 because wage improvements sanctioned by the Coal Wage Board in 1967 had not been implemented by several (private) mine owners and operators. The government was not in favour of appointing another wage board for the industry and felt, instead, that wages and other matters in coalmining should be settled through negotiations and collective bargaining. With this end in view, a Joint Bipartite Committee for Coal Industry (JBCCI) was constituted on August 14, 1973 with union representatives from INTUC, AITUC and HMS, and management representatives from Coal Mines Authority, Tata Iron and Steel Company, and Indian Iron and Steel Company. Subsequently, the committee has signed six bipartite settlements regarding wage revision, working conditions, and other issues relating to coal industry.

The National Commission on Labour (1966-69) reported the existence of collective agreements at all levels. Most of the collective agreements have been at the plant level, though in the important textile centres like Bombay and Ahmedabad, industry-level agreements have been common. Such agreements are also to be found in the plantation industry in the South and in Assam, and in the coal industry. Apart from these, in new industries like chemicals, petroleum, oil refining and distribution, aluminium, manufacture of electrical and other equipment, and automobile repairing, arrangements of settlement of disputes through voluntary agreements have been common in recent years. In ports and docks, collective agreements have been the rule at individual centers. On certain matters affecting all ports, all India agreements have been reached. In the banking industry, after a series of awards, employers and unions are in recent years coming closer to reach collective agreements. On the whole, the record of reaching collective agreements has not been unsatisfactory, though its extension to a wider area is certainly desirable. For promotion of collective bargaining, the commission recommended, among other things, statutory recognition of representative union as the sole bargaining agent.

The following steps may be considered for promoting collective bargaining in our country:

1) Collective bargaining should be declared as an integral part of India's national industrial relations policy. In order to give it a constitutional sanctity, it should be incorporated in the Directive Principles of State Policy.

2) The two relevant instruments setting international standards regarding collective bargaining, namely, Convention 98 concerning the application of principles of the right to organise and to bargain collectively adopted in 1949, and Recommendation 91 concerning collective agreements adopted in 1951, should be ratified/implemented.

3) Collective bargaining should be adopted as a part of the corporate personnel policy in all public sector enterprises, departmental undertakings, and in public utility services.

4) There should be drastic trade union reforms such as: (a) recognition of the majority union as a bargaining agent; (b) development of a trained and educated cadre of worker-leaders through strong, enlightened, responsible and democratic trade unions; and (c) gradual delinking of trade unions from political parties.

5) More emphasis should be given on mutual settlement of industrial disputes through collective bargaining rather than adjudication. A beginning has to be made in this direction by declaring that collective bargaining will acquire primacy in the procedure for settling industrial disputes.

9.5 PRODUCTIVITY BARGAINING

Productivity bargaining has been described as "an agreement in which advantages of one kind or another, such as higher wages or increased leisure, are given to workers in return for agreement on their part to accept changes in working practices or in methods or in organisation of work which will lead to more efficient working. The prime purpose of productivity bargaining is to raise labour productivity and lower unit labour costs. It aims at improving labour productivity, not so much by requiring workers to make greater efforts, but by eliminating the impediments to higher productivity. Moreover, it is an exercise in problem solving and creating new gains for both management and labour. Productivity bargaining is a complex process. It involves lengthy, detailed negotiations about the implementation of a variety of management techniques such as work-study and job evaluation. The content of negotiation is more or less comprehensive in the sense that it includes not only bargaining over earnings but bargaining over other related matters such as reduction in hours of work, introduction or extension of shift working, manning of machines, and the introduction of new payment systems and reallocation of job control.

Productivity bargaining generally occurs at the level of the enterprise or company and covers almost all employees. It can be distinguished from conventional bargaining. The conventional bargaining tends to increase costs. Wage increases which are unaccompanied by productivity increase are inflationary. These wage increases are often reflected in the form of increased prices and in monopolistic industry the increased wage cost of the agreement is passed on to the consumers. The significance of productivity bargaining is three-fold. First, it seems to be more successful in tightening of the pay-productivity link within organisations. Second, it is argued that it opens a whole new source of untapped productivity potential within an enterprise. Third, it provides potential opportunity for improving the climate of negotiation between management and trade union at company or organisational level. Effective productivity bargaining necessitates openness and trust between the parties in the negotiating process. It is one of the most important methods to increase the level of industrial efficiency.

The productivity agreements, which are generally developed by the management and internal union of office bearers and shop floor representatives, leave no meaningful role for the outside union officials. The success of productivity agreement will depend upon how well the workers understand the principles and objectives of the company. There should, therefore, be a communication structure whereby this understanding and cooperation are secure. There should be departmental and plant-wide productivity committees to review the overall progress of production, and make suggestions for removing the hurdles for achieving higher efficiency.

Productivity Agreements

There are a number of industries in India, which have signed productivity agreements.

Many agreements begin with opening paragraphs about productivity, work culture, and the role to be played by the union and the management. The productivity-linked wages settlement by Southern India Textile Association is a unique example of joint agreement of systematic assessment of workloads and the principle of sharing by workers of 50 percent of the savings by the total category of basic workers. Thirty mills were party to the agreement.

The agreement that Bajaj Auto entered into is as follows:

"The Union and the Company agree that in view of the increased competitive environment in the domestic and global markets, the company can survive, let alone prosper, only by gaining competitiveness and improving levels of production, productivity and ensuring better quality in all its operations and activities by means of maximum utilisation of plant, machinery, equipment, human and other resources at its disposal. Therefore, both the parties agree to achieve higher output and man/machine utilisation by continuously reducing cycle time, work simplification, up-to-date maintenance, upkeep of machines and tools, gauges, fixtures, reduction in consumption of consumables and energy, and by use of improved and latest technology. The Union and the Company also agree to ensure continuous improvement in productivity and quality in all the operations of the company."

"The Union agrees that the Company will continue to conduct time studies to decide the rate of production (output rates) and all workmen shall give the production as per the output rates fixed by the Company. The Union also agrees that these output rates may change from time to time, depending on changes in work methods, raw material, jigs, fixtures, etc."

Similar provisions, as shown below, can be found in many productivity agreements signed recently:

"In view of the globalisation of the economy leading to a competitive environment the union and the company recognised the need to improve production and productivity."

"Workers shall extend wholehearted cooperation for optimising performance of the company at all levels."

"Purpose of the agreement is to increase the level of productivity and to improve it further."

"Purpose is to become more versatile, more flexible and more innovative so that the company can be more competitive."

"All the above provisions indicate that both managements and workers are aware of the changed economic environment and the need for working together to enhance productivity."

9.6 COLLECTIVE BARGAINING IN PUBLIC SECTOR

In all literature on industrial relations, collective bargaining is considered as a central place around which other topics comprising industrial relations seem to revolve. There is hardly any qualitative difference between the collective bargaining techniques adopted by the workers in the public sector enterprises and their counterparts in the private sector. But the crux of the problem in the public sector is that with whom do the trade unions negotiate with? The owner of the enterprise is the government. The manager is as much as an employee as any worker and bound by a whole set of rules and regulations and unable to take any decision in the area of industrial relations.

Further, the accumulation of unattended individual grievances fouls up the atmosphere for collective bargaining. In the public sector, the issues taken up for collective bargaining include revision of wages and pay scales, dearness allowance, house rent and other allowances, loans and advances, medical and residential facilities, welfare measures and service conditions. Prior to negotiations, preparations are made in advance, at least a year ahead of the date of expiry of wage agreement. Exercises are carried out to collect voluminous data from within the organisation and many other undertakings. Hike in annual expenditure on account of increase in pay, dearness and other allowances, and fringe benefits are assessed. The organisation's prospects and financial positions are reviewed. Thereafter, a tentative allocation of resources for the ensuing wage revision is made and modalities of extending the benefits are worked out. Attention is then paid to plan the overall strategy and tactics to be employed in conducting the negotiations. In the course of collective bargaining various pressures develop and sometimes, powerful external forces intervene. The negotiations drag on and there is a compulsion to compromise in order to settle the issues by a deadline. The demand for higher wages is seldom made on the basis of higher productivity.

The following features characterise the collective bargaining scenario in public sector:

1) The Government created a special body called the Bureau of Public Enterprises (BPE), which issues guidelines to enterprise managements on a host of matters concerning the management of an enterprise including all aspects of personnel and industrial relations. It also provides guidelines on financial commitments arising out of collective agreements. Invariably, draft agreements between management and union(s) have to be sent to the BPE for approval with or without modifications. Obviously, the delays in processing collective agreements through the BPE undermined the role of enterprise management in collective bargaining.

2) Core sector industries like steel, coal, and ports and docks are characterised by nation-cum-industry-wide bargaining. The steel agreement also covers the Tata Iron and Steel Company, a private sector unit. There is one National Joint Committee for the Steel Industry (NJCS), which enters into an agreement once in three or four years with respective unions of the plants.

3) Public sector is engaged in a wide variety of economic, industrial and trading activities. Some are high-tech and capital intensive (for e.g. computers, electronics, and petrochemicals), while others are labour intensive (coal for instance). Yet, over the years the government has been insistent upon a measure of uniformity in base wage/salary levels and fringe benefits in the entire public sector, irrespective of the nature of industry.

4) Earlier in the public sector, the emphasis was on greater parity across sectors and reducing the gap between the lowest and the highest paid employees. Now the gap is widening. Over 100 out of about 240 public sector companies have not had pay revision since 1992. There is also a trend towards decentralisation of collective bargaining in key sectors, which tends to reduce the power of unions, but makes pay more aligned to enterprise performance.

9.7 SPECIAL PROVISIONS IN COLLECTIVE BARGAINING

Collective bargaining provisions in wage agreements have come to provide an element of contingency based on individual/group/ organisational performance. They are manifested in one way or more of the following ways:

a) Managerial discretion in setting new norms of production/productivity;

b) Proportionate deductions if standard output is not achieved;

c) Two-tier wage agreements;

d) Linking dearness allowance to cost of production rather than to cost of living;

e) Wage cuts/freezes in sick enterprises;

f) Arbitration.

9.8 SUMMARY

Collective bargaining is a dynamic concept. Various types of collective bargaining have been successfully used by both labour and management to respond effectively to the changing demands of workplace functioning and market pressures. Central to the functioning of collective bargaining is the concept of power. At present, there is a definite trend in favour of enterprise bargaining or even workplace bargaining rather than for industry-wide bargaining. The main issue of collective bargaining in India is (a) the mode of ascertaining the majority status of a trade union; and (b) grant of exclusive bargaining rights to the majority union. The labour movement is facing the impact of globalisation, automation, and changing demand patterns as the nation moves toward a service-oriented economy. Such forces have reduced the number of blue-collar, semi-skilled and unskilled workers and increased the number of white- collar, technical, and professional employees. The labour movement must devise organising and bargaining strategies that appeal to these expanding groups. So far unions have generally been unsuccessful in this endeavour. Additionally, the labour movement has to face the growing management opposition to the unions and collective bargaining. To remain competitive in domestic and international market, many companies are taking actions that will either reduce union influence at the workplace or even eliminate the need to deal with a union. However, union co-operation is absolutely essential in all efforts to increase productivity and ensure industrial peace and harmony.

9.9 KEY WORDS:

Collective Bargaining: The relations between management representatives and union representatives.

Quality of Work Life: Employee satisfaction or dissatisfaction with overall conditions of work.

Productivity: A measure of the efficiency of a person, machine, factory, system, etc., in converting inputs into useful outputs.

9.10 SELF-ASSESSMENT QUESTIONS

1. What are the main issues in collective bargaining?

2. What is the recent trend of collective bargaining in India?

3. What are the central issues in productivity bargaining?

4. What are the special features of collective bargaining in India?

5. What are the essential conditions for the success of collective bargaining in India?

6. Collective bargaining in India got some impetus from the various statutory and voluntary measures. Discuss.

9.11 FURTHER READINGS

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LESSON - 10

WAGE COMPONENTS / STRUCTURE

10.0 OBJECTIVE :

After reading this lesson, you should be able to :

- Know the various Components of Wage Structure.
- Understand the importance of Basic Wage.
- Study the Concept of Dearness Allowance and its necessity.
- Visualise Components of Annual Bonus and Benefits.

STRUCTURE :

10.1 Introduction

10.2 Importance of Wage Structure

10.3 Wage Components

10.4 Basic Wage

10.5 Dearness Allowance

10.6 Overtime Payment

10.7 Annual Bonus

10.8 Fringe Benefits

10.9 Incentive System

10.10 Need for sound wage policy

10.11 The Agricultural Wage Structure

10.12 Summary

10.13 Keywords.

10.14 Self Assessment Questions

10.15 Further Readings.

10.1 INTRODUCTION :

Wage structure, according to Prof. Dunlop, “is the complex of rates within firms differentiated by occupation and employees and the complex of inter-firm rate structures”. The concept of wage structure, as such, is a significant aspect of the wage rate analysis. It has no independent reality, nor does it exist in a state of nature. It is an intellectual construct which is useful in thinking about wages and arriving at decisions about them. The essential characteristic of a wage structure is that it moves together in relation to both time and space. But according to Prof. Dunlop, all wage rates do not move together either in the short run or in the long period; and it is also not completely rigid over time. Further, Dunlop states that the general wage level and the wage structure are closely related.

“The wage structure of a plant or an unit, or more broadly, of a national economy can be viewed as a series of wage rates designed to compensate workers for the varying skills and abilities required in the production process”. A significant dimension of wage structure is not only the number of workers at each rate in the scale but also the relative importance of each rate. An analysis of wage structure can be done through internal wage rate comparison of job content and job relationships and external comparison of job rates in the firms to labour market rates.

Annual Wage Supplement

The Annual Wage Supplement (AWS) is commonly known as the 13th month payment. It is a single annual payment to employees that supplements the total amount of annual wage earned by them. Payment of AWS depends on the contractual agreement between the employer and the employee i.e. whether it is provided for in the employment contract or collective agreement. If it is not stipulated in the employment contract, AWS payment is subject to negotiation and mutual agreement between the employer and employee, or the trade union representing the employee.

An employer is not allowed to pay an AWS of more than three months' salary if:

- He/she agreed (either by way of an employment contract or collective agreement) to pay an AWS of up to three months' wages before the commencement of the Employment (Amendment) Act 1988 on 16 August 1988.

  However, the employer can negotiate with the employee, or the trade union representing the employee, to vary the quantum.

An employer is not allowed to pay an AWS of more than one month's wage if he/she:

- Has not paid any AWS prior to 16 August 1988.

If business results are exceptionally poor for any year, an employer may negotiate with the employees, or the trade union representing the employees, to adjust the AWS downwards.

Bonus

Bonus is a one-time payment usually paid to employees at the end of the year to reward them for their contributions to the company. Payment of bonuses is not compulsory. However, it is a contractual obligation for the employer to pay bonus if it is provided for in the employment contract or collective agreement.

Variable Payment

A Variable payment is an incentive payment to employees:

- To increase their productivity; or
- As a reward for their contributions.

The amount of variable payment can be based on trading results, productivity or any criteria as agreed upon between employers, employees or trade unions. Variable payments are not compulsory unless such payment is provided for in the employment contract or collective agreement.

10.2 IMPORTANCE OF WAGE STRUCTURE :

A study of wage structure is important from the academic as well as practical point of view. To understand and appreciate the economics of an industry and in the larger context of a nation, it is essential to have a clear idea of wage structure. The wage structure gives the information regarding all the pay particulars or different components of a job. The job holder or aspirant always compare the wage components with other jobs or similar jobs within or outside the industry. Wage structure is generally the levels or hierarchy of job and pay ranges. It is the interrelationship of the levels of pay for different types of employees.It may mean the way the total wage of a worker or group of workers is composed; for example including such elements as a basic rate, a piecework bonus and other forms of bonus, overtime, etc. It may also mean the established system of pay differentials between groups of workers by occupation or the pattern of differentials on the basis of grade or status.

10.3 WAGE COMPONENTS:

The pay structure of a company depends on several factors such as labour market conditions, company's paying capacity and legal provisions.

Wages: In India, different acts include different items under wages though all the Acts include basic wage and dearness allowance under the term wages. Under the workmen's compensation act, 1923 wages for leave period, holiday pay, overtime pay, bonus and good conduct bonus form part of wages. Under the payments of wages act, 1936, section 2(vi) any awards of settlement and production bonus, if paid constitute wages. Under the payment of wages act 1948, retrenchment compensation payment in lieu of notices and gratuity payable on discharge constitute wages. However the following types of remuneration if paid do not amount to wages under any of the acts.

- Bonus or other payments under a profit sharing scheme which do not form a part of contract of employment.

- Value of any house accommodation supply of light water, medical attendance, travelling allowances, or payment in lieu thereof or any other concession.

- A sum paid to defray special expenses entailed by the nature of the employment of a workman.

- Any contribution to pension, provident fund or a scheme of social security and social insurance benefits.

- Any other amenity or service excluded from the computation of wages by general or special order of an appropriate governmental authority.

- The term Allowances includes amounts paid in addition to wages over a period of time including holiday pay, overtime pay, bonus, social security benefit etc.

The Industrial wage structure in India consists of various components. "Arun Monappa" identified five wage components on the monthly wage package of an industrial worker in India. The Principal wage components are:

1. Basic Wage.
2. Dearness Allowance
3. Overtime.
4. Bonus
5. Fringe Benefits

There are a number of other components also but, they have no direct link with the wage structure of a worker they are generally referred to as perquisites, incentives etc.

We describe below the five principal elements of Indian wage packet. Fringe benefits and incentives have been described in separate lessons.

10.4 BASIC WAGE :

The concept of 'basic wage' is contained in the report of the Committee on Fair Wages. According to this committee, the floor of the basic pay is the "minimum wage". The basic wage has been the most stable and fixed as compared to dearness allowance and annual bonuses which usually change with movements in the cost of living indices and the performance of the industry. The basic wage pattern in industries was set by the industrial tribunals and courts through their awards after the end of the Second World War.

The revisions in the basic wage has become progressively less frequent and insignificant because of the ever growing dearness allowance component. The relative stability in basic wage could be attributed to the industrial tribunals which demonstrated their reluctance to award upward revision in basic wages. For instance, in the case of the Army and Navy Stores Ltd. Bombay Vs. Their Workmen (1951 II LLJ 35), the Labour Appellate Tribunal held that normally, a basic wage once fixed should stand for a reasonable period of time unless some change intervenes. Even when the consumer prices rose and the workers' organisations demanded a revision in basic wages, the tribunals granted them dearness allowance instead leaving the basic wages untouched. Clearly, the basic wage has lost much of its importance in the pay structure.

In some countries, a rise in prices is usually neutralised, not by giving a separate allowance like dearness allowance, but by raising the wages themselves. In our country, the issue of merging a part of dearness allowance with basic wage has been in constant debate for a number of years. Workers' organisations have recognised the increase in importance of the dearness allowance component in the pay packet and have been demanding the merger of this component with basic wages.

The Gadgil Committee (1952) recommended that 50 per cent of the (then) prevailing rate of allowance be treated as pay for purposes of computing pension, provident fund, gratuity, travelling allowance, house rent allowance, and city compensatory allowance. This recommendation was accepted by the Government of India.

There are a number of considerations in the fixation of the basic wage embracing the statutory minimum wage, the awards of Industrial Tribunals, directives of the pay commissions at the national and state levels and collective bargaining.

The basic wage in India corresponds with what has been recommended by the Fair wages committee (1948) and the 15th Indian Labour conference (1957). The various awards by wage tribunals, wage boards, pay commission reports and job evaluation also serve as guiding principles in determining basic wage. While deciding the basic wage, the following criteria may be considered: (1) Skills needed for the job (2) Experience needed (3) Difficulty of work; mental as well as physical (4) Training needed (5) Responsibilities involved (6) hazardous nature of job.

10.5 THE DEARNESS ALLOWANCE (DA) :

The system of 'Dearness Allowance' was used for the first time after First World War, to enable the workers to meet the steep rise in prices of essential commodities such as food stuffs. Although called by various names, the special allowance thus paid aimed at neutralising the high cost of living and protect the real wages of the wage earners. In other words the major purpose of D.A. payment was to provide relief to the workers confronted with inflationary conditions by attempting to offset the cost of living with additional allowance. Usually, the Consumer Price Index (CPI) is used to link D.A. with the cost of living. However, the prevailing practices with respect to the fixation of D.A. across industries, regions, sectors and governmental and private undertakings. As National Commission on Labour (NCL) reports, "In some cases it was linked to the working class Consumer Price Index.. in others it was not. It was at flat rate and was applicable in some cases to all employees irrespective of their wages; in others, it varied according to wage or salary slabs. A graded percentage, linked to wages or salaries, was also prevalent". In view of divergence, the D.A. issue has been usually referred to tribunals and courts for adjudication.

The establishing system of D.A. linked to movement of CPI numbers provides more immediate relief to the workers from the increasing rate of inflation. This system has a built-in mechanism to ascertain the points of neutralisation in terms of fluctuations in the CPI which is related to the cost of basic necessities of life. The correlation between the increase in the number of points of the CPI to the magnitude of money to be paid must be ascertained to settle the DA problem. There are divergent suggestions with respect to the extent of neutralisation. The NCL had recommended that 95 per cent neutralisation should be allowed against rise in cost of living to those drawing a minimum wage in non-scheduled employments. There have also been suggestions to provide maximum (i.e. 100 per cent) neutralisation at lower levels with a gradual tapering off as wage/salary scale improves. Moreover, there has been a great deal of controversy between point-to-point adjustment and adjustment from slab-to-slab. While D.A. can be equated to slab of pay in a way that the lower slabs receive a higher weightage and the higher slabs receive a lower weightage, the size of the slab itself whether it should be 5 points or 10 points is further controversial issue. The Dearness Allowance Commission (1967), also called the Gajendragadkar Commission, felt that the slab system would work better than point-to-point adjustment. The NCL also recommended linkage of DA to a 5 point slab.

Another controversy with respect to D.A. relates to its relationship with capacity to pay. The NCL felt that the capacity to pay was not relevant consideration for payment of D.A. at the minimum level. At other levels or where DA is fixed on the basis of collective bargaining or other methods, the "capacity to pay" may be a relevant consideration.

There is a controversy whether DA has to be fully or partly merged with the basic wage. The merger of full DA or its larger part, with the basic wage is preferred by the workers and their representatives. This arrangement would provide more stability to their pay packets and enable them to enjoy more liberal perquisites in view of increased basic wages or salaries. However, it would increase the wage cost of the employer. Of course, many progressive employers have welcomed the merger of a certain position of DA with the basic wages and salaries of their employees.

It is the allowance paid to employees in order to enable them to face the increasing dearness of essential commodities. It serves as a cushion. A sort of insurance against increase in price levels of commodities. Instead of increasing wages every time there is a rise in price level. DA is paid to neutralize the effects of inflation, when prices go down. DA can always be reduced. This has, however, remained a hypothetical situation as prices never come down to necessitate cut in dearness allowances payable to employees. DA is linked in India to three factors the index factor, the point factor, and the time factor:

- All India consumer price index (AICIPI) The labour Bureau Shimla computes the AICPI base 1960= 100 points) from time to time.
- Time factor: in this case DA is linked to the rise in the All India Consumer Price Index (AICPI) in a related period, instead of linking it to fortnightly or monthly fluctuations in index.
- Point factor: Here DA rises in line with a rise in the number of index points above a specific level.
- Other allowances: the list of allowances granted by employers in India has been expanding thanks to the increasing competition in the job market and the growing awareness on the part of

employees. An illustrative list of allowances are: 1) Attendance 2) Books 3) Car 4) Card (Credit card) 5) City Compensatory 6) Club membership 7) Computer 8) Deputation 9) Driver.

10.6 OVERTIME PAYMENT :

Working overtime in industry is possibly as old as the industrial revolution. In the early days, due to the then existing social order, perhaps the concept of overtime did not exist as there were no defined hours of work. With the passage of time, the government came out with legislation to restrict excessive working by the employees beyond certain limited hours. While the need for such legislation was welcome in situations where labour was exploited, another situation started shaping up in which employees started will fully organising work such a fashion wherein the managements are compelled to give overtime as means of achieving production. During the postwar period, overtime has become quite a regular feature in many industries. The employer began to supplement production.

The payment of overtime allowance to the factory and workshop employees is guaranteed by law. All employees who are deemed to be workers under the Factories Act, 1948 or under the Minimum Wages Act, 1948 are entitled to overtime allowance at twice the ordinary rate of their wages for the work done in excess of 9 hours more than 48 hours in any week. The ordinary rate of wages have been defined as the basic wage plus such allowances, including the cash equivalent of the advantage accruing through the concessional sale to workers of food grains and other articles as the worker is for the time being entitled to, but not including a bonus. Compensatory and house rent allowance as well as the dearness allowance are to be taken into account in computing compensation for overtime work.

There is no uniformity in the period of employment with reference to which overtime is calculated. Where weekly working hours have been prescribed, overtime work is normally computed on a weekly basis. Under the Act, overtime allowance has to be paid on a daily or weekly basis, i.e., for work in excess of hours in a day or for more than 48 hours in a week. The total number of hours of overtime shall not exceed 50 for any period of three consecutive months, beginning on 1st of January, 1st of July, and 1st of October.

There cannot be any compulsion under the terms and conditions to service of the workmen that they should work overtime for any specific number of days in any month. It is not obligatory for any workman to work overtime and the management has also no right to compel a workman to work overtime. Further, overtime work cannot be regarded as either an express of implied term of the contract of employment (Hind Art Press Mangalore V. ESIC and Anr: 1990 II LLJ 195).

The Occupational Wage Survey (1986-87) reveals that out of the five textile industries covered by the survey, overtime was reported in 39 out of 44 occupations in cotton textiles, 41 of 44 occupations in jute textiles, 25 out of 48 occupations in synthetic textiles, 28 out of 38 occupations in woolen textiles and in only 2 occupations out of 33 occupations in silk textiles. About 5 per cent of workers were reported to be working on overtime in the textile sector. As a whole, workers on over time accounted for 3.80 per cent of the total work force in the cotton textiles, 13.47 per cent in the jute textiles, 1.22 per cent in the synthetic textiles, 4.29 per cent in the woolen textiles and 0.13 per cent in the silk textiles.

Analysis of the information on reasons for overtime revealed that 37 per cent of cotton textile units reporting overtime put their workers on overtime to complete time-bound work. Meeting the increased demand for the product was found to be the reason in 16 per cent of units. Shortage of workers was cited as the reason for overtime by 7 per cent of the units. Maintenance and repair work was found to be the reason for overtime in 7 per cent of units. A combination of reasons such as shortage of workers, need to complete time-bound work, meeting the increased demand for the products, urgent loading / unloading work, etc. and other miscellaneous factors contributed to overtime in the remaining 33 per cent of the units.

The Bhoothalingam Study Group has observed, that "excessive overtime can have the effect of distorting the wage structure and even reducing employment, we suggest that, as far as possible, overtime payment should be carefully adjusted to needs and should not be allowed to become systematic". The Fourth Central Pay Commission has also pointed out that the present system of overtime payment in government offices is neither satisfactory nor conducive to efficiency in administration. It has not favoured the present scheme to overtime allowance. On the contrary, the Commission recommended improved work culture among the employees and extended working hours particularly for office staff.

10.7 ANNUAL BONUS :

BONUS SYSTEM IN INDIA :

The term "bonus" is not defined under any enactment in India. The relevant dictionary meaning of the term bonus is "gratuity to workmen beyond their wages". The Bonus Commission has defined it is "sharing by the workers in the prosperity of the concern in which they are employed". In the case of low paid workers such sharing in prosperity "augments their earnings and so helps to bridge the gap between the actual wage and need-based wage". In the opinion of the commission, a properly conceived bonus system which is linked to profit also "imparts a measure of desirable flexibility to the wage structure" and thus, enables the workers to share in the prosperity of the concern without disturbing the underlying basic wage structure.

For quite a long time, bonus was considered as an ex gratia payment made by the employer to his employees with a view to stimulate their extra effort in the production process. Sometimes, it has also represented the desire of the employer annual payment of bonus has become obligatory on the part of the employer under the Payment of Bonus Act, 1965.

STATUS OF BONUS BEFORE THE ENACTMENT :

Historically, payment of "bonus" started probably at the end of World War I, As the Whitley Commission observed, "Suggestions have been made from time to time that the difficulty might be met by the general adoption of profit sharing schemes, but this movement has made practically no progress in India and, in the present stage of industrial development in India, such schemes are unlikely to prove either useful or effective".

During World War II, bonus was considered as a payment made to the workers out of the extraordinary profits earned by the employer. The Indian Labour Conference, 1943 discussed the issue of profit sharing bonus and resolved that, it should be treated separately from the dearness allowance issue and that it had to be settled by employers in consultation with their employees. Although many employers paid bonus voluntarily, several disputes over this issue were referred to adjudication under the Defense of India Rules. The adjudicators felt that labour had a right to share in the increased profits during a particular period. Thus, the claim to bonus was accepted on the basis of justice, equity and conscience. For the first time, Justice M.C. Chagla in the Bombay High Court held that payment of bonus could be demanded by workers as a right in the form of extra remuneration.

COMMITTEE ON PROFIT SHARING :

In response to the Indian Labour Conference, 1948 the Government of India appointed the Committee on Profit Sharing to advise on the principles of determination of : (1) fair wages to labour, (2) fair return on the capital employed in the industry, (3) reasonable reserves for maintenance and expansion of the undertaking, and (4) labour's share of the surplus profits, calculated on a sliding scale normally varying with production, after provision has been made for (2) and (3) above. The committee could not evolve a system through which labour's share of profit could be ascertained on a sliding scale to production. If felt that with a view to promoting industrial peace profit sharing might be experimented in well-established industries including cotton, textiles, jute, steel (main products) , cement, manufacture of tyres and manufacture of cigarettes. It also recommended that the responsibility for ascertaining surplus profits and certifying their disbursement according to law should be laid squarely on the duly appointed auditors of the undertakings. However, the recommendations of the committee could not be implemented, and the profit sharing continued in the form of periodic bonuses awarded by industrial courts and tribunals without any uniform basis.

BONUS COMMISSION :

The Bonus Commission was formed in the year 1960 by the Government of India to examine the issue of profit bonus. The commission endorsed that bonus could be claimed as a matter of right by workers. The major elements of the formula evolved by the commission include: (1) the available surplus, (2) distribution of the available surplus, (3) the system of "set on" and "set off" (4) applications to public sector undertakings which are not departmentally run and which compete with private sector undertakings, (5) exemptions as a result of agreements between parties, (6) concessions for new concerns, (7) mode of payment, and (8) retrospective effect of the recommendations. The Government of India accepted the recommendations of the commission with certain modifications on September 2, 1964. The Union Labour Minister clarified in Parliament on September 18, 1964 in the legislation to be promoted to give effect to the recommendations of the Bonus Commission, suitable measures would be taken to enable the labour to receive the benefits of the existing basis or on the basis of the new formula, whichever was higher.

THE PAYMENT OF BONUS ACT, 1965 :

An ordinance for regulating payment of bonus was issued in May 1965 which was replaced by the Payment of Bonus Act, 1965 in September of that year. The Act has been amended from time to time and provides for the payment of bonus to employees in certain establishments on the basis of profit or on the basis of production or productivity. It extends to the whole of India and is applicable to every factory and all establishments which employed 20 or more individuals on any day in the accounting year. The Act prescribes allocation of 60 per cent of the available surplus for distribution purposes to the eligible employees. However, in respect of foreign companies which do not pay dividends in India, this allocable surplus is 67 per cent. The eligible employees are all employees whose wages or salaries are below Rs.1,600 (at present raised to

Rs.10,000) per month per employees and who are not apprentices. The bonus is paid on the basis of salary or wage earned by the eligible employees which includes dearness allowance but excludes other allowances. As per provisions of the Act, the available surplus for a particular accounting year is calculated by deducting from the gross profits the items embodied in section 6. These deductions include depreciation permissible under the income tax statutes, development rebate or investment allowance or development allowance admissible under the income tax law, direct taxes as specific in section 2(12) of the Act, subject to provisions of section 7 and some additional deductions permissible as per schedule III of the Act.

ELIGIBILITY :

Every employee not drawing salary/wages beyond Rs. 10,000 per month who has worked for not less than 30 days in an accounting year is entitled for the payment of bonus. An employee is considered disqualified for the payment of bonus if he/she is dismissed from service for reasons of fraud, riotous violent behaviour or theft, misappropriation or sabotage. The minimum amount of bonus is computed at the rate of 4 per cent (8.33 per cent after the ordinance of September 23, 1972) of the salary or wage earned by an eligible employee in an accounting year which should not be less than Rs.40 (at present, raised to Rs. 100 for an employee above 15 year of age and Rs. 60 for below 15 years of age). The minimum bonus 8.33 per cent is payable even in the absence of profit. The amount of the maximum bonus has not to exceed 20 per cent of the salary or wage earned during an accounting year. There is also provision for a proportionate reduction in bonus when an employee has not worked for all the working days in an accounting year.

'SET ON AND SET OFF' :

The Act further provides that if in a particular accounting year the allocable surplus is more than the amount of maximum bonus payable to the employees, the excess amount, subject to a limit of 20 per cent of the total salary or wage of the employees employed in the establishment in that accounting year has to be carried forward for being set on in the succeeding accounting year and so on up to and inclusive of the fourth accounting year for the purpose of payment of bonus as per the "fourth schedule". If for any accounting year, there is no available surplus or the allocable surplus is less than the minimum bonus payable, such minimum amount or the deficiency is carried forward for being set off in the succeeding accounting year or so on up to and inclusive of the fourth accounting year. While calculating bonus for the succeeding accounting year, the amount of "set on" or "set off" is first taken into consideration. In establishments which are newly set up, the employees are entitled for bonus from the sixth year provided that the employer earns profit in the proceeding accounting year during which they are entitled for payment of bonus. The bonus has to be paid to the employees within eight months from the close of the accounting year. The Act specifies for deductions of any customary bonus or any advance towards bonus from the bonus amount payable to the employees which is calculated in the same way as provided in the Act.

APPLICABILITY :

The Act applies to all the private sector establishments. In the case of a public sector establishment which computes with the private sector establishments and in which accrued income from sales or service is not less than 20 per cent of the gross income in an accounting year, that particular establishment comes under the purview of the Act and will continue to be so governed even if its income form sales or services falls below 20 per cent thereafter. The employees in non-competitive public sector establishments are excluded from the provisions of the Act which are paying bonus on an ex gratia basis. The central government is now also paying bonus linked with productivity to employees of some of their undertakings including the Railways, Posts and Telegraph, Mints, Ordinance and other defence production establishments as well as ex gratia payment equal to 15 days pay to central government employees.

The Act embodies provisions for recovery of bonus due from an employer, reference of disputes under the Act, and presumption about accuracy of balance sheet and profit and loss account of corporations and companies. The appropriate government may appoint inspectors for the purpose of determining whether or not any of the provisions of this Act have been compiled. There are also provisions in the Act for penalty in respect of contraventions and offences as well as protection of action taken under it. Section 31-A embodies a special provision for the payment of bonus linked with production or productivity. The employees who have entered into an agreement or a settlement with their employer prior to the commencement of the Payment of Bonus (Amendment) Act, 1976, or who have entered into an agreement or settlement with their employer after such commencement for the payment of an annual bonus linked with production or productivity in place of profit bonus as per this Act, can receive bonus under such agreement or settlement. Any such agreement or settlement can neither deprive them of the minimum bonus under section 10 nor entitle them for payment of bonus of more than 20 per cent of the salary or wage earned by them during the accounting year in question.

The Act does not apply to certain classes of persons employed by the Life Insurance Corporation of India, the Indian Red Cross Society, Universities and other educational institutions, the Reserve Bank of India, the Industrial Finance Corporation of India, financial corporations established under the State Financial Corporation Act, 1951, the Deposit Insurance Corporations, the National Bank of Agriculture and Rural Development, the Unit Trust of India and several other organisations specified under section 32 of the Act. The appropriate government may exempt for specified period certain establishments or class of establishments from all or any of the provisions of this Act.

PAYMENT OF BONUS IS STATUTORY :

Bonus payment has become compulsory under the Act and is no more dependent on agreement, freely entered into between the parties involved. In situations where there exist profits, bonus can be designated as profit sharing determined in advance under the law. However, the minimum limit which is compulsorily payable to the employees even by a losing establishment, is definitely not a profit sharing amount. Rather, it has become a part of the wages. Although the Act has benefited a larger portion of workers than had been receiving bonus under the earlier system akin to profit sharing schemes, the payment of bonus has failed to provide stimulation to productivity and improve industrial relations. Rather, it has caused numerous industrial conflicts, litigation and inflation in the country.

10.8 FRINGE BENEFITS :

The remuneration that the employees receive for their contribution cannot be measure by the mere estimation of wages and salaries paid to them. Certain supplementary benefits and services known as “fringe benefits” are also available to them. The characteristics of fringe benefits are:

- These benefits are distinctly additional to the regular wages paid to the workers. As such, they are not provided as a substitute for wages or salaries of the employees.

- These benefits are meant primarily to be an advantage to the employees.

- The advantages accrued to the employees through the provision of fringe benefits are as such they cannot be secured through their own individual efforts.

- Only those benefits fall within the purview of fringe benefits which are or can be expressed in cash terms.

- The scope of fringe benefits is different from that of welfare services. Fringe benefits are provided by the employers alone whereas welfare services may be provided by other agencies as well. Benefits that have no relation to employment should not be regarded as fringe benefits.

Fringe benefits have been classified in several ways. In terms of their objectives, Meggison classifies them into two groups: those providing for employees' security and those purporting to increase employees' job satisfaction causing reduction in labour turnover and improvement in productivity. The former group includes retirement programmes, workmen's compensation, unemployment compensation, social insurance, and other provisions. The latter group incorporates vacations, holidays, sick leave, discounts on company goods and services, and allied tangible and intangible benefits.

Fringe benefits are also categorized as statutory, contractual, and voluntary. Statutory benefits include social security and medical care, unemployment compensation, workmen's compensation, provident fund, and gratuity. The benefits provided by the employers in pursuance of agreements with workers may include dearness allowance, house rent allowance, city compensatory allowance, medical allowance, night-shift allowance, heat allowance, transport, housing and educational allowances. Voluntary fringe benefits which are provided unilaterally by the company include group insurance, death benevolent fund, washing allowance, leave encashment, leave travel concession, conveyance allowance, incentive for family planning, service awards, and suggestion awards.

Currently fringe benefits are a significant part of employee compensation system and the employees tend to take them for granted and do not link these items with wages or income as they do not have any direct bearing on payments. They are no more on the fringe of compensation but form an integral component of individual's earnings involving spiraling costs for the company. However, the fringe benefit system can become effective if attempts are made to gear them to the needs of human resource in organizational settings.

10.9 INCENTIVE SYSTEM:

The term "incentive" has been used in the widest sense of financial motivation. It is used to signify inducements offered to employees to put forth their best in order to maximize production results. Incentives are classified as financial and non-financial. Important financial incentives are attractive wages, bonus, dearness allowance, traveling allowance, housing allowance, gratuity, pension, and provident fund contribution. Some of the non-financial incentives are designation, nature of the job, working conditions, status, privileges, job security, opportunity for advancement and participation in decision making. However, a vast diversity exists in regard to policy and practice of incentive payments. Incentive systems also have been classified into three groups: (1) individual wage incentive plan, (2) group incentive scheme, and (3) organization-wide incentive system.

1. The individual wage incentive plan is the extra compensation paid to an individual over a specified amount for his production effort. Individual incentive systems are based upon certain norms established by work measurement techniques such as past performance, bargaining between union and the management, time study, standard data, predetermined elemental times and working sampling. There are four types of individual incentive systems such as measured day-work incentive wage system, an individual receives his regular hourly rate of pay, irrespective of his performance. Piece-work system form the most simple and frequently used incentive wage. In this, individual's earnings are direct and proportionate to their output. Group plans embody a guaranteed base rate to the workers in which the performance over standard is rewarded by a proportionate premium over base pay. Gains-sharing involves a disproportionate increase in monetary rewards for increasing output beyond a predetermined standard. As the gains are shared with the entrepreneurs, the worker gets less than one per cent increment in wage for every one percent increase in output.

2. The group or area incentive scheme provides for the payment of a bonus either equally or proportionately to individuals within a group or area. The bonus is related to the output achieved over an agreed standard or to the time saved on the job – the difference between allowed time and actual time. Such schemes may be most appropriate where:

- people have to work together and team work has to be encouraged; and
- high levels of production depend a great deal on the cooperation existing among a team of workers as compared with the individual efforts of team members.

3 The organization-wide incentive system involves cooperation among employees and the management and purports to the accomplish broader organizational objectives such as:

- to strengthen loyalty to the company;
- to reduce labour material and supply costs;
- to promote harmonious labour-management relations; and
- to decrease turnover and absenteeism.

One of the aspects of organization-wide incentive system is profit sharing under which an employee receives a share of the profit fixed in advance under an agreement freely entered into. The major objective of the profit sharing system is to strengthen the unity of interest and the spirit of cooperation. Some of the advantages of such a scheme are:

- it inculcates in employees' a sense of economic discipline as regards wage costs and productivity;
- it engenders improved communication and increased sense of participation.

- It is relatively simple and its cost of administration is low; and
- It is non-inflationary, if properly devised.

One of the essentials of a sound profit sharing system is that it should not be treated as a substitute for adequate wages but provide something extra to the participants. Full support and cooperation of the union is to be obtained in implementing such a scheme.

Prerequisites for sound incentive plan

1. Proper climate
2. Co-operative workers
3. Workers participation
4. Scientific standards
5. Simplicity
6. Equitable
7. Flexible
8. Less costly
9. Wide coverage
10. Careful planning
11. Guarantee minimum wages
12. Sufficient incentives
13. Ceiling on earnings
14. Grievance settlement
15. Timely payment
16. Review rates
17. Follow up

10 10 NEED FOR SOUND WAGE POLICY

1. It should be related with productivity
2. It should be related with job requirements
3. Lower cost of production
4. Incentive system
5. Minimum wages
6. Efficiency
7. Difference in wages
8. Flexibility
9. Good relation with trade unions

10.11 THE AGRICULTURAL WAGE STRUCTURE :

The wage structure in agriculture is somewhat different than that of industry. The main difference between them lies in the fact that industrial wages are completely monetized in contrast to agricultural wages which are paid in kind as well.

Another difference is the irregularity of payment of agrarian wages. In industry wages may be paid daily, weekly, fortnightly and even monthly. In agriculture, the casual labourers whether male or female get their wages sometimes daily or by-weekly and sometimes even weekly.

Wage differentials in agriculture, both inter-regional and intra-regional or between men, women and children are more apparent than in the industry. But inter-regional comparisons of wage levels is not easy due to difference in mode of payment and commodity-wise variation in price levels in different regions. In view of these characteristics, the wage structure and agriculture, widely different both in space and time.

The wages are not uniform in all farm operations. A male labourer may receive a little more a day in a certain farm and on a particular season, but at the same time he may get less in other farm operations or in lean or slack season.

The other reasons of wage discrimination as explained by the National Commission on Labour, lay in the poverty and illiteracy of agricultural labour; the causal nature of their employment and their ignorance of the law, all of which apply particularly to women. Because of these handicaps, agricultural labour as a whole and women in particular are not able to employ methods now common to industrial labour to improve their bargaining power. There are considerable disparities in wages between men and women depending upon the region, between crops and the bargaining power of labour. Apart from the differentials in wages for the same jobs, discrimination against women is strengthened by having lower rates for the jobs traditionally performed by women i.e., sowing, weeding, transplanting, winnowing, threshing and harvesting, as against ploughing normally done by men only.

As per the Minimum Wages Act, 1948 minimum wages are to be fixed by State Governments for agricultural labour and the rates are to be reviewed periodically at intervals not exceeding five years. There are still some states which have not brought large areas of agricultural employment within the ambit of the Act. The machinery for the fixation and enforcement of minimum wages is not uniform.

The NCL has criticised the inadequate implementation of the Act. As observed by it, “the fixation of statutory minimum wages by the government has tended to narrow the gap between wages of men and women.” The Commission, however, noted the continuation of wage differentials between men and women, particularly in agriculture. “In the larger sectors where women are employed, viz., agriculture and small industries, evidence shows that in fixing wages rates some state governments have not been free from discrimination against women.”

Being essentially an agricultural operation, the plantation industry attracts Part II of the Schedule of the Minimum Wages Act, 1948. The minimum wages fixed for agricultural workers apply to plantation workers as well. In practice, the workers are mostly paid the minimum wages fixed by the State Government for agricultural workers. However, in Kerala, wages are fixed through negotiated settlements or under conciliation settlements.

10.12 SUMMARY :

The Wage structure is the complex of various components and rates within firms differentiated by occupation and employees and also the complex of inter-firm rate structures. The wage components in wage structure of our country are basic wage, dearness allowance, overtime, bonus, incentives and fringe benefits. Determination of the relative importance of each component in the pay packet is a delicate task. Furthermore, in devising a suitable wage structure, a balance has to be struck among conflicting interests of the employers, the employees and the public. The recent trend in wage structure shows that industrial wages are still low in certain occupations and among certain categories of employees, and they differ from state to state and are moving upward. Hence there is need to review critically the existing wage and salary structure in order to ensure that they are economically viable and consonance with the principles of social justice. Moreover, while formulating a wage structure in a given case, considerations of right and wrong, propriety and impropriety, fairness and unfairness, internal and external pay equity, stability and growth of the industry and the economy, have to be taken into consideration.

10.13 KEY WORDS :

Wage Structure : Wage Structure is the complex rates of wage components of particular job.

Basic Wage : The basic wage is contained in the report of the Committee on Fair Wages, the floor of the basic pay is the minimum wage.

Dearness Allowance : It is an additional payment made by the employer to his employees to compensate them to a certain extent for the raise in the cost of living.

Overtime Payment : Excessive wage/payment for the additional work done than, the regular working hours.

Bonus : The Encyclopedia Britannica has defined bonus as an award in cash or its equivalent by an employer to an employee, for accomplishment of desirable results.

Fringe Benefits : Certain supplementary benefits and services for wages are called fringe benefits.

10.14 SELF ASSESSMENT QUESTIONS :

1. What are the various components of Industrial Wage Structure ?

2. What steps have been taken in revising wage structure in India ?

3. Should wages be adjusted directly as cost of living changes ?

   Why, or Why not ?

4. Examine the status of bonus system before the enactment in India. Why and how can it be linked with productivity in Indian Organisations ?

5. What are the recent trends in payment of bonus in India ?

6. Describe various provisions embodied in the Payment of Bonus Act, 1965 ?

10.15 FURTHER READINGS :

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LESSON - 11

DEARNESS ALLOWANCE

11.0 OBJECTIVE :

After reading this lesson, you should be able to :

- Understand the concept of Dearness Allowance
- Know the Principles, Norms and Recommendations to fix D.A. in India.
- Visualise the various Systems of Payment of D.A. in India.
- Review the Prevalent Practices of D.A. Fixation in Indian Organisations.

STRUCTURE :

11.1 Introduction

11.2 Origin and Coverage of Dearness Allowance

11.3 Principles and Norms of D.A. Fixation

11.4 Recommendations of Committees for Fixation of D.A.

11.5 Systems of Payment of Dearness Allowance

11.6 Payment of Uniform D.A.

11.7 Rate of Neutralisation

11.8 Ceiling on Dearness Allowance

11.9 Merger of Dearness Allowance in Basic Wage

11.10 Prevalent Practices of D.A. Fixation

11.11 Study of Employer Federation of India

11.12 Impact of Dearness Allowance

11.13 Summary

11.14 Self Assessment Questions

11.15 Further Readings.

11.1 INTRODUCTION :

Employees are employed with a particular wage or salary rate. In due course of time due to price increase, the real income of employees goes down. It means with the same level of wages employees are unable to buy goods and services, which they were able to buy before increase in prices. Dearness Allowance (DA) is paid to employees by way of compensating them for the loss of real income caused to them by increase in the cost of living due to increase in prices.

Dearness Allowance is a part of the total compensation an employee receives for having performed his/her job. DA is a cost of living adjustment allowance. It is calculated as a percentage of basic salary to mitigate the impact of inflation on people. Employee receives a basic salary or pension that is then supplemented by housing or dearness allowance, or both. Calculated amount is added to the basic salary along with house rent allowance to get the total salary. Rates vary as per rural/urban areas etc. Pensioners and the family pensioners also granted D.A. against the price rise.

The percentage is reviewed and may be changed on a six-month cycle. Many changes to DA and its computations have occurred over the last 60 years. DA is paid twice each year (January and July) based on a percentage of pay in two specific months. Numbers used to calculate DA include twelve month average of pay and a set index level to get the percentage increase in prices/cost of living. DA is paid on a range of base-pay levels. The DA for central government employees and pensioners increased to 107% from July 1, 2014 onwards.

In our country, at present, there are several systems of paying dearness allowance to the employees to meet the changes in the cost of living. In practice, they differ from place to place and industry to industry. The methods of paying dearness allowance, the first is flat rate, the second is linkage with consumer price index numbers published periodically by the government, and the third is graduated scale according to slabs.

DA calculation sheet

Formula for calculating DA for central government employees after 1.1.2006 is:

- Dearness Allowance %= {(Average of AICPI(Base year 2001=100) for the past 12 months – 115.76)/ 115.76}*100

Formula for calculating DA for central public sector employees after 1.1.2007 is:

- Dearness Allowance %= {(Average of AICPI(Base year 2001=100) for the past 3 months - 126.33)/ 126.33}*100

Dearness allowance with effect from January or July of a particular year in the future, once the AICPI(IW) for a particular month is published by the government, whereas for PSU (Public sector undertaking) employees it is declared quarterly by DPE (Department of Public Enterprise).

Beginning 1 January 1996, the DA is granted to compensate for price increases to which the revised pay scales relate. This will be reviewed twice a year, on 1 January and 1 July.

The following table shows All India Consumer Price Index since 1.1.2006 with Base year 2001=100

Year	Jan	Feb	March	April	May	June	July	Aug	Sept	Oct	Nov	Dec	Average
2006	119	119	119	120	121	123	124	124	125	127	127	127	**123**
2007	127	128	127	128	129	130	132	133	133	134	134	134	**131**
2008	134	135	137	138	139	140	143	145	146	148	148	147	**141.66**
2009	148	148	148	150	151	153	160	162	163	165	168	169	**157**
2010	172	170	170	170	172	174	178	178	179	181	182	185	**175.9**
2011	188	185	185	186	187	189	193	194	197	198	199	197	**191.5**
2012	198	199	201	205	206	208	212	214	215	217	218	219	**209.33**
2013	221	223	224	226	228	231	235	237	238	241	243	239	**232.16**
2014	237	238	239	242	244	246	252	253					

Source: http://labourbureau.nic.in/indtab.html

Pensioners

Both pensioners and their families are granted DA and this continues following reemployment with the Central or State Government, a Government undertaking, an autonomous body or a local body; that is, DA is allowed in addition to a recipient's fixed pay or "time scale". In other cases of reemployment, access to DA is subject to the limit of emoluments last drawn. DA is not allowed during a pensioner's time overseas if employment is undertaken; however, the DA remains accessible to overseas pensioners while the recipient is not employed. From 1 April 1979 to 30 September 1984 there were 28 installments of DA paid to pensioners at certain fixed rates for 13 groups of pension amounts. From 1 October 1984 to date, pensioners are paid DA at a certain percentage of basic pension. The allowance is calculated on the original pension without commutation. From 1 July 1986 the percentage has been revised every 6 months based on the cost of living index .72 to 80 DA may be allowance.

11.2 ORIGIN AND COVERAGE OF DEARNESS ALLOWANCE :

The system of payment of 'Dearness Allowance' is peculiar to India and some Asian countries. In the advanced western countries, employees are generally compensated through periodical salary revisions or salary indexation. Its origin in our country may be traced to the First World War when it was introduced for the first time in the cotton textile industry in Bombay and Ahmedabad, called “dear food allowance”. Ad hoc allowances were paid to employees to compensate the rise in the cost of living.

During the Second World War when the Bombay Working Class Cost of Living Index (base year 1933-34) rose from 105 in August 1939, to 113 in December 1939, the textile workers made a representation to the Provincial Government to undertake immediate legislation for the purpose of raising their wages in proportion to the rise in prices. This demand resulted in the appointment of a Board of Conciliation under the Chairmanship of Sri S.S. Ranganekar, Retired High Court Judge, which in its majority report recommended the payment of ‘Dearness Allowance’ at a flat rate of 2 annas per day with effect from December, 1939 to cover the variations in the cost of living index figure between 105 and 123. The ‘Dearness Allowance’ paid to the employees was not linked to the cost of living index. Later, the then Government of Bombay prevailed upon the mills to pay to their workers dearness allowance at a rate of 1.75 pies per day point rise over 105 during the later period of the war.

In 1946, the Rashtriya Mill Mazdoor Sangh (RMMS), the representative union for the cotton textile industry in Bombay raised a dispute regarding standardisation of wages and dearness allowance. The Industrial Court, Bombay, by its award dated 31st May, 1947 fixed Rs. 30 as the minimum occupational basic wage for mill workers. As regards the demand for dearness allowance, the Industrial Court by its part II award dated 8th April, 1948 decided that the rise in the cost of living over the pre-war level of 105 in the case of employees drawing Rs. 30 per month of 26 working days should be neutralised to the extent of 90 per cent and all employees should be paid dearness allowance at the flat rate.

11.3 PRINCIPLES AND NORMS OF FIXATION OF D.A. :

At the Index No. 279, which was the average for the year 1947, the amount of dearness allowance at 90 per cent neutralisation came to Rs.44/-. The rate of dearness allowance by arithmetical calculation came to 1.9 pies per point rise per day for the cost of living index over 105. This came to be known as Old Textile Dearness Allowance. Dearness allowance payable to the industrial workers was thus, for the first time, linked the consumer price index. The Court also directed that if the cost of living index number reached 325, either party will be at liberty to ask for a revision.

After the Index crossed the figure of 325, the RMMS approached the Industrial Court in September, 1951 for a revision of the rate of dearness allowance. After hearing the parties, the Court gave an award on 9th April, 1953 raising the quantum of dearness allowance by 10 percent for the Consumer Price Index number exceeding 325. The RMMS as well as the Millowners’ Association went in appeal to the Labour Appellate Tribunal (LAT). The LAT by its decision dated January 17, 1955 directed that if the consumer price index exceeds 325, then in addition to the dearness allowance given by the Standardisation Award, the mill workers shall be given percentage increase as shown below :

C.P.I. Number	Increase	Neutralisation Percentage
Index up to 325	Nil	90.00%
For Index between 325 and 335	5%	95.4%
For Index between 335 and 350	7.5%	96.7%
For Index 350 onwards	10%	99%

The rate of dearness allowance at 99 per cent neutralisation came to 2.09 pies per day per point rise over the consumer living index 105. This is what is known as the Revised Textile Dearness Allowance.

In deciding the rate of dearness allowance for Bomaby textile workers, both the Industrial Court as well as Labour Appellate Tribunal took into account the financial capacity of the Bombay Textile Industry at that point of time. It laid down that the near cent percent neutralisation shall be in respect of the minimum wage earner of Rs. 30 p.m. and all workers, irrespective of their basic wage, shall be paid dearness allowance at a flat rate even though it may result in a lower percentage dearness allowance to the higher paid employees.

An additional factor contribution to the extension of the system of dearness allowance during the war period was the awards given by the adjudicators. Faced by the sharp rise in prices and cost of living, undertakings in the textile and engineering industries resorted to the practice of paying additional allowance instead of revising wages to compensate for the rise in the cost of living. Gradually, the payment of dearness allowance became a common phenomenon in most industries, government departments, government undertaking and semi government bodies. This is well borne out by the finding of the occupational wage surveys conducted by the Labour Bureau from time to time.

The practice of paying dearness allowance relates not only to the organised sector but has also been extended to a wide section of industries in the unorganised sector under the Minimum Wages Act, 1948. Though the dearness allowance constitutes an integral part of the wage system, hardly anything is known about the size of expenditure incurred by industries on its payment. The study Group on Wage Policy set up by the National Commission on Labour in June 1967 roughly placed the proportion of dearness allowance to wage bill at about 30 percent. On this basis, the group estimated the total expenditure on dearness allowance in the economy during 1965-66 in the vicinity of about Rs. 1,419 crores out of the total estimated wage bill of Rs. 4,728.43 crores in that year. It is not only that the payment of dearness allowance accounts for a large proportion of the wage bill of companies and the earnings of the employees; but it has also registered a continuous rise over the past many years.

Thus, the system of payment of dearness allowance to offset the decline in the purchasing power of money has become a dominant feature of wage fixation in our country. However, the payment of dearness allowance in our country is not regulated by any law or a set of principles, but it is being included in an ever increasing number of wage fixation in our country. However, the payment of dearness allowance in our country is not regulated by any law or a set of principles, but it is being included in an everincreasing number of wage awards and collective agreements.

11.4 RECOMMENDATIONS OF COMMITTEES FOR FIXATION OF D.A. :

The different aspects of dearness allowance have been examined by several high-powered committees and commissions appointed by the Central and State Governments during the last fifty years. Some of the better known attempts are reflected in the reports of the Gregory Committee (1944), the Committee on Fair Wages (1948), the First Pay Commission (1946-47), the Gadgil Committee (1952), the Second Pay Commission (1957-59), the Das Commission (1964-65), the Gajendragadkar Commission (1967), the Third Pay Commission (1970-73), Rath Committee (1977), the Study Group on wages, Income and Prices (Bhoothalingam Committee) 1978, and the subsequent pay commissions.

The question of framing certain principles to streamline the dearness allowance system was first considered at the 5th session of the tripartite Indian Labour Conference held at New Delhi in September 1943. The Conference favoured the fixation of dearness allowance on a regional basis with reference to cost of living. Following this Conference, the Government of India appointed the Gregory Committee to recommend general principles for the fixation of dearness allowance. This Committee, in its report submitted in 1944, made valuable suggestions on the subject and was the first attempt to put the system of dearness allowance on a more rational basis in the post-war period. The Committee recommended that:

1. The Payment of dearness allowance should be limited to an income level below Rs. 200 per month.
2. The amount of dearness allowance should be fixed in terms of rupees and not as a percentage of actual income. However, as there was disagreement in the Committee as to what income figure the absolute amount of compensation should be related, it suggested two alternatives, namely, (a) either to equate the absolute amount of dearness allowance to full compensation for the weighted average of the earnings of all wage-groups below the weighted average as calculated in (a).
3. The payment of additional dearness allowance should be determined in relation to the cost of living index.
4. There should be a single dearness allowance in each region to which the workers in that region should be entitled.
5. The degree of assistance given towards the increased cost of living should diminish as wages increase above the subsistence level; this result would follow from the adoption of either of the formula mentioned in (2) above.
6. The payment of dearness allowance should be made in such away that it would raise the allowance below the prescribed standard and lead to a check in granting a higher allowance.
7. There should not be an automatic increase in dearness allowance with every small change in the index.
8. There should be only one flat rate of dearness allowance for all workers.

The government, however, did not take any suitable decision on the recommendations of the report.

11.4.1 THE FAIR WAGE COMMITTEE :

The Committee on Fair Wages has accepted the need for provision of dearness allowance in the following terms: "Until the cost of living comes down to the level of 160 to 175 (All India Consumer Price Index), it is clearly necessary for this country to continue to pay dearness allowance to neutralised, wholly or atleast substantially, the increases in the cost of living. The necessity for the continuance of such an allowance has been admitted on all hands".

11.4.2 THE FIRST CENTRAL PAY COMMISSION :

The First pay Commission held the payment of dearness allowance "as a necessity in order to bring the total emoluments to correspond with the present day of cost of living." The Commission opined that the payment of such an allowance was a necessity in the case of lower grades of government servants "whose pay only enables them to live on the marginal level in normal times" and that the "allowance must be so fixed as to neutralise the rise in prices". The Commission thus conceived dearness allowance as being relevant to the needs of the most vulnerable section of the employees.

11.4.3 THE SECOND CENTRAL PAY COMMISSION :

The Second Pay Commission gave the concept of dearness allowance a much wider connotation. It held that dearness allowance is "a device to protect, to a greater or lesser extent, the real income of wage earners and salaried employees from the effect of rise in prices." It however, did not state explicitly, like the First Pay Commission, as to whether the payment of allowance should be confined only to the highly vulnerable sections. The Commission stressed that dearness allowance should be paid only in the case of abnormal rise in prices. It current level of prices does not represent a normal situation and there is a reasonable likelihood of prices coming down. And if the dearness allowance is to be retained, it is necessary to come to a conclusion as to what should be regarded as a stable level of prices, a level with reference to which the basic remuneration can be determined and the dearness allowance adjusted".

11.4.4 THE DEARNESS ALLOWANCE COMMISSION :

The Dearness Allowance Commission (1967) under the Chairmanship of P.B. Gajendragadkar, on reviewing the views of the first two central pay commissions, came to the conclusion that "having regard to its basic character, dearness allowance is applicable to those employees whose salaries are at the subsistence level or a little above it". It observed, "In our opinion, the word 'dearness allowance' primarily suggest and refer to an allowance paid to employees in order to enable them to face the increasing dearness of essential commodities. Besides dearness allowance has always been treated as a temporary expedient by the pay commissions in the past and we think that is its main feature".

11.4.5 NATIONAL COMMISSION ON LABOUR RECOMMENDATIONS :

The National Commission on Labour, however, viewed the concept in a much broader perspective. It held that the purpose of dearness allowance was basically one of enabling "a worker in the event of a rise in cost of living to purchase the same amount of goods of basic necessity as before". It opined that the main function of any dearness allowance as we envisage it, ought to be to provide a desired neutralisation of a temporary or short-period rise in the cost of living" (p.240). This view as shared by the Third Pay Commission which expressed that dearness allowance should be treated as a compensation to the wage-earners and salaried employees against rise in prices over the index level to which the pay structure was related. Accordingly, it suggested a formula which visualised the payment of dearness allowance to all employees except those getting a pay above Rs. 2,250.

11.4.6 BOOTHALINGAM STUDY GROUP :

The Bhoothalingam Committee emphasised the need for a single national corrective formula to compensate for the rise in the cost of essential consumption basket. It arrived at a minimum pay of Rs. 260 for the lowest division clerk in the Central Government as on 1st January, 1973 at the All India Consumer Price Index of 200 (base 1960). The rate of dearness allowance of Rs. 1.30 per point was arrived at for the full neutralisation of a rise in consumer price index over 200. In addition, the industrial tribunals, courts and other wage-fixing authorities have also been actively involved in the examination of various issues related to the determination of scale of compensation and the extent of neutralisation itself.

11.4.7 THE FOURTH CENTRAL PAY COMMISSION :

The Fourth Central Pay Commission, while reviewing the extension of the principle of dearness allowance to higher pay brackets stated", ... The employee should be assured that his emolument will not erode by increases in the cost of living and government will make an effort to provide as much relief as possible when the degree of tolerance is exceeded. Failure to do so will give rise to a sense of insecurity in the employee, for he will not know what the future has in store for him, by dint of factors and circumstances and their inter-play over which he has no control, by way of increase the cost of living by inflation. To save him from that predicament, consumption has to be provided for not only in the present but also in the future ...."

It recommended that the dearness allowance in future is to be paid twice in a year, payable with the salary for March and September. The Commission has suggested under its dearness allowance formula the payment of compensation to the extent of 100 per cent up to the pay level of Rs. 3,500 per month, at 75 per cent for the pay between Rs. 3,501 per month and 6,000 per month, and at 65 per cent for the pay above Rs. 6,000 per month.

11.4.8 FIFTH CENTRAL PAY COMMISSION RECOMMENDATIONS ON D.A.:

The Fifth Central Pay Commission (1994-96), in the context of principles of pay determination, has examined the concepts of inclusiveness, comprehensibility and adequacy, and the parameters of job evaluation, fair comparison, equal pay for equal work, and model employer. The Commission observed that the Central Government can no longer pretend to be a model or even a good employer in the context of other sectors of the economy having forged ahead of it in the matter of compensation package to employees.

The Commission has evolved a strategy on pay determination by applying a number of parameters such as intrinsic value of a job, as shown by the skills, the drudgery, the work environment, the qualification required, the power, the prestige, the perquisites - all the quantifiable and non-quantifiable characteristics which make a job what it is. It has suggested for delinking of pay from rank in the hierarchy, which has been introduced through the assumed progression scheme. The Commission has suggested pay scales merger for civil employees with a result that the total of 51 pay scales which exist today are likely to be reduced to 34.

As far as allowances are concerned, the Commission has noted that the existing formula of differential rates of neutralisation of cost of living through the dearness allowance has operated unjustly against the middle and senior management in Government. The Commission has recommended that inflation neutralisation be made uniform at the rate of 100 per cent at all levels.

The Commission has recommended that pay revision should in future be entrusted to a permanent pay commission. Further, pay should be revised annually as in other countries. As an alternative, it has been suggested that dearness allowance should be converted into dearness pay every time the cost of living rises by 50 per cent over the base level.

11.4.9 SIXTH CENTRAL PAY COMMISSION RECOMMENDATIONS ON D.A.:

The Sixth Central Pay commission was set up by Union Cabinet of India on 5 October 2006 for revising the salaries of central government's employees. The commission was set up under Justice B.N. Srikrishna with a time-frame of 18 months. Other members were Prof. Ravindra Dholakia, Mr. J.S. Mathur and Member-Secretary Smt. Sushama Nath. Report of Sixth Central Pay Commission was submitted to Finance MinisterP. Chidambaram by Justice B. N. Srikrishna on 24 March 2008. The cabinet has approved sixth pay commission recommendations with some modifications on 14 August. Revised pay will be implemented with effect from 01.01.2006 and allowances will be paid with effect from 01.09.2008. The recommendations related to the report were to be implemented prospectively. The report led to a 6% increase in dearness allowance for central government employees from 16% to 22%. It also changed base year for DA calculation to 2001 (base year 2001=100)

11.4.10 SEVENTH CENTRAL PAY COMMISSION RECOMMENDATIONS ON D.A (SUGGESTION FOR DA MERGER WITH BASIC PAY):

The Union Cabinet raised dearness allowance to 100% from 90%, benefiting 50 lakh employees and 30 lakh pensioners.The government has also cleared the way for merger of 50% DA with basic pay by approving it among the terms of reference of the Seventh Pay Commission. An official said now the commission can suggest the merger in its interim report. It added that 50% DA merger with basic pay will roughly increase the gross salaries of central government employees by around 30%. The Cabinet approved the proposal to release an additional installment of DA and dearness relief (DR) to pensioners with effect from January 1, 2014, in cash, but not before the disbursement of the salary for the month of March 2014 at the rate of 10% increase over the existing rate of 90%, said an official statement.Central government employees as well as pensioners are entitled for DA/DR at the rate of 100 per cent of the basic with effect from January 1, 2014, it said.The government has estimated that the combined impact on exchequer on account of both DA and DR would be Rs 11,074.80 crores every year.

11.4.11 THE HIGH POWER PAY COMMITTEE RECOMMENDATIONS :

The High Power Pay Committee appointed to examine the grievances of the employees in certain public sector undertakings, in its report of November, 1988, has dealt with the twin questions, viz., whether the dearness allowance was meant only to off-set the rise in the cost of living or to protect the real incomes of the employees and whether the principle of "equality of sacrifice" required that the real income of only those who are at or near the subsistence or minimum wage level should be protect the purchasing capacity of those at the level of the minimum wage in relation to a certain basket of goods, but an allowance that is meant to protect all categories of employees from an erosion of their wages and salaries due to price increases subsequent to a wage revision. Justice, of course, demands that the minimum wage should be protected from any erosion whatsoever, after it is initially fixed.

11.5 SYSTEM OF PAYMENT OF DEARNESS ALLOWANCE :

It varies from centre to centre, industry to industry, and even within the same centre and industry to industry, and even within the same centre and industry. In most industries it is linked to the consumer price index number. These different system of dearness allowance have come into existence over a period of time during the last four decades as a result of ad-hoc decision taken either in the process of collective bargaining or a awards given by the wage fixing authorities. Some of the dearness allowance payment systems are as follows :

11.5.1 FLAT RATE :

Under this method, a fixed amount, say Rs. 200 per month, is paid to all categories of workers, irrespective of their wage scales. The Gregory Committee (1944) which advocated this system stated that the amount of dearness allowance should be an absolute amount i.e., it should be a fixed amount in terms of rupees (a flat rate). In rejected the idea of an automatic increase with every small change in the index (cost of living). The main advantage of this system is that it is simple and it give greater relief to the low-paid workers.

11.5.2 GRADUATED SCALE :

It is a method of paying dearness allowance on a graduated scale according to slabs. Under this, workers are divided into groups according to different wage slabs. They are paid fixed amounts of dearness allowance on a graduated scale. After a limit, there will not be any increase in the amount of dearness allowance at all, however high the wage rate may be. This method of paying dearness allowance is popular because it is convenient and it is also considered to be equitable.

11.5.3 COST OF LIVING AND CONSUMER PRICE INDEX NUMBER :

The consumer Price Index Number is a system of linking dearness allowance with the cost of living index. In this method, dearness allowance automatically increases and decreases with a rise or fall in the value of money. The Consumer Price Index Number is intended to show, over a period of time, the average percentage change in the prices paid by the consumers belonging to the population group proposed to be covered by the index, for a fixed list of goods and services consumed by them. The average percentage change measured by the index is calculated month after month with reference to a fixed period known as "Based Period'. The index during the base period is taken to be 100 so that the indices for later periods are automatically expressed as percentages of the index of the base period. The dearness allowance is calculated on the number of points by which the consumer price index has risen above the base index.

Movement of Consumer Price Index Numbers determines the nearest approximation of the changes in the cost of living of the workers and these indices are used for wage indexation. On the basis of measurement of relative change in costs at retail prices, of baskets of goods and services consumed by the working class families of industrial workers and rural labour households, the labour bureau compiles (Consumer Price Indices) for industrial workers and agricultural and rural labourers respectively. The consumption pattern of industrial workers is determined on the basis of family income and expenditure surveys conducted by Labour Bureau and that of agricultural and rural labour on the basis of data thrown up by the Rural Labour Enquiry. The CPI numbers for industrial workers on base 1982=100 are compiled on the basis of price data collected from various markets on industrial centres spread over the country. The Consumer Price Index numbers for agricultural and rural labourers on base 1986-87 = 100 (w.e.f. Nov. 1995) are computed with the help of price data obtained from different villages spread over different states. On account of the nature of relevant consumption baskets and the wide gap between the base periods and the two series, the indices did not move in an identical fashion.

The consumer price indices are compiled by the Labour Bureau, Simla based on measurement of relative change in costs at retail prices, of baskets of goods and services consumed by working class families belonging to the industrial and agricultural sectors. The consumption pattern of these segments of workers is determined on the basis of family living surveys conducted by the Labour Bureau. Based on these surveys, consumption baskets or weighting diagrams are prepared as applicable to these workers. The consumer price indices for workers are compiled on the basis of prices collected from different markets spread over in various industrial centres. For agricultural labourers price indices are compiled on the basis of prices collected from different villages spread over in different states. On account of the nature of relevant consumption of baskets and the relevant market prices, generally indices relating to agricultural workers fluctuate more sharply than those concerning industrial workers.

The various studies carried out by the Labour Bureau indicates a variety of scales and rates of dearness allowance which differed widely not only between one centre and another but also between different industries in the centre. The Labour Bureau classified the schemes of dearness allowance under two systems. In the first system, dearness allowance is provided without any linkage to the cost of living (i.e., Consumer Price Index Number). In the second system, the payment of dearness, allowance is linked to the cost of living index number. Generally, these two systems have adopted the methods of : (a) a flat rate; (b) as a specific percentage of basic pay ; or (c) under a formula where the rate of dearness allowance is arranged corresponding to a grade scale of pay.

The classification of schemes according to the method adopted under these two systems as prevalent during the fifties is presented in table 11.1

TABLE 11.2

CLASSIFICATION OF DEARNESS ALLOWANCE

System of Dearness Allowance where it is :

Methods of Dearness Allowance	Linked to CPI Number Numbers	Not Linked to CPI
A) At Flat Rate	Dearness allowance rate per point or slabs of point or slabs of points is fixed : this varies with the variation in points in CPI Number.	A fixed amount is payable per month to employees in all pay groups regardless of variation in CPI Numbers.
B) As a percentage of	Under this method, dearness Pay allowance is fixed as percentage of pay per point or slabs of the CPI Numbers. Under few schemes, this rate diminishes with the rise in the CPI Number.	Dearness allowance rate is prescribed as a percentage of basic pay which varies with pay regardless of variation in CPI.
C) Dearness allowance arranged on a graded scale of pay	Under this method, dearness allowance payment which is arranged on a graded scale of pay consists of two parts, viz. (a) a fixed rate (FDA) usually prescribed at a flat rate which differs with different pay slabs, and (b) a variable dearness allowance (VDA) which is prescribed as a specific percentage of pay and equated to a slab of 5 or 10 points of the CPI Number. Any variation by 5 or 10 points over the CPI slab to which variable dearness allowance rate is equated is compensated by additional dearness allowance which is prescribed as a percentage of basic pay and varying with pay slab. Under this scheme, sometimes minimum dearness allowance payable is indicated.	

Source : Report of the EFI Social and Labour Research Foundation on Dearness Allowance in India: Concept, Practice, and Impact, p.56.

Over the years, the relative importance of the methods mentioned above has undergone a marked change. The Labour Investigation Committee observed that in most cases, dearness allowance was being paid on the healthy principle, namely, "that the allowance is paid at a flat rate irrespective of income or on a regressive scale". It added that "this has resulted in the low-paid categories of workers securing a much larger quantum of relief than high-paid workers".

The study on Industrial Award published in 1951 and updated subsequently also observes that the payment of dearness allowance at a flat rate and unconnected with the cost of living had been widely prevalent in industries. But, nearly two decades later, the Third Occupational age Survey conducted by the Labour Bureau (1974-78) revealed a pronounced shift towards the CPI linked system under which dearness allowance is paid.

The system of dearness allowance without any linkage is now relatively less in vogue, while the system based on linkage has acquired pre-eminence. The growth in the use of the Consumer price Index linked system in the organised segments of industry and services has, however, given rise to a variety of schemes. The survey conducted by the EFI Social and Labour Research Foundation (1987) has disclosed seven variants of the system, including two variants providing for exclusive linkage with Consumer Price Index and three based on a double linkage. These seven variants are classified under four basic categories, namely :

"A" Category. This category consists of schemes belonging to two variants, namely the first, under which dearness allowance is fixed at a single flat rate in rupees per point or slab of points and linked exclusively and directly to CPI (Variant 1) and the second, under which different flat rates linked exclusively and directly to CPI are prescribed for different pay brackets (variant 2).

"B" Category. In this category falls schemes which conform to one specific variant (Variant 3), namely, schemes where dearness allowance consists of two parts, namely (i) an amount representing a fixed sum of dearness allowance (FDA) equated to a certain point or slab or points on CPI and (ii) variable rate of dearness allowance (VDA) meant to provide additional allowance to compensate for a change in every point additional allowance to compensate for a change in every point or slab of points to which FDA is equated. The amount of dearness allowance calculated under this arrangement is usually paid uniformly to all pay groups.

"C" Category. This category consists of schemes where dearness allowance comprising FDA and VDA are arranged on a graded scale in three variants. One variant provides for the fixation of FDA and VDA in rupee terms on a graded scale corresponding to different pay slabs (Variant 4). Under the Second variant, both the FDA and VDA at varied rates are prescribed as percentage of basic pay on a graded scale corresponding to different pay slabs (Variant 5). There is still a third variant (Variant 6) under which only a specific percentage rate of VDA varying with the cost of living is prescribed".

"D" Category. This category covers only one variant which provides for fixation of dearness allowance as a specific percentage of textile scale in vogue in the textile industry.

Both the types of systems, namely, one which is based on the linkage with Consumer Price Index and, the other, without linkage reveal certain merits and drawbacks. Thus, the variants of dearness allowance based on a non-linkage with Consumer Price Index are simple to administer but since they do not provide for adjustment in dearness allowance in relation to Consumer Price Index, they fail to ensure adequate neutralisation in times of price rise due to flat nature of dearness allowance rates.

11.6 PAYMENT OF UNIFORM DEARNESS ALLOWANCE :

The adjudicators have generally favoured the payment of uniform dearness allowance to factory operative and clerical staff when they get the same pay. The Supreme Court of India articulated this principle in following words; "...Time has now come when employes getting the same wages should get the same dearness allowance, irrespective of whether they are working as clerks, or members of subordinate staff or factory workmen. The pressure of high prices is the same as these various kinds of employees. Further, subordinate staff and factory workmen these days are keen to educate their children as clerical staff and in the circumstances there should be no difference in the amount of dearness allowance between employees different kinds getting the same wages. Further, an employee, whether he is of one kind or another, getting the same wage hopes for the same amenities of life and there is no reason why he should not get them, simply because he is, for example, a factory workman though he may be coming from the same class of people as a member of clerical staff"... (Greaves Cotton &Co.v. Their Workmen, 1964-I LLJ 349).

11.7 RATE OF NEUTRALISATION :

The method and extent to which neutralisation in the cost of living should be given have been under constant examination by the industrial tribunals and other wage fixing authorities. The Fair Wages Committee in its report suggested that the lowest categories of employees should be granted compensation to the extent of hundred percent of the increase in the cost of living. Further, it recommended that a lower rate of compensation must be based on salary scales or slabs. The Dearness Allowance Commission set up by the Government of India in 1967 recommended neutralisation at the rate of 90 per cent in the case of the lowest paid Central Government employees.

The National Commission on Labour pointed out that the only purpose of dearness allowance is to enable the worker, in the event of a rise in the cost of living, to purchase the same amount of goods of basic necessity as before. The purpose of neutralisation, therefore, is to ensure that the employee is not worse off by reason of the rise in the prices so far as basic goods necessary for his living are concerned. Since the purpose of neutralisation is to ensure that the employee should be in a position to buy the same basket of goods as before, that purpose would be served effectively by only protecting that portion of the wage against the rise in prices which is necessary to buy the same quantum of basic essentials of life.

The Commission observed that unless monetary wages rise as fast as the consumer prices, it would result in an erosion of real wages. But the extent of this impact will depend on the margin of cushion available at different levels of income. It proposed that neutralisation at the rate of 95 per cent should be granted against a rise in the cost of living to those drawing minimum wage in non-scheduled employments. The Commission, however, observed that this should not be allowed to have any adverse effect on such agreements or on award rates of dearness allowance. The higher rates of neutralisation already achieved should be protected. The wage boards have also considered the question of neutralisation. The extent of neutralisation granted by the wage boards in respect of the lowest paid employees varied from 90 per cent to 100 per cent.

The Third Pay Commission recommended a neutralisation of 95 per cent on the lowest pay of Rs. 185 per month and a decline of Rs. 50 per cent neutralisation in respect of employees drawing up to Rs.1,000 per month and still lower to 22 per cent in case of those drawing up to Rs. 2,250 per men sum.

In a series of decisions, the Supreme Court expressed the view that 100 per cent neutralisation cannot be allowed as it would lead to a vicious circle and add to the inflationary spiral. It was observed that there was no reason why the industrial worker should not make sacrifices like all other citizens. In Clerks of Calcutta Tramways Co. Ltd. v. Calcutta Tramways Co., (1956-II LLJ 450), the Supreme Court observed that in the matter of fixing rates of dearness allowance, the tribunal must keep in mind the rule that, except in the case of the very lowest class of manual labourers whose income is just sufficient to keep the body and soul together, it is impolitic and unwise to neutralise keep the body and soul together, it is impolitic and unwise to neutralise the entire rise in the cost of living by dearness allowance. More so in the case of the middle classes. The same view was expressed in the Hindustan Motors v. Its Workmen (1962-23 FJR 109), and was reaffirmed in Hindustan Times Ltd., New Delhi V. Their Workmen (1963-I LLJ 108). Furthermore, in the case of Kamani Metals & Alloys Ltd. v. Their Workmen (1967-32 FJR 64), it was held that 100 per cent neutraluisation is not advisable as it will lead to inflation and, therefore, dearness allowance is often a little less than one hundred percent neutralisation.

11.8 CEILING ON DEARNESS ALLOWANCE :

In Killick Nixon Case (1975-II LLJ-53), the Supreme Court considered the question of ceiling on dearness allowance. The Court observed.... "We do not wish to lay down as an invariable rule that in all cases there should be a ceiling on dearness allowance. Whenever a case of this nature comes for industrial adjudication, it will always be a delicate task for the Tribunal to strike a balance, keeping in view the above principles, weightage of each one of which being variable according to conditions obtaining. Whether or not there should be a ceiling on dearness allowance in a given case must depend on the facts and circumstances of that case. There can be no inexorable rule in that respect. We have formulated the various principles which must be taken into account by the Tribunal in determining this question, but the most dominant of these must always be that of social justice, for that is the ideal which we have resolved to achieve when we framed our Constitution.

In the case of Workmen of Indian Hume Pipe Company Ltd., Bombay V. Indian Hume Pipe Company Ltd., (1986-I LLJ 520), the Supreme Court held that the theory of ceiling on the quantum of dearness allowance cannot be accepted since under the prevailing conditions, there is no control over the prices of essential commodities and as such a ceiling would not give sufficient cushion when prices of essential commodities continuously rise.

The Division Bench of the Bombay High Court in its decision in the case of Hindustan Lever Mazdoor Sabha V. H.L.L. (1989 II CLR 558) set aside the impugned order of a single judge and the award of the

Tribunal granting a ceiling on dearness allowance and directed the company to continue the existing system of dearness allowance without any ceiling. In this case, the court relied on the Supreme Court decision in the Indian Hume Pipe's Case (1986 I LLJ 520) that if the system of payment of dearness allowance already prevalent in the establishment is more beneficial to the workmen, the same should not be disturbed unless they are compelling reasons to do so. The court has also observed in the same case that when the reference for the change in the system for the payment of dearness allowance is made at the instance of the employer, it is for him to justify the need for such a change. Hence the rational of the decision is that when adjudication bodies and the courts are not called upon to introduce dearness allowance system for the first time but to replace the existing one by a new one, the courts should not replace it by a system which would be less beneficial than the existing one.

The Court came to the conclusion that the existing dearness allowance system of Hindustan Lever Limited does not result in over neutralisation of the cost of living index at any level of the income group. It maintains a tapering scale, though not a steeply declining one. The system also does not result in distortion of total incomes either of the workmen inter se or between the workmen and their superiors, namely, the executive staff. The company does not plead any financial inability. The industry-cum-region formula does not warrant its replacement. There are no other compelling reasons why the existing system which is beneficial to the workmen should be replaced by the new one which is less beneficial to them and which would result in a steep decline in their income they would otherwise gain. It is a well-recognised principle of industrial adjudication that the courts, wage bodies and the industrial adjudicators should not tinker with the existing benefits available to the workmen unless it becomes unavoidable and obligatory to do so. The company has failed to make out any such case.

The respondent -company, with manufacturing units at Bombay and Madras, had provided the slab system of dearness allowance (DA) for its employees under which the DA paid was linked to the cost of living index as well as the basic wage. This double-linked DA scheme was included in various settlements between the respondent-company and its workmen and remained operative for about 30 years. The question arose whether the respondent-company was entitled to restructure the DA scheme by abolishing the slab system and substituting the same by a scheme prejudicial to the workmen on the ground that the slab system has resulted in over-neutralisation thereby landing the workmen in the high-wage island and that the financial position of the company had so much deteriorated that it was unable to bear the burden of the slab system of DA. The Industrial Tribunal, to which the question was referred, by its award abolished the existing slab system of DA and directed that, in future, dearness allowance in the company be linked only to the cost of living index at 33 paise per point over 100 points of the Madras City Cost of Living Index 1936 base.

On appeal to the High Court, a single judge upheld the findings of the Tribunal and dismissed the writ petition filed by the workmen. A writ appeal filed by the workmen was also dismissed by the High Court. On appeal, the Supreme Court held that, having regard to the modern conditions of life, the Industrial Tribunal was not justified in abolishing the slab system of DA which had stood the test of time for almost 30 years and had been approved by various settlements between the parties.

11.9 MERGER OF DEARNESS ALLOWANCE IN BASIC WAGE :

With the accelerated rate of inflation and ever increasing basic wages, the rise in dearness allowance, particularly under the double-linkage system has tended to be highly disproportionate both in relation to the rise in the cost of living and in relation to its relative weight in the basic earnings of employees. This has produced one serious consequence leading to the erosion of differentials between bargainable and non-bargainable category; more so in the case of supervisory and managerial staff who in most industrial enterprises, notably in the private sector, received fixed dearness allowance or no dearness allowance at all.

The question of merger of dearness allowance was considered at some length by the Central Wage Boards and the National Commission on Labour. The Boards were generally anxious to evolve a wage structure by merging a portion of dearness allowance in the basic wage. The first Central Wage Board for the Cotton Textile Industry, for instance, suggested in 1957 the consolidation of dearness allowance with basic wage in each mill at an index which yielded an amount equal to three-fourths of the average dearness allowance of the first six months of 1959. Most other Boards also examined this question, but their recommendations in this regard were influenced by the need to strike a balance between the views of trade unions and management which held contrary views.

Generally, the trade unions favoured the merger on the ground that it would make basic wage realistic in keeping with the improved levels of production and productivity while those representing employers expressed against such merger on the plea that dearness allowance being linked to an external factor like the cost of living, its merger in the basic wage would not reflect the true worth of the skill of workers or the true economic value of their work. Some managements opposed it on the ground that any such merger would upset the incentive schemes in cases where incentive payment was related to basic wages. Additionally, several associations of employers held the view that unless price stability was ensured, such merger would be meaningless because otherwise the basic wage would have to be revised every now and then, thus, raising a hornets' nest of wage disputes. Most Central Wage Boards were in favour of treating the components of basic wage and dearness allowance as one integral whole, but in practice, held them as two distinct components under the influence of opposite pulls and pressures.

11.10 PREVALENT PRACTICES FOR D.A. FIXATION :

The existing system of dearness allowance in the public and private sectors present a bewildering variety of patterns in the matter of linkage to salary, the mechanism of linkage, degree of linkage, periodicity of revision and the extent of neutralisation, both inter-sectorally and intra-sectorally.

For Central Government employees, the dearness allowance formula is based on the recommendations of the Pay Commission. As regards State Government employees, there are varying systems, but, by and large, these systems are based on the Central Pattern.

In the Banking Industry, the clerks and subordinate staff are being paid dearness allowance on the basis of the Desai Award which provided for payment at the rate of 3 per cent for every 4 points rise over 100 in the quarterly average of the All-India Average Working Class Consumer Price Index (1949=100). In respect of sub-staff, they are paid 1.20 per cent 'pay' for every rise of 4 points over 332 in the quarterly average of the All India Average Working Class Consumer Price Index (General) Base 1960=100. In the case of clerical staff, it is 1 per cent of 'pay' for every rise of 4 points over 332 in the quarterly average of the All-India Average Working Class Consumer Price Index (General) Base 1960=100, subject to a maximum of Rs. 15.80 for every four points. In the case of class IV employees, it is 1.2 per cent of the basic pay and the special allowance, it any, for every four points in the quarterly average of the All India Consumer Price Index above 332 points.

In a number of commercial establishments, pharmaceutical and other affluent companies, the slab system of payment of dearness allowance predominates. Such a slab system was first introduced by an award in British Insulate Calendar Cables Ltd., Bombay, in 1949 which was subsequently adopted by a number of concerns. The slab system has been approved by the Supreme Court in Greaves Cotton & Co. v. Their Workmen, (1964-ILLJ 751); and Unichem Laboratories Ltd. v. Their Workmen (1972-I LLJ 576).

The slab system provides for payment of different rate on various slabs. Normally, for the first 100, the rate of variation is 5 per cent, the second, 2 per cent and the third and above, at the rate of 2 per cent of the basic pay. The slab system compensates differentially at different salary levels and the dearness allowance payable to the employees under the scheme is substantially high. Originally, the scheme applied to the clerical staff, but because of the decision of the Supreme Court in the case of Greaves Cotton, the scheme has been extended to other categories of employees on the principle that there should be no discrimination in the matter of payment of dearness allowance. One of the most glaring faults in the system is that it often permits more than 100 percent neutralisation, contributing to inflation. The fact that the slab system provides 100 per cent neutralisation was obvious from the decision of the Supreme Court in the case of Shri Chalthan Vibhag Khand Udyog Sahakari Mandali Ltd. V. G.S. Barot, Member, Industrial Court, Gujarat (1980-40 FLR 458).

Example of calculation and expected DA increase from 2013

Calculation of DARates

- DA rates for Government employees are to be announced half yearly which will be applicable from first January and first July.

- On implementation of Sixth Pay Commission recommendations with effect from 01.01.2006 a new method of calculation of DA (dearness allowance) rates is adopted by Central (including Railways)and State Governments.

- DA rates are fixed on the basis of All India Consumer Price Index (AICPI) for industrial workers with Base year as 2001.

Method of DA calculation using the following formulae:

➢ **Dearness Allowance = (Avg of AICPI for the past 12 months – 115.76)*100/115.76 (Fractions are ignored)**

Example: **To calculate Jan 2013 DA rate Price index average from Jan 2012 to Dec 2012 is taken.**

AICPI data for Jan 2012 to Dec 2012 as per Labour Bureau, Department Statistics, Government of Indiais as follows:

Jan-12	198
Feb-12	199
Mar-12	201
Apr-12	205
May-12	206
Jun-12	208
Jul-12	212
Aug-12	214
Sep-12	215
Oct-12	217
Nov-12	218
Dec-12	219
Total	2512
Average	**209.33**

Source: Indian railway employee

Dearness allowance (01.01.2013) = (209.33-115.76)*100/115.76=80.83

- **DA (after ignoring fraction)=80 %**
- **So Rate of DA expected from 01.01.2013 is 80 %**
- **The rate of increase will be 8% (72% to 80%).**

11.11 STUDY OF THE EMPLOYERS' FEDERATION OF INDIA :

The Employers' Federation of India (FFI), in its study entitled "Dearness Allowance : Principles, Practices and Problems" (Monograph No. 19 on 1975), had disclosed that the methods followed by the industrial organisations belonged to the four main types as follows: (i) Dearness allowance computed according to changes in the consumer price index; (ii) Dearness allowance linked to pay slabs and to consumer price index; (iii) Dearness allowance paid at a flat rate and not linked to the consumer price index; and (iv) Dearness allowance prescribed in relation to graduated pay scales. The study shows that there are a number of agreements and awards bearing clauses on dearness allowance.

The study has brought into sharp focus the several weaknesses in the system of dearness allowances. According to it, the compulsion of paying progressively higher dearness allowance has proved injurious to industrial growth and stability. The study further point out that the automaticity of payment of dearness allowance, being linked to the consumer price index, and its lack of relationship with either productivity or paying capacity of the industry, cannot be considered altogether wholesome for the growth and stability of the industry. The study criticises the dearness allowance system on grounds of methodology adopted for the computation and payment of dearness allowance. The problem, according to it, is not only economic, but also technical. The disparity in the rates of allowance, it alleges, can only be explained by a lack of uniformity in the method and procedures utilised for their computation.

11.12 IMPACT OF DEARNESS ALLOWANCE :

The different systems of dearness allowance have created disparities in the dearness allowance payment. The contributing factors are its automatic linkage with the consumer price indices; payment on point-to-point basis; cent-per-cent neutralisation and sometimes even more; absence of any ceiling, wide diversities in the rates prescribed by industrial tribunals or settled in collective agreements. In the process, the fundamental and sound principles governing wage fixation, viz., productivity of labour; prevailing rates of wages in the same or similar occupations in the neighbouring localities; level of national income and its distribution; place of industry in the economy of the country; and capacity of the industry to pay have been completely ignored.

The payment of dearness allowance linked to consumer price index is highly injurious to the financial stability of the industry as it ensures automatic increase in the compensation to employees without any corresponding increase in productivity. The existing system of dearness allowance payment has no relation whatsoever with productivity, profitability or paying capacity of the industry. As employees receive automatic rise in their pay, they tend to show indifference to the need to improve their performance and productivity. It is conductive to inflation as, by raising the wage costs, it gives further fillip to the price rise, thus giving rise to the wage-price spiral. Augmentation in the money earnings brought about by its payment has proved to be a potential source of demand-pull and cost-push inflation in our country. Further, it serves as a great disincentive to highly skilled workmen due to the narrowing down of wage differentials.

In some cases, supervisory and middle management cadre often draw less emoluments than those to whom they supervise and manage. Such disparity in the levels of remuneration tends to create a sense of general discontent with the wage system. Furthermore, the system has contributed to disparity in the earnings between workers engaged in the organised and unorganised sectors. The main reason for this being its widespread adoption in the former and its restricted use in the latter. In brief, the payment of dearness allowance has distorted the wage structure and has contributed in no small measure to the galloping inflation.

In view of the adverse effects produced by the dearness allowance system on the operation of the industry, various suggestions have been put forward for its reationalisation. Firstly, the present practice of dearness allowance should be discontinued altogether and the same is to be substituted by a system of consolidated wages by merging a portion of the dearness allowance with the basic wages. Secondly, the slab system should be discontinued and instead a per point index system to be adopted wherein the question of imposing a ceiling on dearness allowance would not arise. Thirdly no dearness allowance should become payable as soon as the total wages of an employee exceeds a particular amount, say, Rs. 3,000 per month. Fourthly, adjustment of dearness allowance should be made on the basis of the average variation in the Consumer Price Index at the interval of every six months to prevent sharp changes in the dearness allowance payment. Fifthly, one single rate of dearness allowance should be paid uniformly to all employees regardless of their pay. Sixthly, instead of the point-to-point adjustment, dearness allowance should be adjusted for a variation of 10 points (1960-100) as it is only a substantial increase in the price level that needs to be adjusted. Seventhly, the dearness allowance should be linked to a recent base year to avoid distortions in payment. Lastly, a proper scheme should be devised for supplementing the payment of dearness allowance with the provision of a network of fair price shops with essential supplies.

11.13 SUMMARY :

In the ultimate analysis, the problem of spiraling dearness allowance is basically the problem of controlling the increase in the prices of food and other essential consumer goods. Unless and until the prices of these commodities are stabilised, it is not possible to find any satisfactory solution to the problem. Tying of compensation to consumer prices by the unions and other groups in society would lead to a vast engine of inflation, which, once it began to roll, would continue to gain speed. It is most desirable that government should adopt appropriate measures and policies to control inflation as far as possible. Furthermore, a proper wage policy dovetailed with a integrated type of income and price policy assumes paramount importance in the national economy of our country against the backdrop of future economic and industrial perspectives. To put the system of dearness allowance on sound lines, it is desirable to bring out the necessary reformation, rationalisation and reorientation.

11.14 SELF ASSESSMENT QUESTIONS :

1) Define Dearness Allowance, discuss its importance in India.

2) Briefly describe Principles and Norms of D.A. and Various Committees Recommendations on D.A.

3) What are various systems of Dearness Allowance, Discuss.

4) Examine the Prevalent Practices of D.A. in Indian Industries.

5) For the Calculation of D.A. the Consumer Price Index Numbers are necessary, Give your opinion.

6) What is the concept of D.A. ? What are the methods adopted for computing the cost of living index for neutralisation ?

11.15 FURTHER READINGS :

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LESSON-12

FRINGE BENEFITS

12.0 OBJECTIVE:

After reading this lesson, you should be able to:

- Understand the Concept of 'Fringe Benefits'.
- Describe the importance and need of Fringe Benefits in the Organization.
- Study the different types of Fringe Benefits practicing in the Organization.
- Visualize the Perspectives on Fringe Benefits in India.

STRUCTURE:

12.1 Introduction

12.2 Concept of Fringe Benefits

12.3 Objectives of Fringe Benefits

12.3.1 Social Goal

12.3.2 Human Relations Goal

12.3.3 Macro Economical Goal

12.4 Nature and Significance of Fringe Benefits

12.5 Types of Fringe Benefits

12.5.1 Payment for Time Not worked

12.5.2 Employee Security

12.5.3 Safety and Health Benefits

12.5.4 Welfare and Recreational Facilities

12.5.5 Old age and Retirement Benefits

12.6 Perspectives of Fringe Benefits in India: The view points of M. Chandra

12.7 The Findings of Laxmi Narain

12.8 The View Point of National Labour Law Association on Social Security in India

12.9 Summary

12.10 Keywords

12.11 Self assessment Questions

12.12 Further Readings

12.1 INTRODUCTION:

The primary effect of fringe benefit type of compensation is to retain the employee in the organization on a long term basis. There is little or no evidence that the tremendous variety of supplementary pay plans often termed fringe benefits served to motivate employees to higher productivity. In a study of 550 white collar employees, it was concluded that the average employee was aware of about one half of the supplementary pay programme feature- this despite an unusually comprehensive and active programme of communication with respect to employee benefits available. One of these firms' most costly and widely publicized benefits - a disability wages was essentially unheard of by 60% of those responding to the questionnaire. When asked if they felt that they knew enough about these plans over three quarters replied that they did. In a second study in another company 249 new hires were queried concerning their knowledge of benefits explained during a comprehensive induction programme. A correlation between knowledge and attitude towards the company's fringe benefit programmes proved to be quite low. Despite the absence of motivational affects employee benefit programme make up a significant portion of most personnel department budgets. Therefore it should be a major concern in any organization to make their employees abreast about the fringe benefit programmes in order to motivate them and thereby improving the status of their organization.

Management is concerned with attracting and keeping employees, whose performance meets at least minimum levels of acceptability, and at keeping 'absenteeism' and 'turnover' to tolerable levels. The provision of 'benefits' and 'services' are important in maintaining the employees and reducing or keeping turnover and absenteeism low.

The term "fringe" was for the first time used by the War Labour Board to apply to the minor benefit awards. Employees were allowed to pay employees for vacations, holidays, sick leaves, work clothes, eating time, transportation, insurance protection, pension programmes and allied issues. At that time, these additional compensations did not form an important component of employees' income and accordingly were designated as "fringe benefits". However, at present these payments are a significant part of the 'Employee Compensation Management".

TERMINOLOGY AND MEANING

The benefits usually provided by employer to employees are known as 'fringe benefits' as they are offered to the employee as a 'fringe'. Different terms have been used for these benefits, such as "Fringe Benefits", "Welfare Expenses", "Wage Supplements", "Sub wages" or "Social Charges", :Perquisites other than wages" or Transpecuniary Incentives' the other terms used are: "Extra Wages" "hidden payroll" "Non-Wage Labour Costs" or "Selected Supplementary Compensation Practices". It is difficult to define what a fringe benefit is, for there is no agreement among the experts on its precise meaning, significance or corporation. The chief area of disagreement is between "wages" and "fringe" on the one hand and between "fringes" and "Company Personnel Services" on the other. There are also differences on whether the benefits which have been usually provided for should be included among the "fringes".

Contribution of Other Factors on The Concept of 'Fringe Benefits'

For instance,

(i) Rising prices and cost of living has brought about incessant demand for provision of extra benefits to the employees.

(ii) Employers too have found that fringe benefits present attractive areas of negotiation when wage and salary increases are not feasible.

(iii) As organizations have developed more elaborate fringe benefits programmes for their employees, greater pressure has been placed upon competing organizations to match these benefits in order to attract and keep employees.

(iv)Recognition that fringe benefits are non-taxable rewards has been a major stimulus to their expansion.

(v) Rapid industrialization, increasingly heavy urbanization and the growth of a capitalistic economy have made it difficult for most employees to protect themselves against the adverse impact of these developments. Since it was workers who were responsible for production, it was held that employers should accept responsibility for meeting some of the needs of their employees. As a result, some benefits-and-services programmes were adopted by employers.

(vi) The growing volume of labour legislation, particularly social security legislation, made it imperative for employers to share equally with their employees the cost of old age, survivor and disability benefits.

(vii) The growth and strength of trade unions has substantially influenced the growth of company benefits and services.

(viii) Labour scarcity and competition for qualified personnel has led to the initiation, evolution and implementation of a number of compensation plans.

(ix) The management has increasingly realized its responsibility towards its employees and has come to the conclusion that the benefits of increase in productivity resulting from increasing industrialization should go, at least partly, to the employees who are responsible for it, so that they may be protected against the insecurity arising from unemployment, sickness, injury and old age. Company benefits-and-services programmes are among some of the mechanisms which managers use to supply this security.

A “tripartite” concept of individual protection has developed in recent years. First, every individual is expected to be at least partially responsible for his own present and future well-being. Second, industry is now expected to protect its workers from the hazards of life. Finally, the government is involved in supporting and financing worker assistance programmes. The contribution of these three parties varies in accordance with the nature and purpose of the various employee benefits-and services programmes.

A number of factors influence the decision to set up a particular employee benefits and services programme. According to Nielson, the criteria governing such a programme are:

(a) Cost;

(b) The ability to pay;

(c) The needs of the employees;

(d) The bargaining strength of the trade union;

(e) Tax considerations;

(f) Public relations;

(g) Social responsibility; and

(h) The reactions of the employees.

The following table summarizes the factors, key forces and their potential impact on benefits:

Table 12.1
Factors Likely to Shape Future Benefits and Their Relative Impact

Relative Impact of Forces on Benefits		
Some	**Moderate**	**Strong**
1. Better labour-force education 2. Growth in white-collar versus-blue-collar occupations 3. Relative growth of minorities and increased participation in work force 4. Growth in relative youthfulness of work force 5. Growth in female component of work force 6. More technological changes 7. More urbanization	1.Rise in individual influence 2. Extension of unionization, new unions 3. Medical advances (e.g. transplants, life extension) 4. Participative planning with institutional members	1. More leisure time, vacations, holiday 2. Pressure from established unions 3. New public welfare programme 4. Minority, frustrations and Pressures.

12.2 CONCEPT OF 'FRINGE BENEFITS':

The Glossary of Current Industrial Relations and Wage Terms have defined fringe & benefits as "supplements to wages received by workers at a cost to employers. The term encompasses a number of benefits-paid vacation, health and insurance plans tec. Which usually add up to something more than a "fringe" and is sometimes applied to a practice that constitutes a dubious benefit for workers".

International Labour Organization has defined "fringe benefits" as under : Wages are often augmented by special cash benefits, by the provision of medical and other services, by the provision in kind that form part of the wage for expenditure on the goods and services. In addition workers commonly receive low-rent housing etc. Such additions to the wage proper are sometimes returned to as fringe benefits.

"Belcher" defines these benefits as "any wage cost not directly connected with the employees, productive effort, performance, service or sacrifice; according to Employer's Federation of India "fringe benefits" include payments for non—working time, profits and bonus, legally sanctioned payments on social security schemes, workmen's compensation, welfare cess, and the contribution made by employers under such voluntary schemes as cater for the post retirement, medical, educational, cultural and recreational needs of workmen.

The term also includes the monetary equivalent of free lighting, water, fuel, etc. Which are provided for workers, and subsidized housing and related services. "Cockman" views employee benefits as "those benefits which are supplied by an employer to or for the benefits of an employee, and which are not in the form of wages, salaries and time-rated payments.

We may define 'fringe benefits' thus: Fringe benefit is primarily a means in the direction of ensuring, maintaining and increasing the income of the employee. It is a benefit which supplements to a working ordinary wages and which are of volume to them and their families in so far as it materially increases their relation.

12.3 OBJECTIVES OF FRINGE BENEFITS AND SERVICE PROGRAMMES:

An organization designs and established a benefit and service programme to achieve the following objectives:

a) To keep in line with the prevailing proactive of offering benefits and services which are given by similar concern.

b) To recruit and retain the best personnel/Human Resources.

c) To provide for the needs of employees and protect them against certain hazards of life.

d) To increase and improve employee morale and create a helpful and positive attitude on the part of workers towards their employers.

e) To make the organization a dominant influence in the lives of its employees with a view to gaining their loyalty and co-operation, encouraging them to greater productive efforts;

f) To improve and furnish the organizational image in the eyes of the public with a view to improving its market position and bringing about product acceptance by it;

g) To recognize the official trade union's bargaining strength, for a strong trade union generally constrains an employer to adopt sound benefits and service programme for their employees.

In other words, fringe benefits satisfy three goals viz.

12.3.1 SOCIAL GOAL:

Human Resource is the most precious of all resources. In other words of the Philadelphia Charter, 1944 of ILO; "Labour is not a commodity. It is entitled to a fair deal as an active participation in any programme of economic development and social reconstruction."

Article 43 or the Constitution of India Provides:

"……all workers should be given a living wage condition of work ensuring decent standard of life and fuller employment of ensure social and cultural opportunities".

The fringe benefits act as a social lever in helping conservation of this precious resource, by guarding against its unnatural erosion and providing the climate for its development in a working environment.

12.3.2 HUMAN RELATIONS GOAL:

The management, through motivation, tries to develop and maintain "human relations' i.e., mutual interest', individual differences, motivation and human dignity. The management provides with an environment which will reasonably the economic, social and psychological needs of the employees so that their co-operation could be obtained and productivity of the organization enhanced.

12.3.3 MACRO-ECONOMICAL GOAL:

F or maintaining the growth of and stability in the economy of a country, ideal utilization of the non human and human resources is imperative. Fringe benefits do provide protection, during periods of contingencies of life, for training and development of the employees, and for good working condition and assistance to supplement their main in came, opportunities afro social interaction through cultural, recreational facilities etc.

12.4 NATURE AND SIGNIFICANCE OF FRINGE NENEFITS:

The literature does not provide any uniform definition of the concept "fringe benefits". However, as Megginson lucidly observes, the concept is so broad that it can embrace form regular employment at fair wages to the payment of tuition for employees pursuing, management courses or from a wide safety programme to athletic activities or from free meals to free medical or legal assistance. In addition, there is divergence of opinion as to what items should be included in these systems. While on the one hand, attempts are made to exclude workmen's compensation, suggestion awards and allied items, on the other hand, shift differentials, overtime premium pay and allied payroll items are included in these systems. Indeed, the inclusion of specific items in these systems relates to one's viewpoint.

Thus, the employer while providing such benefits takes into account something of value which increases the actual or potential income of employees by the magnitude of the contribution. However, the employees tend to take them for granted and do not link these items with wages or income as they do not have direct bearing on payment. Indeed, some types of fringe benefits, even if considered as wage are not visualized as a substitute for a basic, satisfactory in the form of social obligations or legal bindings upon the company which the employers have to provide as their responsibility, and employees have to obtain as their right. Furthermore, the employers are increasingly inclined to the view or afford to pay their part of the contribution. Again, the management regards these benefits as a burden on the company.

12.5 TYPES OF FRINGE BENEFITS:

Benefits consist of items or awards which are supplementary to normal pay. Some – such as pensions and sick pay - are essential entitlements, so the common term 'fringe benefits' is perhaps misleading.

Certain provisions of the maintenance of adequate standards of living have been underwritten by the state, which has legislated for employees and employers alike to, bear some of the cost. They are awarded to anyone who meets certain qualifying conditions and as such are independent of the employer's discretion and performance considerations. Other benefits such as cars, medical insurance and 'perks', are more in the nature of optional extras and as such may be part of the recruitment retention and incentives strategies of the organization.

The National Association of Manufacturers has indicated the following classification of fringe benefits

(a) Premium Payments for the period of time a worker has worked; for example, payment on daily or weekly basis, holidays, overtime pay, shift differentials, the cost of living bonus, bonus in lieu of vacation.

(b) Payment for special duties, such as working on grievance redressal procedures and labour contract negotiations.

(c) Payment for health and security benefits: These include retirement plans, social security payments, savings plans, profit-sharing plans, group life insurance, medical, surgical and hospital insurance, accident and sickness insurance, supplemental employment benefits, payments under the Workmen's Compensation Act, disability insurance, old age and survivor insurance, and unemployment compensation.

(d) Payment for time not worked, which includes payment for sick leave and for time during which an employee is under medical care, payment for holidays, vacations, witness time, voting time, excused absence, lunch periods, rest periods, work-up time, reporting pay, severance pay, payment for call all time, call-back time, dressing time, portal-to-portal time and wet-time.

(e) Payment for employee services, including cafeteria subsidies, union credit, house financing, parking space operations, etc.

(f) Other expenditure, such as that incurred on making Christmas gifts or offering Christmas bonus, on educational reimbursements, employee uniforms, work clothes, safety equipment or allowance, laundry allowance, supper money or meal allowance.

Organizations provide varieties of fringe benefits. The United States Chamber of Commerce includes five categories of services and benefits under the term fringe benefits. These are:

i. Legally required payments – old age pension, survival benefits, disability pension, health insurance, unemployment insurance, separation pay, and payments made under Workmen's Compensation Act.

ii. Pension and group insurance and welfare payments

iii. Paid rest periods, waste-up time, lunch periods.

iv. Payment for time not worked – vacation and holidays.

v. Festival Bonus

"Dale Yoder" and Paul D. Standohar Classified the Fringe Benefits fewer than four heads as given under:

i) For Employment Security: Benefits under this head include unemployment insurance, technological adjustment pay, leave travel pay, overtime pay, leave for negotiation, leave for maternity, leave for grievances, holidays, cost of living bonus, call-back pay, lay-off pay, retiring rooms, jobs to the sons/daughters of the employees and the like.

ii) For Health Protection: Benefits under this head include accident insurance, disability insurance, health insurance, hospitalization, life insurance, medical care, sickness benefits, sick leaves etc.

iii) For Old age and Retirement: Benefits under this category include, deferred income plans, pension, gratuity, provident fund, old age assistance, old age counseling, medical benefits for retired employees, travelling concession to retired employees, jobs to sons/daughters of the decreased employee and the like.

iv) For Personnel Identification, Participation and Stimulation: This category covers the following benefits: Anniversary awards, attendance bonus, canteen, cooperative credit societies, educational facilities, beauty parlor services, housing, income tax aid, counseling, quality bonus, recreational programmes, stress counseling, safety measures etc.

Robert H. Honge Classified the Fringe Benefits as follows:

1. Payment for time not worked:

Benefits under this category include: Sick leave with pay, vacation pay, paid rest and relief time, paid lunch periods, grievance time, bargaining time, travel time etc.

2. Extra Pay for time worked:

This category covers the benefits such as: Premium pay, incentive bonus, shift premium, old age insurance, profit sharing and unemployment compensation, Christmas bonus, Diwali or Pooja bonus, food coat subsidy, housing subsidy, recreation etc.

The following classification of fringe benefits is adopted for discussion about the fringe benefits in India (See Chart 12.1).

12.5.1 PAYMENT FOR TIME NOT WORKED:

This category includes: a) Hour of Work, b) Paid Holidays, c) Shift Premium, d) Holiday Pay and e) Paid Vacation.

a) **Hour of Work:** Section 51 of the Factories Act, 1948, specifies that no adult worker shall be required to work in a factory for more than 48 hours in a week. Section 54 of the Act restricts the working hours to 9 in a day. In some organizations, the numbers of working hours are less than the legal requirements.

b) **Paid Holidays:** According to the Factories Act, 1948 an adult worker shall have a weekly paid holiday. When a worker is deprived to weekly holidays, he/she is eligible for compensatory holidays of the same number on the same month. Some organizations allow the workers to have two days as paid holidays in a week.

c) **Shift Premium:** Companies operating shifty system, pay a premium to the workers who are required to work during the odd hours shift.

d) **Holiday Pay:** Generally, organizations offer double the normal rate of the salary to those workers, who work on paid holidays.

e) **Paid Vacation:** Workers in manufacturing, mines and plantations who worked for 240 days during a calendar year are eligible for paid vacation at the rate of one day for every 20 days worked in case of adult workers and at the rate of one day for every 15 days worked incased of child workers.

12.5.2 EMPLOYEE SECURITY:

Physical and job security to the employee should also be provided with a view to promoting security to the employee and his family members. The benefit of confirmation of the employee on the job creates a sense of job security. Further, a minimum and continuous wage or salary gives a sense of security of the life. The Payment of Wages Act, 1936, The Minimum Wages Act, 1948, The Payment of Bonus Act, 1965, Provide income security to the employees.

a) **Retrenchment Compensation:** The Industrial Disputes Act, 1947 provides for the payment of compensation in case of lay-off and retrenchment. The non-seasonal industrial establishments employing 50 or more workers have to give one month's notice or one month's wages to all the workers who are retrenched after one year's continuous service. The compensation is paid at the rate of 15 days wage for every completed year of service with a maximum of 45 days wage in a year; Workers are eligible for compensations stated above even in case of closing down of undertakings.

b) **Lay-off Compensation:** In case of lay-off, employees are entitled to lay-off compensation at the rate to 50% of the total of the basic wage and dearness allowance for the period of their lay-off except for weekly holidays. Lay-off compensation can normally be paid up to 45 days in a year.

12.5.3 SAFETY AND HEALTH BENEFITS:

Employee's safety and health should be taken care of in order to protect the employee against accidents, unhealthy working conditions and to protect worker's capacity. In India, the Factories Act, 1948, stipulated certain requirements regarding working conditions with a view to provide a safe working environment. These provisions relate to cleanliness, disposal of waste and effluents, ventilation and temperature, dust and fume, artificial humidification, over-crowding, lighting, drinking water, public utility and spittoons. Provisions relating to safety measures include fencing of machinery, work on or near machinery in motion, employment of young person's on dangerous machines, striking gear and devices for cutting off power, self-acting machines, easing of new machinery, probation of employment of women and children ear cotton openers, hoists and lifts, lifting machines, chains, ropes precautions against dangerous fumes, explosive or inflammable dust, gas etc. Precautions in case of fire, power to require specifications of defective parts of test of stability, safety of buildings and machinery etc.

a) **Workmen's Compensation:** In addition to safety and health measures, provision for the payment of compensation has also been made under Workmen's Compensation Act, 1923. The Act is intended to meet the contingency of invalidity and death of worker due to an employment injury or an occupational disease specified under the Act at the sole responsibility of the employer. The Act covers the employees whose wages are less then Rs. 500 per month. Amount of compensation depends on the nature of injury and monthly wages of the employee. Dependents of the employee are eligible for compensation in cases of death of the employees.

b) **Health Benefits:** Today, various medical services like hospital, clinical and dispensary facilities are provided by organizations not only to employees but also to their family members.

In order to protect the employees' health, the companies provide the facilities for physical exercises, sports and games.

Employees State Insurance Act, 1948, deals comprehensively about the health benefits to be provided. This Act is applicable to all factories, establishments running with power and employing 20 or more workers. Employees in these concerns and whose wages do not exceed Rs. 1000 per month are eligible for benefits under the Act. Benefits under this Act include:

(i) **Sickness Benefit:** Insured employees are entitled to get cash benefit for a maximum of 56 days in a year under this benefit.

(ii) **Maternity Benefit:** Insured women employees are entitled to maternity leave for 12 weeks (six weeks before the delivery and six weeks after the delivery) in addition to cash benefit of 75 paise per day or twice sicken benefit, whichever is higher.

(iii) **Disablement Benefit:** Insured employees, who are disabled temporarily or permanently (partial or total) due to employment injury and/or occupational diseases are entitled to get the cash benefit under this head.

(iv) **Dependent's Benefit:** If an insured person dies as a result of an employment injury sustained as an employee, his dependents that are entitled to compensation under the Act shall be entitled to periodical payments referred to as dependent benefit.

(v) **Medical Benefit:** This benefit shall be provided to an insured employee or to a member of his family where the benefit is extended to his family. This benefit is provided in the following forms:

- Out-patient treatment or attendance in a hospital, dispensary, clinic or other institutions; or
- By visits to the home of the insured person; or
- Treatment as in-patient in a hospital or other institutions.

An insured person shall be entitled to medical benefits during any week for which contributions are payable, or in which he/she is eligible to claim sickness or maternity benefits or eligible for disablement benefit.

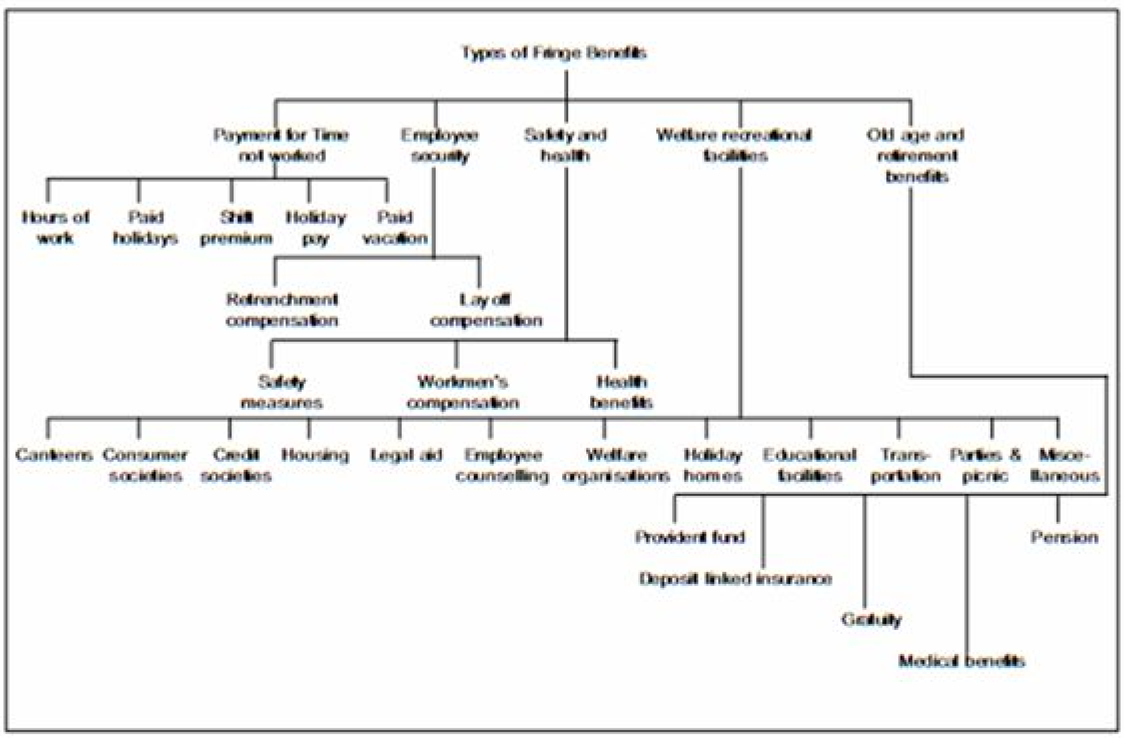
c) **Voluntary arrangements:** However, most of the large organizations provide health services over and above the legal requirements to their employees free of cost by setting up hospitals, clinics, dispensaries and homeopathic dispensaries. Company's elaborate health service programmes include.

(i) Providing health maintenance service, emergency care, on-the-job treatment care for minor complaints, health counseling, medical supervision in rehabilitation, accident and sickness prevention, health education programme, treatment in employee colonies etc.

(ii) Medical benefits are extended to employee's family members and to the retired employees and their family members.

(iii) Small organizations which cannot set up hospitals or large organization (in those where hospitals cannot be set up because of various reasons) provide the medical services through local hospitals and doctors. Sometimes, they provide the facility of reimbursement of medical expenses borne by the employees.

Chart No: 12.1. Types of Fringe Benefits



12.5.4 WELFARE AND RECREATIONAL FACILITIES:

Welfare and recreational benefits include : a) Canteens; (b) Consumer societies; (c) Credit societies; (d) Housing; (e) Legal aid; (f) Employee counseling; (g) Welfare organizations; (h) Holiday homes; (i) Educational facilities; (j) Transportation; (k) Parties and picnics and (l) Miscellaneous.

(a) Canteens: Perhaps no employee benefit has received as much attention in recent years as that of canteens. Some organizations have statutory obligation to provide such facilities as Section 46 of the Factories Act, 1948, imposes a statutory obligation to provide canteens in factories employing more than 250 workers. Other has provided such companies provide lunch rooms when canteen facilities are not available.

(b) Consumer Societies: Most of the large organizations located far from the towns and which proved housing facilities near the organization set up the consumer stores in the employees colonies and supply all the necessary goods at fair prices.

(c) Credit Societies: The objective of setting-up of these societies is to encourage thrift and provide loan facilities at reasonable terms and conditions, primarily to employees. Some organizations encourage employees to form cooperative credit societies with a view of fostering self-help rather than depending upon money lenders, where as some organizations provide loans to employees directly.

(d) Housing: Of all the requirements of the workers, decent and cheap housing accommodation is of great significance. The problem of housing is one of the main causes for fatigue and worry wrong employees and this comes in the way of discharging their duties effectively. Most of the organizations are located very far from towns where housing facilities are not available. Hence, most of the organizations built quarters nearer to the factory and provided cheap and decent housing facilities to their employees, whilst a few organizations provided and/or arrange for housing loans to employees and encourage them to construct houses.

(e) Legal Aid: Organizations also provide assistance or aid regarding legal matters to employees as and when necessary through company lawyers or other lawyers.

(f) Employee Counseling: Organizations provide counseling service to the employee regarding their personal problems through professional counselors. Employee counseling reduces absenteeism, turnover, tardiness etc.

(g) Welfare Organizations and Welfare Officers: Some large organizations set-up welfare organizations with a view to provide all types of welfare at one centre and appointed welfare officers to provide the welfare benefits continuously and effectively to all the employees fairly.

(h) Holiday Homes: As a measure of staff welfare and in pursuance of government's policy, a few large organizations established holiday homes at a number of hill stations, health resorts and other centers with low charges of accommodation, so as to encourage employees use this facility for rest and recuperation in a pleasant environment.

(i) Educational Facilities: Organizations provide educational facilities not only to the employees but also to their family members. Educational facilities include reimbursement of fees, setting up of schools, colleges, hostels providing grants-in-aid to the other schools where a considerable number of students are the children of employees. Further, the organizations provide reading rooms and libraries of the benefit of employees.

(j) **Transportation:** Companies provide conveyance facilities to their employees form the place of their residence to the place of work as most of the industries are located outside the town and all employees may not get quarter facility.

(k) **Parties and Picnics:** Companies provide these facilities with a view to inculcating sense of association, belongingness, openness, and freedom among employees. These activities help employees to understand other better.

(l) **Miscellaneous:** Organizations provide other benefits like organizing games, sports with awards, setting up of clubs, community services activities, Christmas gifts, gifts for Diwali and other festivals, birthday gifts, leave travel concessions and awards, productivity/performance awards etc.

12.5.5 OLD AGE AND RETIREMENT BENEFITS:

Industrial life generally breaks the family system. The saving capacity of the employee is very low due to lower wages, high living cost and increasing aspirations of the employees and his family members. As such, employers provide some benefits to the employees, after retirement and during old age, with a view to create a feeling of security about the old age. these benefits are called old age and retirement benefits. These benefits include: (a) Provident Fund; (b) Pension; (c) Deposit Linked Insurance; (d) Gratuity and (e) Medical benefit.

(a) **Provident Fund:** This benefit is meant for economic welfare of the employees. The Employee's Provident Fund (Family Pension Fund and Deposit Linked Insurance) Act, 1952, provides for the Institution of Provident Fund for employees in factories and establishments. Provident Fund Scheme of the Act provides for monetary assistance to the employees and/or their dependents during post-retirement life. Thus, this facility provides security against social risks and this benefit enables the industrial workers to have better retired life. Employees in all factories under Factories Act, 1948, are covered by the Act. Both the employee and the employer contribute to the fund. The employees on attaining 15 years of membership are eligible for 100% of the contributions with interest. Generally, the organizations pay the Provident Fund amount with interest to the employee on retirement or to the dependents of the employee contributions to the Provident Fund to the tune of 1.5% of employee wage.

(b) **Pension:** The Government of India introduced Employees Pension Scheme for the purpose of providing Family Pension and Life Insurance benefits to the employees of various establishments to which the Act is applicable. The Act was amended in 1971 when Family Pension Fund was introduced in the Act. Both the employer and the employee contribute to this fund. Contributions to this fund are from the employee contributions to the Provident Fund to the tune 1.5% of employee wage.

Employee's Family Pension Scheme 1971 provides for a Family Pension to the family of a deceased employee as per the following rates:

This scheme is also for the payment of a lump sum amount of Rs. 4000 to an employee on his retirement as retirement benefit and a lump sum amount of Rs. 2000 in the event of death of an employee as life insurance benefit.

Table No: 12.2

Pay for Month	Rate
Rs. 800 or more	12% of the basic subject to a maximum of Rs. 150 as monthly pension.
More than Rs. 200 but less than Rs. 800	15% of the basic subject to a maximum of Rs. 96 and a minimum of Rs. 60 as monthly pension.
Rs. 200 or less monthly	30% of the basic subject to a maximum of Rs. 60 as pension

(c) **Deposit Linked Insurance:** Employees Deposit Linked Insurance Scheme was introduced in 1976under the Provident Fund Act, 1952. Under this scheme, if a member of the Employees Provident Fund dies while in service, his dependents will be paid an additional amount equal to the average balancing during the last three years in his account. (The amount should not be less than Rs. 1000 at any point of time, Under the Employees' Deposit Linked Insurance Schemes, 1976, the maximum amount of benefit payable under the deposit linked insurance is Rs. 10000.

(d) **Gratuity:** This is another type of retirement benefit to be provided to an employee either on retirement or at the time of physical disability and to the dependents of the deceased employee. Gratuity is a reward to an employee for his long service with his present employer.

The Payment of Gratuity Act, 1972, is applicable to the establishment in the entire country. The Act provides for a scheme of compulsory payment of gratuity by the managements of factories, plantations, mines, oil fields, railways, shops and other establishments employing 10 or more persons to their employees, drawing the monthly wages of Rs. 1600 per month.

Gratuity is payable to all the employees who render a minimum continuous service of five years with a present employer. It is payable to an employee on his superannuation or his retirement or on his death or disablement due to accident or disease. The gratuity payable to an employee shall be at the rate of 15 days wage for every completed year of service on part thereof in excess of six months. Here the wage means the average of the basic pay last drawn by the employee. The maximum amount of gratuity payable to an employee shall not exceed 20 months wage.

(e) **Medical Benefit:** Some of the large organizations provide medical benefits to their retired employees and their family members. This benefit creates a feeling of permanent attachment with the organization to the employees even while they are in service.

12.6 PERSPECTIVE ON FRINGE BENEFITS IN INDIA:

When the Employers' Federation of India conducted a study of fringe benefits in this country, it was revealed that, in 1960,981 companies, which were included in the survey, paid a little over Rs. 2,148.3 million in wages and fringe benefits, and that the latter was about 21.3 per cent of their total wage bill in that year.

The fringe benefits were high in the mining (24.84 per cent of the wage bill) and plantations industries (24.3 per cent of the wage bill), and were comparatively low in the manufacturing sector (19.99 per cent of the wage bill). In each of these three sectors, however, variations were considerable. In the mining industry, the percentage of fringe benefits varied from 24.5 to 27.88, while in the manufacturing sector it varied between 13.42 and 32.11, followed by the cigarette industry (31.42) and aluminum, brass and copper industries (30.56).

A break-up of fringe benefits by types revealed that, of the total amount paid on fringe benefits, that which was paid for the time not worked and for profits and bonus was the highest, accounting for a little more than 9 per cent of the total wage bill. Payments which had to be made under legislative enactments were between 6.1 per cent and 7.5 per cent of the total, while voluntary welfare schemes accounted for 5.36 per cent of the wage bill.

In the plantation industry, however, these welfare schemes formed 9.4 per cent of the wage bill, while in the other two (mining and manufacturing industries), they respectively accounted for 4.12 per cent and 3.4 per cent of the total wage bill. A considerable proportion of fringe benefits was in the shape of monetary bonus and constituted about 5 per cent of the wage bill. The bonus was of various kinds - profits bonus, attendance bonus, service bonus, gratuity payments, etc. The quantum of the bonus varied from sector to sector.

Payments for Time not worked:

These payments were fairly substantial in the manufacturing industry (5.35 per cent), the mining industry (4.81 per cent) and plantations (3.24 per cent). In the manufacturing sector, the percentage of expenditure on this item varied between 3.06 and 10.42.

Industries which spent a relatively large sum on this item were cigarette manufacturing and distributing (10.42 per cent), petroleum refining and selling (7.15 per cent), chemicals and allied industries (7.11 per cent) and shipbuilding (6.60 per cent).

Statutory Fringe Benefits

These benefits are generally social security, and include gratuity and pension payments, the employer's contribution to the employees' provident fund account and health insurance scheme.

The employers' contribution to statutory provident fund constitutes by far the largest item of expenditure, accounting for 4.23 per cent of the total wage bill in the plantations, mining and manufacturing industries put together.

The expenditure on employees' state insurance contributions by the manufacturing industries was 0.36 per cent, while that on gratuity account was 0.59 per cent.

The "other expenditure" incurred under statutory regulations and tribunal awards was on compensation paid to workers, welfare-cess payments in the coal mining industry and on the supply of protective clothing in the plantations industry. The expenditure on maternity clothing in the manufacturing and mining industries.

Voluntary Benefits

Retirement benefits, medical care, compensation for injuries and disablement, subsidized food and housing, educational and cultural facilities, payment on life insurance premium, the maintenance of canteens, cafeterias, assistance to co-operative societies - these are some of the benefits accounted for 9.40 percent of the total wage bill in the plantations industry against 3.74 per cent and 4.12 per cent in the mining and manufacturing industries respectively.

The social security benefits voluntarily provided by companies include provident fund, gratuity and pension. The medical assistance schemes voluntarily provided by employers were the largest single item of expenditure, and accounted for 1.80 per cent of the total expenditure of 5.36 percent voluntarily incurred by them.

The plantations industry spent 4.78 per cent of its total wage bill on this particular voluntary service against only 0.84 per cent spent by the manufacturing industries. The latter's expenditure on canteens, however, was about 0.70 per cent of its total wage bill against that of 0.07 per cent spent by the mining industries.

In the manufacturing industries, nearly two-thirds of the benefits were in the form of profit and bonus, of payments for time not worked and of contributions by employers to social security benefits. In the plantations and mining industries, however, this percentage was 57 and slightly more than 50 respectively.

Apart from the general fringe benefits for employees, there was a wide range of other benefits as well. Some of these benefits are: Rifle allowance to watchmen, cycle allowance to peons, free driving licenses for drivers, compensation for a waiting period of three days, free quarters, water and electricity; free uniforms to certain categories of employees, conveyance allowance when no transport is provided by the company, travel concessions, assistance to buy spectacles, provision of snacks during night shifts, shoe allowance of 20 paise and an allowance of 37 paise per hour if a worker attends education classes; sale of company products at concessional rates, benevolent fund assistance if a worker is struck down by tuberculosis or cancer, scholarships to employees' children; employees' tours of government projects, study leave, gift of a wrist watch after a meritorious service of ten years, presents to employees on the occasion of their marriage, co-operative bank facilities, festival allowance, free libraries and facilities for inpatient hospital accommodations.

12.6.1 THE VIEWPOINT OF M. CHANDRA:

Chandra lucidly describes fringe benefits provided by the employers to their employees under the statutory provisions or on a voluntary basis. The social services provided under the Factories Act, 1948, in the manufacturing industries include canteen, rest shelters, crèche, storage or lockers, sitting arrangement, bathing and washing facilities, overtime payment and appointment of welfare officer etc. Other benefits provided to the workers include festival, year-end profit sharing, attendance and production bonuses, protective equipments, free supply of uniforms, soda water, sap, cigarette, gur, hair oil, food articles and allied items supplied on concessional rates. Social security system provides benefits such as provident fund, employees' state insurance (ESI) scheme retrenchment compensation, lay-off compensations, employment injury compensation, maternity benefits, and benefits for occupational diseases, gratuity, pension dependent allowance and contribution toward pension and gratuity claims.

In addition, other facilities enjoyed by the workers include medical and health care, restaurant and other food services, cooperative credit societies and consumer stores, company housing, house rent allowance, recreational and cultural services, ladies club, cash assistance to employees at the time of the death, birth, marriage, prolonged sickness, accident, fire, flood and allied items. Again, there are arrangements for adult literacy, vocational training and for education of workers' children. Several employers run primary schools, middle schools and high schools providing books, scholarships to poor and meritorious students. Some employers provide transport facilities (free or subsidized) from home to work place and back. Some employers make advances for the purchase of conveyance. Likewise, in mining industries the Mines Act, 1952 and the rules framed there under impose a statutory obligation on the management to provide several amenities under health, safety and welfare programmes. The Plantation Labour Act. 1951 and rules framed there under make it obligatory on the part of employers to provide many benefits to the workers. Some of the employers' organizations also provide various social services to their employees.

Numerous methods are being adapted for financing social services such as through cess or levy on production, allocation of a fixed percentage of the wage bill by employers, bipartite contributions, tripartite contribution and government contribution. Again, social services are also financed by welfare funds created at industry, state and enterprise levels. Explicitly, as Chandra concludes, fringe benefits provided in large establishments in different industries compare favorably with those provided in many advanced countries. However, the workers in the unorganized sector and small and medium-sized establishments in the organized sector and deprived of these services.

12.7 THE FINDINGS OF LAXMI NARAIN:

In conjunction with the above fringe benefits for workers the general perspective on social security and perquisites for managers, there exist a number of security programmes for workers. Indeed, in India social security legislation is quite comprehensive, Even before Independence, Workmen's Compensation Act, 1923 and Maternity Benefit Act, 1941. Were in operation in several states. The Workmen's Compensation Act, 1923 which has been amended several times purports to impose an obligation upon the employers to pay compensation to the workers receiving injury arising out of and in the course of employment resulting in total or partial disablement for a period exceeding three days. The Act embraces all workers whose wage does not exceed Rs. 1000 per month, excluding casual worker. There exist four central acts providing for maternity benefits to women workers, including the Mines Maternity Benefit Act, 1941, the plantations Labour Act, 1951, the Employees State Insurance at 1948, and the Maternity Benefit Act, 1961.

The Maternity Benefit Act, 1961 which has been passed to provide uniform standards for maternity protection, operatives since November 1, 1963 in every establishment which is a factory, a mine or a plantation to which the provisions of the Employees State Insurance Act are not applicable. In addition, several Acts have been passed by the state governments. Thus, along with the central Maternity Benefit Act, 1961 which provides for the payment of a medical bonus of Rs. 25, some state acts also provide for additional benefits such as free medical aid, maternity bonus, and provision for crèches. Additional rest intervals, etc. Payments under these acts are made by the employers. The period of rest for which payment is made is frequently eight months.

The Employees State Insurance Act, 1948 forms a significant part of social security legislation in India and is administered by a corporation embodying representatives of employers, employees, the medical profession, the central and state governments and Parliament. The Act applies to employees whose total monthly remuneration does not exceed Rs. 1600 to whom it provides for free medical treatment in cases of sickness and employment injury, free maternity care for women employees, cash disablement benefit in the case of employment injury, life pension in the case of permanent disablement and pension for the family or dependents of decreased in the case of death. The scheme is financed by a fund raised room contributions collected from employees and employers and grants from the central and state governments. The Act is limited to perennial factories as defined under the Factories Act, 1948, using power and employing 20 or more persons. However, the government is empowered t extend its application to any other industrial, commercial or agricultural establishment.

In addition, there are other social security schemes such as the Coal Mines Provident Fund and Bonus Schemes, 1948, and the Employees, Provident Fund Scheme 1952. The Coal Mines Provident Fund and Bonus, Scheme provide for the grant of bonus equivalent to four months basic wage to persons sawing up to Rs. 300 per month basic wage and the institution of a compulsory provident fund. The Provident Fund Act, 1952, has been amended several times to have a wider coverage and to place the public and private sectors at par in respect of the application of provident fund. The rate of provident fund at present is 12 per cent. The scheme is administered by a central board of trustees incorporating representatives of the central and state governments. Employers and workers. Moreover, there are several retrenchment and lay-off benefits provided under the Industrial Disputes Act, 1947.

12.8 THE VIEWPOINT OF NATIONAL LABOUR LAW ASSOCIATION ON SOCIAL SECURITY IN INDIA:

As the National Labour Law Association indicates, we in India have several laws and schemes which provide protection to certain specified groups of people under certain contingencies. They are very much limited in scope both in terms of coverage as well as the benefits provided.

There is no uniformity either in their coverage or in the nature and level of benefits provided. While the employees of the Central government and also, to a lesser extent, the employees of the State Governments are well protected against loss of income due to sickness, maternity, occupational injury, old age, etc. there are wide variations in the nature and extent of protection extended to the employees in the private sector. The existing schemes are applicable comparatively to larger establishments in certain specified industries or employments. While the ESI Corporation administers a social insurance type of scheme providing medical and other benefits on a contributory basis, its coverage being limited to about 6 million persons, bulk of the labour force is outside the scheme.

The Workmen's Compensation Act, the Maternity Benefit Act and Payment of Gratuity Act provide for some measure of protection against loss of income due to occupational injury and maternity at the expense of the employers, there is no provision for medical or sickness benefit in such cases. The Employees Provident Fund Act provides for an old age benefit and survivors benefit, but there is no pooling of risks in the Employees

Provident Fund scheme. The extent of protection provided is directly proportional to the amount of contribution made to it. Although an insurance element has been introduced through the Family Pension Scheme and the Deposit Linked Insurance Scheme, there is much dissatisfaction about the working of these schemes on the part of the beneficiaries for the reason that the level of benefits admissible is low. So far as the employees in the unorganized sector are concerned, they remain largely uncovered by any statutory social security scheme. A few schemes have recently been introduced through executive orders for providing maternity and survivors benefits. Their coverage is limited and they are subject to budgetary constraints. There is no scheme for self-employed persons. Non-employees are given unemployment assistance and old age pensions, but the criteria for application of these schemes are somewhat rigid and the level of benefits very low.

12.9 SUMMARY:

The course and extent of development of fringe benefits has varied from country to country in response to different economic, social and political environment. However, they were mostly the outcome of purely philanthropic and paternalistic attitudes of employers. As trade unions grew in strength, they included fringe benefits in their demands and were able to secure their incorporation in collective agreements. Also, many employers recognized that providing such benefits was to their own advantage too, because by doing so, it might lead not only to improved industrial relations but also to larger output and less labour turnover.

Significantly, fringe benefits are a part of employee compensation system and the employees tend to tale them for granted. They are no more on the fringe of compensation but constitute an integral component of individual earnings, involving spiraling costs of production. Increased labour costs get transmitted to the consumers in the snaps of higher price levels. In spite of their adverse effects, fringe benefits will continue to be substantial part of the compensation system in the foreseeable future. They purport of develop a harmonious industrial relations climate, improve employee productivity and loyalty, and provide a sense of individual security. For better results, they should also receive equal attention in terms of both research and administration. They are to be planned in such a way that they exert a beneficial effect on the workers and at the same time, contain the total wage cost within the control of managements.

12.10 KEYWORDS:

Compensation Benefits

Fringe Benefits

Indirect Remuneration

Insurance Benefits

Pension Plans

12. 11 SELF ASSESSMENT QUESTIONS:

1. Define fringe benefits. Bring out their importance

2. Bring out the various employee benefits and services. Describe each in brief.

3. Outline the principles of fringe benefits.

4. Explain the various steps in the benefits administration.

5. Briefly describe the benefits that an organization might give its employee to provide them with greater financial security.

6. Fringe Benefits serve as golden hand-cuffs. Discuss.

7. Explain the various legally required fringe benefits in India.

8. Fringe Benefits have psychological and social base. Discuss.

9. Explain various social security measures in India.

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LESSON- 13

WAGE PAYMENT METHODS/SYSTEMS

13.0 OBJECTIVE :

After reading this lesson, you should be able to:

- Review the importance and need of different wage payment methods following in industries
- Know the various types of payment methods.
- Visualize the different methods of payments implemented in the organization.
- Observe the payment methods in different countries.

STRUCTURE:

13.1 Introduction
13.2 Payment By Results
13.3 Work Study
13.4 Balance or Deft Method
13.5 Incentive Rate System
13.6 Job Evaluation System
13.7 Choices in Payments System
13.8 Changes in Payment System
13.9 Payment System in Different Countries
13.9.1 Payment System in United Kingdom
13.9.2 Payment System in Germany
13.9.3 Payment System in U.S.A
13.9.4 Payment System in Australia
13.9.5 Payment System in Netherland
13.9.6. Payment System in Japan
13.10 Global Payment methods
13.11 Summary
13.12 Keywords
13.13 Self Assessments
13.14 Further Readings

13.1 INTRODUCTON:

Employee is remunerated through the payment of wages. The system of the payment of wages is vital significance to the workers as it has an important bearing on the size of their earnings. There are different methods of wage payment prevalent in the different industries in various countries. But an ideal wage system should fulfill certain characteristics. Firstly, it should be conductive to the interests of both the employer and employees. If should also be capable of providing certain incentives to workers necessary to accelerate production. Secondly, the wage system should be fairly simple as well as flexible.

Wage payment system consists of the pay structures and the methods used to motivate and reward work force for their contribution to the goals of the organization. Various systems of the wage payments have been developed in different industries and in different countries. All of these systems may, however, be regarded as variants or combinations of different principles of time rate system payment by results system, place rate system, balance or debt system, incentive rate system, and job evaluation system. These systems reflect the basic philosophy of a company and its management.

Wage and Salary*:* Wage and salary are the most important component of compensation and these are essential irrespective of the type of organization. Wage is referred to as remuneration to workers particularly, hourly-rated payment. Salary refers to as remuneration paid to white-collar employees including managerial personnel. Wages and salary are paid on the basis of fixed period of time and normally not associated with productivity of an employee at a particular time.

Incentives: Incentives are the additional payment to employees besides the payment of wages and salaries. Often these are linked with productivity, either in terms of higher production or cost saving or both. These incentives may be given on individual basis or group basis.

Fringe Benefits: Fringe benefits include such benefits which are provided to the employees either having long-term impact like provident fund, gratuity, and pension; or on occurrence of certain events like medical benefits, accident relief, health and life insurance; or facilitation in performance of job like uniforms, Canteens, recreation, etc.

Perquisites: These are normally provided to managerial personnel either to facilitate their job performance or to retain them in the organization. Such perquisites include company car, club membership, free residential accommodation, paid holiday trips, stock options, etc.

Wages: According to economic theory, wages are defined broadly as any economic compensation paid by the employer to his labourers under some contract for the services rendered by them. In its actual sense which is prevalent in the practice, wages are paid to workers which include basic wages and other allowances which are linked with the wages like dearness allowances, etc.

Concept of Reward/ Wage Payments:

A reward is an appetitive stimulus given to a human to alter its behavior. Rewards typically serve as reinforces. A reinforce is something that, when presented after a behavior, causes the probability of that behavior's occurrence to increase. Note that, just because something is labeled as a reward, it does not necessarily imply that it is a reinforce. A reward can be defined as reinforce only if its delivery increases the probability of a behavior.

Reward or reinforcement is an objective way to describe the positive value that an individual ascribes to an object, behavioral act or an internal physical state. Primary rewards include those that are necessary for the survival of species, such as food, sexual contact, or successful aggression. Secondary rewards derive their value from primary rewards. Money is a good example. They can be produced experimentally by pairing a neutral stimulus with a known reward. Things such as pleasurable touch and beautiful music are often said to be secondary rewards. For example, there is a good deal of evidence that physical contact, as in cuddling and grooming, is an unlearned or primary reward. Rewards are generally considered more desirable than punishment in modifying behavior.

13.2 PAYMENT BY RESULTS (PBR)

There are many different systems of wage payment under which the workers earnings are related directly to some measurement of the work done either by him/her or by the group or working unit to which he belongs. Such systems, known as payment by results, cab be classified in four main groups such as : (1) in the same proportion as output; (2) proportionately less that output; (3) proportionately more than output; or (4) in proportions which differ at different levels of output.

Payment by results is a payment system under which money rewards vary with the measured changes in performance according to predetermined rules. The PBR system relates the pay or a part of the pay received by the worker to a number of items reproduces or the time he takes to do a certain amount of work. Under this system, the worker is paid a wage which bears some fairly direct and continuous relation to his output or performance, or to the average output of the group of workers to which he belongs. Under this plan, the worker working in a given condition and with the given machinery is paid exactly in proportion to his physical output. Under PBR, the workers pay during a given period is directly related to the levels of measured performance. The essential difference between PBR and time rate system is how performance. The essential difference between PBR and time rate system is how performance is related to reward. The basic alternative to PBR is time payment. The PBR system varies with the variation in individual and group performance at the plant or enterprise as a whole.

The most common scheme of payment by results which is purely individual in character is what is called straight piece work. A workers earning can be calculated on the basis of the number of pieces produced and the rate per piece. This means payment of uniform price per unit of production, and it is most appropriate where production is repetitive in character and can easily be divided into similar units. There is also the differential piece work system where the wage cost per unit is adjusted in relation to output. Under this scheme two piece rates may be fixed: one considerably higher than the going time wage for the job and the other somewhat lower than the time wage. The lower rate is paid when the workers fail to achieve the standard level of performance.

The main idea behind establishing two differential piece rates has been to reward high production and to discourage low production. This system has been used mainly by firms with heavy non-labour costs. The main problem in applying this system is the difficulty of setting the standard and the amount of difference between the two piece rates. Further, it may lead to excessive speeding by some workers, who then get much higher earnings than others.

The group PBR is generally viewed as lending itself to jobs that are interdependent, either because they are performed in sequence, as in assembly work, or because joint efforts are required to ensure effective performance. Instead of being limited to the individual worker of his group, the unite of accountability in PBR schemes can extend to all the departments, work divisions, entire plants or even all worker in the enterprise.

The PBR may be introduced with certain safeguards such as; (a) quality of output is to be controlled through strict supervision; (b) wastage of material is to be prevented; (c) health of the worker is to be protected; (d) supply of raw materials, maintenance of plant and efficiency of management are to assured; (e) workers are to be guaranteed job security or continued employment; and (f) work-load is to be fixed by impartial experts.

Rates once fixed should not be cut by management without justification. The design of an appropriate PBR scheme involves basically three different types of decisions. The first concerns the safeguards and the procedures to be incorporated in the scheme to make it acceptable and effective; the second concerns the amount of bonus, or incentive potential that the scheme should provide; and the third concerns the precise way in which increased productivity should be shared between the worker and the employer.

When a system of payment by result is applied in a particular undertaking the interest of employers and workers may be seriously affected. The employees, in a desire to raise their earnings, may attempt to increase their output to a level at which quality is adversely affected. Such deterioration of quality is, of course, not in the interest of the employers or of the workers.

The safeguards needed to ensure the equitable operation of any system of payment by results include (1) safeguards relating to the introduction of the system, (2) safeguards relating to the operation of the system.

Systems of payment by results are to be applied in an equitable and reasonable manner. The health and safety of the workers may suffer if the task is set too high. Again, inequities may result if some workers are able to earn considerably more than their colleagues. Further, workers may be tempted to neglect security regulations while on piece work. When such a system is applied the interest of both employers and employees require to be protected by suitable provisions in collective agreements. Unless a system of payment by results in applied equitably from both the managements and the workers points of view, good industrial relations will be difficult to secure or maintain. District between management and workers and friction among the workers themselves may prevent the system from functioning properly, may lead to wasteful strikes, or may even force the complete abandonment of the system.

A recent ILO study on incentive schemes makes it clear that most PBR schemes are today quite distinct from the past, although links between pay and performance have been retained. The point made by the study is that piece work and other similar incentive schemes which were firmly established thirty years ago, are on wane, giving place to what is called pay for collective or teamwork. This is to ensure production and productivity in a plant or industry. Today, PBR tends to reward teamwork. Many schemes have shifted from being based on individual worker output to group and plant-wide output.

A survey in the USA covering enterprises with at least 1000 employees found that only 7 percent of the workers under incentive plans were paid according to systems based on individual output. Nearly one-third or 31 percent were paid on the basis of group output, and 61 percent were covered by incentive plans which paid bonuses according to a combination of individual and group output. In most developing countries, while payment by results is still based largely on individual output, there is a growing trend to rely on group or enterprise incentive schemes, perhaps because of the difficulties of establishing individual production standard.

The PBR has many advantage; (a) it pays the workmen according to their efficiency as reflected in the amount of work turned out by them; (b) it involves less supervision as the workers are not likely to while away their time; (C) being interested in the continuity of his work, a workman is likely to take greater care in the maintenance of the machine.

The demerits of this system are (a) a piece rate worker in his anxiety to produce more may neglect the quality of output' (b) he may, in his desire to earn more, any work so hard as to impair his health, unmindful of the fact that this would ultimately reduce his earning power; (c) under this system, the workers earning may suffer because of causes beyond his control, such as inadequate supply of raw materials, failure of machinery, lack of demand in the market for the goods produce; and (d) trade union are often opposed to this system as they are of the opinion that such a system encourages rivalry among workers and endangers their solidarity in labour disputes.

The success of any system of payment by results depends in a large measure on the way in which it is introduced and applied. First, the requirement for the success of a system of payment by results is that it should be developed and applied with the arrangement of the workers concerned and in an atmosphere of goods industrial relations. Second, wherever possible the methods to be followed in the introduction and application of systems of payment by results should be settled by collective bargaining between the employers and workers concerned.

13.3 WORK STUDY:

If workers are to be paid by results, these results must be accurately measured. This means that the nature of the task which the worker is expected to perform and the quality of the product must be clearly defined. Work study must cover such matters as the layout, equipment, materials, process, machine speeds and feeds, working conditions, the quality of the product and all other relevant and significant details affecting the output. It also requires detailed study of work procedures and of every operation of workers and supervisors. In many undertakings its followed for the purpose of ensuring that the most effective use is made of the organization, labour force and equipment at their disposal. It draws attention to unnecessary, ineffective or wasteful procedures and operations which need to be eliminated or to be improved.

The work study techniques comprises of methods study and work measurement. Both are complementary and must be used in sequence. Production methods and tasks are capable of improvement by systematic and detailed methods study. An important feature of many methods

improvement programmes is the care which is taken to secure the widest possible participation of workers and supervisors in the development and adoption of improved methods of working.

The methods study procedure consists of a sequence of steps, namely, selection of study, recording the fact, analyzing the facts, developing an improved method, defining the new method, installing the new method, and maintaining the new method.

A number of attempts have been made to measure directly the work content of different industrial tasks. A number of alternative methods of work measurement have been developed and have been adopted widely in industry in certain countries. Most modern methods of work measurement, however, require that the operation or task be broken down into its constituent elements, each of which is rated and timed separately.

Inflation has caused some awkwardness for those piece work schemes which have not been modernized through work measurement. Piece rates are still prevalent in many units established long ago. Workers engaged in spinning and weaving in the textile industry have usually been employed in piece work. It is oldest form of incentive payment that is still widely used in our country. It is adopted generally in jobs of a repetitive nature where tasks can be readily measured, inspected and counted. This undermines much of the simplicity and directness which piece work seems to offer.

13.4 BALANCE OR DEBT METHOD:

This is a combination of time and piece rate. The worker is guaranteed an hourly or a day rate with an alternative piece rate. If the earnings of a worker calculated at the piece rate exceed the amount which he would have earned if paid on the time basis, he gets credit for the balance, namely, the excess piece rate earnings over the time rate earnings. If the piece rate earnings are equal to his time rate earnings, the question of excess payment does not arise. Where piece rate earnings are less than time rate earnings, he is paid on the basis of the time rate; but the excess paid is carried forward as a debt against him to be recovered from any future balance of piece work earning over time work earnings. This system pre-supposes the fixation of time and piece rates on a scientific basis. The obvious merit of this system is that an efficient worker gets an opportunity to improve his earning.

13.5 INCENTIVE RATE SYSTEM:

Incentive Rates can be used more effectively in a production situation where output is measurable in homogeneous units, where product specifications do not change frequently, and where workers effort can directly influence output. Incentives are difficult to employ where output is fixed substantially by the requirements of production process and cannot be controlled by the workers. The most common type of incentive system is straight piece work, which simply means a constant rate of pay per unit of output. Bonus plans represent another method of incentive pay and involve, in general, the determination of standard tasks. Bonuses are paid for production above standard.

A great many problems arise in connation with incentive plans. Of basic importance is the way in which production standards are determined under either straight piece work or bonus systems. Under boons plans, the extent to which increased production will be rewarded must be decided. The question of incentive rate adjustment in the light of technical changes is also important. Another crucial area is the guarantee of minimum earnings under the incentive systems.

A substantial amount of controversy between labour and management has arisen over the use of incentive pay methods. Organized labour does not, however, have a uniform position in the matter. Some unions are opposed in principle to the incentive plans; others accept wage incentives and are concerned primarily with the equitable determination of rates and prevention of abuses.

13.6 JOB EVALUATION SYSTEM:

Job evaluation is a method used to describe, analyze, compare and evaluate jobs within a unit, a branch, or an industry on the basis of the work content and the job requirements in order to place them under particular wage or salary grades. The main characteristics of job evaluation may be summed up as:

1. It is a method with a systematic approach
2. It is an analysis of the work involved in its starting point.
3. It is an attempt to determine the requirements of the work involved for any incumbent
4. It is a process by which jobs in an organization are appraised.
5. It is a process of analyzing and describing positions, grouping them, and determining their relative value by comparing the duties of different positions in terms of their different responsibilities and other requirements. Different methods of job evaluations of wage determination were discussed in the earlier unit.

13.7 CHOICES IN PAYMENT SYSTEMS:

The management has certain broad choices concerning payment systems. The choices are not always mutually exclusive, so it may be better to think of these ‘choice of emphasis’. The first choi8ce of emphasis is between simplicity or complexity in payment systems. An example of simplicity would be, for example, a flat rate system or one based on traditional piece work methods without any additional features. A complex system would be one where, for example, job evaluation was used in conjunction with various types of incentives, bonus or profit-sharing schemes. A second choice of emphasis, closely related but not identical to the first, is whether to hold to relatively fixed and rapid payment system, or to prefer a flexible and adaptable one.

13.8 CHANGES IN PAYMENT SYSTEM:

There is a tendency towards rapid change in payment systems. A wide range of factor has been involved in this change process. There is some movement away from the traditional system of payment by results due to changes in technology and production arrangements. Moreover, there have been growing doubts about the motivational effectiveness of the traditional schemes and the willingness of workers to tolerate fluctuations in earnings for reasons beyond their control. The shift has been towards either time payment schemes or tot payment by results schemes, base partly at least on non-output related measures of performance.

Another development has been that owing to changing social attitudes, employer-employee relations, equal pay for equal work, and influence of trade unionism, the employers have rationalized their payment practices and followed more open policies about pay. They have adapted their pay structures to make them both equitable internally and competitive externally. Particularly for non manual workers, there has been an increasing recourse to various formal job evaluation procedures. And those directly affected have been given an increasing say in the development of the new pay structures.

13.9 PAYMENT SYSTEMS IN DIFFERENT COUNTRIES:

There is no uniformity in wage payments of different countries as there is a wide variation in the methods of negotiation and settlement, base on historical, cultural and national factors. There is a wide variation as regards government intervention in industrial relations field; the type of collective bargaining; the extent to which payment by result methods are being replaced by standard grades based on job evaluation; the amount of range benefits included in the wage bill; the gaps between the pay of men and women; and the strength of organize labour in different countries. However, the system of free collective bargaining at the plant and industry level covering both blue and white collar workers became the cornerstone of wage determination in several countries. A brief review of payment systems in some countries is given below.

13.9.1 PAYMENT SYSTEM IN UNITED KINGDOM:

The U.K. has suffered from the disadvantages of being the world's oldest industrial country. An important consequence of its early industrial development was to enable a great diversity of methods and practices to grow up in various industries and occupations. This fragmentation continues to manifest itself in employment systems, in industrial relation systems, and in payment systems, although there are tendencies in more recent years for integrating factors to emerge.

Wage in Britain are fixed by a variety of methods. The British Parliament adopted the minimum wage legislation in 1909 aimed at abolishing "sweating". Wage councils continue to exist but their importance is declining. About three million workers in the less well organized and underpaid industries (e.g. food, clothing, laundries and catering) are covered by wage councils which fix minimum remuneration and conditions of employment. There is also a wage board for agriculture. These bodies consist of equal number of employers; and workers representatives plus about three independent members. In the main, however wages and conditions are determined by collective bargaining. Plant level bargaining is based on an elaborate system of shop stewards and shop committees. There have been two major attempts to control wages statutorily and to prevent inflation-first under the Labour Government in 1966 and later under the conservative sin 1972-73. The system of voluntary bargaining was restored by Labour in summer of 1974, and the official pay board was abolished although strict control was maintained over certain prices. Most national collective agreements lay down rates of pay, holidays, hours of work, and also cover such issues as shift working, overtime rates, apprenticeships, redundancy and pensions. Piece work rates, bonus payments, merit money and work arrangements are normally dealt with locally and involve substantial additions to the nationally agreed rates. Productivity bargaining first became established in a number of oil refineries. The major stimulus to the wider adoption of productivity bargaining came through government intervention.

In the middle of 1950s a major development tool place in work measured individual incentive schemes in manufacturing industry. The foundations of the new payment systems were provided by the techniques of work study and method study. Many companies at this time set up work study department. Work-measured incentives were introduced on a large scale both in industries with a tradition of piece work method and in those where time work predominated. Piece work is still the oldest form of incentive payment that is widely used in Britain. Its retention in a number of industries, especially textiles, footwear and clothing, seems to be partially a function of the strength of the tradition there. System of job evolution and job grading for manual workers were not developed in Britain as early as in the U.S. and certain other European countries such a the Netherlands.

There is no national minimum wage in Britain. Built-in cost of living agreements have long existed in many industries, e.g., building. A recent innovation has been the introduction of there should agreements which provide for a pay rise when the retail price index increases by a certain amount. Though most employers prefer negotiations to be conducted on a national basis, there has been an increasing tendency towards plant agreements. In this, shop stewards play a major part. The growth of productivity bargaining which was a feature of the 1960s slowed down in the 1970s when unemployment started to rise. Some, but not all agreements, include procedures for the settlement of grievances. There is no system of compulsory arbitrations as existed during the Second World War.

There are also wide differentials between the highly paid and the lower paid and great attention is given towards maintaining these. Fringe benefits continue to be the most significant form of reward for labour in Britain. In the manufacturing industries they steadily rose, as a proportion of average pre-tax total remuneration from 11.1 percent in 1964 to 19.4 percent in 1981. Similar rises took place in other sectors. An Equal Pay Act was introducing in 1970 whose objective was to implement the principle by the end of 1975. The gap between men's and women's rates, though progressively narrowed by incremental increases, has remained wide.

The British coal miners have traditionally been among the higher paid blue collar employees since 1920. But due to hydro-electric developments and use of oil fuels together with more economical use of coal, there were attempts to bring coal miners at par with other blue collar employees. There was a six month unsuccessful strike by coal miners in 1974 when the government took a tough stand. Soon after, due to the oil crisis and change of government the miners were able to stake special claims and their special status as aristocracy of labour continued.

A striking feature of the British scene during the 1970s has been the emergence of militancy among the white collar workers. Local government officers, teachers, civil servants and hospital workers have been among those who have resorted to some form of industrial action to win concession and to reduce the gap between their pay and that of manual workers. White collar workers unions have represented the highest rate of growth among TUC unions.

13.9.2 PAYMENT SYSTEM IN GERMANY:

The then Federal Republic of Germany (FRG) is fortunate in possessing a rational trade union structure. FRG had only 16 union groups organize done an industrial basis. The apex trade union organization had about 8 million workers, and its powerful constituent was the Metal Workers Union which could, and did, set the pace in negotiations. The DGB exercise a powerful coordinating and educative influence and enforced a strong discipline over its affiliates.

In Germany, negotiations can be conducted on an industry-wide or national basis. The right of collective bargaining is legally guaranteed. Collective agreements do not need government approval but have to be reported to the federal minister of labour. Both the DGB and the employers' organization (BDA) issue guidelines for the coordination of wage movements.

There is no legal minimum wage as such, but agreements usually lay down minimum wages and working conditions and normally include provision for conciliation, undertaken by labour courts at local, provincial or federal level. Both sides are obliged to maintain social peace during the currency of a collective agreement, which usually lasts for 1-2 years and outlaws resort to industrial action or lockouts.

Rates of pay vary widely according to industry, area and degree of organization. The highest paid groups in terms of earnings are printing and publishing, chemicals, petroleum, automobiles, iron and steel, metallic ore mining, coal, transport and metal manufacture. The lowest paid groups include food manufacture, clothing furniture and transport. In general, however, the gap between skilled and unskilled workers is small than in the U.K.

Fringe benefits represent an important part of remuneration and can add more than 50 percent to cash wages. The gap between the pay of weekly and monthly paid workers has progressively been narrowed, except for a category of senior salaried employees who are not bound by collective agreements.

In common with other European Union countries, Germany is bound by the Treaty of Rome and by its own Constitution, to provide equal pay for men and women. Owing to the nature of women's work pattern, there is a gap and in 1971 in FRG, the average of women's earnings in manufacturing represented 70 percent of those of the men. The aim is to reduce progressively the length of the working week to 40 hours. Overtime rates are usually about 25 percent above the basic rate and are higher for those working on Sundays or public holidays. Most companies provide canteen and transport facilities and in some cases subsidized housing. Profit sharing schemes are widely operated and there are numerous schemes for saving, including acquisition of companies' shares. Now, there is a growing tendency for group bonus schemes to replace systems of payment by results. The practice of direct plant bargaining is growing. Recent agreements have tended to give priority to the lower paid sections. German unions are as much concerned with the raising of status of workers through co-determination system as with the physical size of the pay packet.

13.9.3 WAGE PAYMENT METHODS IN USA

An employee will have the method by which they are paid (by cash, cheque or bank transfer) defined by their contract of employment. There is no statutory right to have wages paid in a certain way, for example, in cash.

All employees, irrespective of the number of hours they work, are legally entitled to a written statement of their main terms and conditions of employment within two months of the date when their employment started. This statement must provide information on how frequently wages will be paid, for example, weekly or monthly. The written statement is evidence of the contract of employment but does not contain everything that would be in the contract. The contract should also give details of when wages are paid and if these are paid in advance or in arrears.

If the employer changes the method or timing of paying wages this could be a change to the contract of employment. Any changes to a contract of employment must be agreed by both parties.

Most employees have a statutory right to receive a detailed written pay statement from their employers at or before the time of the payment of wages. Every pay statement must give the following information:

- The gross amount of the wages or salary;
- The amounts of any fixed deductions and the purposes for which they are made, for example, trade union subscriptions;
- The amounts of any variable deductions and the purposes for which they are made;
- The net amount of any wages or salary payable;
- The amount and method of each part payment when different parts of the net amount are paid in different ways, for example, the separate figures of a cash payment and a balance credited to a bank account.

An employer may choose to give either a pay statement which specifies the amounts and purposes of every fixed deduction separately or a pay statement which specifies only the total amount of all fixed deductions without any explanation of their purpose. In this case the employer must give the employee a standing statement of fixed deductions (which identifies all deductions from the wages) at or before the time the pay statement is issued. If a standing statement is used it must be in writing and must for each item deducted state the amount, the intervals at which the deduction is made and the purpose or description of the deduction. This statement must be reissued at intervals no longer than twelve months apart incorporating any changes.

If an employer fails to provide an itemised pay statement or, there are queries about what should be included in the pay statement or standing statement of fixed deductions, or an employee has had certain deductions made which are unauthorised, the employee should raise a grievance with their employer.

13.9.4 POPULAR PAYMENT METHODS IN AUSTRALIA

The range of criteria on which minimum wage upratings are based is broad. The objective of the National Minimum Wage is to “establish and maintain a safety net of fair minimum wages, taking into account: (a) the performance and competitiveness of the national economy, including productivity, business competitiveness and viability, inflation and employment growth; (b) promoting social inclusion through increased workforce participation; (c) relative living standards and the needs of the low paid; (d) the principle of equal remuneration for work of equal or comparable value; (e) providing a comprehensive range of fair minimum wages to junior employees, employees to whom training arrangements apply and employees with a disability" (Section 284 of Fair Work Act 2009).

In addition, the objective of the 'modern award' is to "ensure that modern awards, together with the National Employment Standards, provide a fair and relevant minimum safety net of terms and conditions, taking into account: (a) the relative living standards and the needs of the low paid; and (b) the need to encourage collective bargaining; and (c) the need to promote social inclusion through increased workforce participation; and (d) the need to promote flexible modern work practices and the efficient and productive performance of work; and (e) the principle of equal remuneration for work of equal or comparable value; and (f) the likely impact of any exercise of modern award powers on business, including on productivity, employment costs and the regulatory burden; and (g) the need to ensure a simple, easy to understand, stable and sustainable modern award system for Australia that avoids unnecessary overlap of modern awards; and (h) the likely impact of any exercise of modern award powers on employment growth, inflation and the sustainability, performance and competitiveness of the national economy" (Section 134, Fair Work Act 2009).

Australia does not have an official poverty line, but it follows international conventions, such as using 40% of the average wage. Poverty indicators provided by charitable institutions are also published, but there is no formal national poverty line calculated and used for purposes of setting the national minimum wage.

13.9.5 PAYMENT SYSTEM IN NETHERLAND

Most people taking up employment in the Netherlands must obtain a work permit before they start. There are exceptions, including those working for International Organisations such as the International Court and the European Space Agency where the organisation will take care of all necessary paperwork, and the citizens of the European Union nations (except Bulgaria and Romania). Highly skilled migrants may also be exempted. A work permit can be obtained by employer from the UWV Werkbedrijf (Uitvoeringsinstituut Werknemers Verzekeringen), which is the office for re-integration, unemployment benefits etc. (formerly the Centre of Work and Income)

The Foreign Nationals Employment Act (Wet Arbeid Vreemdelingen or WAV) requires employers to first recruit in the Netherlands and other Western European countries. This is intended to protect the Dutch and Western European labour markets. The work permit system allows the Ministry of Social Affairs and Employment to regulate the intake of labour in the Netherlands. The work permit application procedure requires the employer in most cases to show that no qualified Dutch or EU nationals are available to fill the vacancy. This needs to be done after advertising for at least five weeks prior to filing the application. Applicants for work permits must be between the ages of 18-45.

The maximum length of a work permit is three years. People who have had work permits for three consecutive years, and who have not moved their residence outside the Netherlands since then, become exempt from the work permit requirement. Their residence permits can be endorsed with a note stating "Employment freely permitted" and "No work permit required". If the residence permit is not approved (for example, the IND discovers that the applicant has a criminal record), then the work permit is automatically withdrawn when the residence permit is denied. If you are allowed to work in the Netherlands, then your spouse/partner is usually allowed to work as well.

13.9.6 PAYMENT SYSTEM IN JAPAN

It is typical for Japanese companies to pay wages on a monthly basis, and to pay employees summer and winter bonuses. One characteristic of Japanese wages is the make-up: monthly wages usually include a basic wage and a range of allowances, which may include accommodation, family and transportation allowances. Another characteristic is that the amount paid in bonuses makes up a relatively high proportion of total wages paid to employees (*1). An effect of the high proportion of wages made up of various allowances and bonuses consequently is to lower the rate of overtime pay paid for work outside normal working hours. This system also allows labour costs to be immediately reduced in the event of a recession, for example. Although more businesses are adopting a yearly wage system, there are often few benefits for employers in practice under Japanese labour law (*2). Further information is available through the Basic Survey on Wage Structure statistics collated annually and provided by the Ministry of Health, Labour & Welfare in both Japanese and English.

1. In FY2011, the average bonus paid by private-sector companies was 3.94 months' worth of prescribed monthly wages (for clerical and technical occupations). (Source: National Personnel Authority)

2. Whether or not a yearly wage system is introduced or extra wages are paid for overtime work is irrelevant. If a company in Japan introduces a yearly wage system, it almost always only covers management-level employees.

13.10 GLOBAL PAYMENT METHODS

It is still too early to know precisely which sectors and which occupations have been most affected by the crisis, as too few countries have published data on the structure of wages. The principal source of such data at the international level, the ILO's "October Inquiry", is being revised to capture trends in occupational wages: in particular, a wide consultation is seeking to determine the most relevant industries and occupations for which labour market variables are to be collected globally, and the units in which these variables should be reported. The consultation seeks to take into account the significant differences in industry structures and staffing patterns in different economies around the world by consulting with experts from a wide range of developing and developed countries.

In the meantime, country-specific data nevertheless suggest that wages may have been more adversely affected in the private sector than in the public sector. According to calculations by the Public Services International Research Unit, largely based on Eurostat's Labour Cost Index dataset, nominal earnings in the public sector have risen faster – or fallen less – than earnings in the private sector in 11 out of 18 European countries for which data are available. The same is true in the United States, where, in the two-year period from March 2008 to March 2010, private sector workers were found to have experienced a slower rise in earnings than state and municipal workers. Preliminary data for 2010 suggest, however, that this trend may be reversed in some of the countries that have implemented austerity measures to contain public debt and/or which have signed recent agreements with the IMF.

The more robust nature of public sector wages is probably linked to the higher level of unionization in the public sector than in the private sector, and also to a higher degree of coordination among public sector employees. At the same time, the evolution of the public sector to private sector wage ratio also reflects some sector-specific factors. In the United States, for example, during the past two years pay has risen faster than average in the education and health sectors, in both the public and the private sectors. By contrast, wage growth in the financial sector – which had outpaced average wage growth before the crisis – has fallen behind in recent quarters. In Europe, too, wages and salaries in financial services grew more slowly than the general movements in wages. In the United Kingdom, for instance, nominal gross average weekly pay increased by an average of 1.6 per cent in 2009, compared to 1.4 per cent in financial and insurance activities, –0.4 per cent in manufacturing and –3.5 per cent in accommodation and food service activities. 1 Also, UK bonus payments declined sharply by more than 25 per cent during the first year of the crisis to £19 billion at the end of 2008/early 2009, before climbing back to £22 billion one year later.

13.11 SUMMARY:

The system of wage payment is the method adopted by manufacturing concerns to remunerate workers. It is the way of giving financial compensation to the workers for the time and effort invested by them in converting materials into finished products. It indicates the basis of making payment to the workers, which may be either on time basis or output basis. The selection of the system depends on the type and nature of the concern and its products.

13.12 KEYWORDS:

Wage Payment Methods

Wage and Salary

Trade Unions

Fixed Deductions

13.13 SELF ASSESSMENT QUESTIONS:

1. Explain wage payment methods in brief.
2. Define work study. Discuss the Role work study in wage payment.
3. Explain the essence of incentive rate system in brief.
4. Explain the payment system in various countries.

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LESSON- 14

WAGE INCENTIVES

14.0 OBJECTIVE:

1. After reading this lesson, you should be able to:
2. Understand the nature and Importance of Incentive Payments
3. List the various pre-requisites for an efficient system
4. List the different types of incentives
5. Understand the Role of Incentives in the Compensation

STRUCTURE:

14.1 Introduction

14.2 Meaning and Definition

14.3 Need for Incentives

14.4 Importance and Advantages of Incentives

14.5 Objectives of Wage Incentive Schemes

14.6 Pre-requisites for Effective Incentive System

14.7 Scope of Incentive Schemes

14.8 Working of Incentive Schemes

14.9 Principles and Procedures for Installing Incentive System

14.10 Recommendations of the NCL

14.11 Incentives and Motivation

14.12 Linkage of Incentives to performance

14.13 Improving the Role of Incentives

14.14 Classification of Incentive Schemes

14.15 Problems arising out of incentives

14.16 Summary

14.17 Keywords

14.18 Self Assessment Questions

14.19 Further Readings

14.1 INTRODUCTION:

Besides wages and salaries, employees are paid incentives depending upon their performance incentive payments are quite substantial and are paid as regularly as wages and salaries. Incentives are the most likely drivers of attracting and retaining the best employees in startups. They are universal. Incentives are paid in all sectors-manufacturing, service sector or medical transaction etc. this lesson is devoted to a detailed discussion on the nature, significance and types of incentives.

The term "Wage incentives has been used both in the restricted sense of participation and in the widest sense of financial motivation ". It has been defined differently by different authors. We give below a few of these definitions.

"It is a term which refers to objectives in the external situation whose function is to increase or maintain, some already initiated activity, either in duration or in intensity". According to '**Hummel and Nickerson**'. "It refers to all the plans that provide extra pay for extra performance in addition to regular wages for a job. ' Florence' observes, it refers to increased willingness as distinguished from capacity. Incentives do not create but only aim to increase the national momentum towards productivity".

14.2 MEANING AND DEFINITION:

According to the 'National Commission on Labour ', "wage incentives are extra financial motivation. They are designed to stimulate human effort by rewarding the person, over and above the time rated remuneration, for improvements in the present or targeted regulations.

"A wage incentive scheme is essentially a managerial device of increasing a worker's productivity. Simultaneously, it is a method of sharing gains in productivity with workers by rewarding them financially for their increased rate of output."

According to 'Suri' this definition is based on the principle that "an offer of additional money will motivate workers to work harder and more skillfully for a greater part of their working time, which will result in a stepped-up rate of output."

We may define a "wage incentive as a system of payment under which the amount payable to a person is linked with his output. Such a payment may also be called payment by results." The term incentive has gradually acquired a wide connotation and includes all the possible factors, besides economic gains, which can possible motivate human beings towards better and greater performance.

Incentives are monetary benefits paid to workmen in recognition of their outstanding performance. They are defined as "variable rewards granted according to variations in the achievement of specific results." The 'International Labour Office' refers to incentives as 'payment by results'. But it is appropriate to call them 'incentive systems of payment' emphasizing the point of motivation, that is the imparting of incentives to workers for higher production and productivity. However, both these terms are used in this chapter. Unlike wages and salaries which are relatively fixed, incentives generally vary from individual to individual, and from period to period for the same individual.

14.3 NEED FOR INCENTIVES:

It is true that monetary compensation does constitute very important reason for the working of an employee. But this compensation alone cannot bring job satisfaction to the workers. One cannot expect effective performance from a worker who is dissatisfied with its job, even if he is well paid. Sociologists and industrial psychologists also view that the financial aspect is not the only dominant motivating force. Confidence in the management, pride in the job and in firm and concern for the overall good cannot be brought by a bonus. Hence the modern authorities on management science have recognized the need for the provision of incentives to build up good morale.

14.4 IMPORTANCE AND ADVANTAGES OF INCENTIVES:

The primary advantage of incentives is the inducement and motivation of workers for higher efficiency and greater output. It may not be difficult to get people for fixed wages and salaries. But with fixed remuneration, it is difficult to motivate workers to show better performance. Fixed remuneration removes fear of insecurity in the minds of employees. A feeling of secured income fails to evoke positive response. Positive response will surely come when incentives are included as a part of the total remuneration.

Earnings of employees would be enhanced due to incentives. There are instances where incentive earnings exceed two to three times the time-rated wages or salaries. Increased earnings would enable the employees to improve their standard of living.

There will be reduction in the total as well as unit cost of production, through incentives. Productivity would increase resulting in greater number of units produced for given inputs. This would bring down the total and unit cost of production.

Production capacity is also likely to increase. The Bangalore-based Rail Plant, for example, has now a production capacity of 77,000 wheels and 48,000 axles as against the initial capacity of 56,800 wheels and 23,000 axles. The higher capacity has been achieved as a result of implementation of the recommendations for the adoption of a group-incentive scheme carried out by the Rail India Technical and Economic Services.

The other advantages of incentive payment are reduced supervision, better utilization of equipment, reduced scrap, reduced lost time, reduced absenteeism and turnover, and increased output. Furthermore, systems of payment by results would, if accompanied by improved organization and work measurement, enable firms to estimate labour costs in more accurately than under the system of payment by time. This would facilitate the application of cost-control techniques like standard costing and budgetary control.

Apart from the benefits cited above, incentive packages are a very attractive proposition for managements because they do not affect employer's contribution to the provident fund and other employee-retirement benefits.

14.4.1 DISADVANTAGES OF INCENTIVES:

On the other hand, systems of payment by results may have disadvantages. There is a tendency for the quality of products to deteriorate unless steps are taken to ensure maintenance of quality through checking and inspection. This involves added expenses. In some cases, it may not be possible or may be too expensive to maintain quality fully, and the benefit, gained in the form of increase output and lower cost may be offset to a considerable degree by deterioration in the quality of the products.

Difficulties may arise over the introduction of new machines or machines or methods. Workers may oppose such introduction for fear that new piece or bonus rates set, when the job is restudied at intervals of time, may yield lower earnings; or when new machines or methods are introduced; they may slacken their rate of work in order to avoid rising output to a level which would make a restudy of the job necessary. Costs may not, therefore, be lowered to the extent that would be necessary if the workers were on time-based work. Most trade unions agree that cuts in piece or bonus rates are justifiable in such circumstance. But individual workers may not share this view, and output and the level of costs may be affected accordingly.

Workers tend, moreover, to regard their highest earnings as normal and may, therefore, press for a considerable higher minimum wage when they are paid by results than when they are paid by the hour. Payment by results may, therefore, lead to higher labour costs in certain industries such as paper-making and coal mining where workers experience, for reasons beyond their control, good and bad runs. Their earnings on the days then have good runs are apt to be regarded by them as normal earnings.

Besides, there is evidence that some workers paid by results have disregarded security regulations in order to achieve high output, thus, increasing the danger of accidents. Some workers tend to overwork during the normal working day and sometimes keep on working in their lunch hour. These practices would affect their health.

Another disadvantage is that jealousies may arise among workers because some are able to earn more than others. In the case of group-incentive schemes, the workers who are fast in their work may be dissatisfied with those who are slow. Where heavy work is involved, older workers are likely to be criticized for being too slow.

One of the greatest difficulties with the incentive systems in the setting of piece or bonus rates. Rate fixing involves delicate problems of judgment in which there is always a risk of error. If rates are set too low, workers are bound to be dissatisfied and will be under pressure into work very hard. If rates are set too high, workers may slacken their efforts at times so that their employers may not have cause to ask for a revision of rates because the earnings are too high. Workers sometimes decide approximately how much they feel they wish to earn and are, therefore, not interested in working for that part of the day which remains after they have earned the amount they want.

Difficulty also arises in determining the standard performance many organizations follow a safe route to fix the standards – which is usually the average of past year’s performance. Past performance may not be the ideal basis for fixing production norms.

Since preparing incentive schemes is such a complex business, managements usually outwit their employees. For instance, the period over which incentives are payable is an important factor in determining how much a worker earns. At bharat gears, for example, an incentive a payable on the average of three month's production. This gives the company the opportunity to recover the production lost a s a result of late deliveries of raw materials, technical breakdowns, and so forth. Even if the workers produce for a certain period, in excess of the norm, they may not be eligible for incentive pay.

14.5 OBJECTIVES OF WAGE INCENTIVE SCHEMES:

Wage incentive schemes aim at the fulfillment of one or more of the following objectives:

1) To improve the profit of a firm through a reduction in the unit costs of labour and material or both;

2) To avoid or minimize additional capital investment for the expansion of production capacity.

3) To increase a worker's earnings with dragging the firm into a higher wage rate structure regardless of productivity; and

4) To use wage incentives as a useful tool for securing a better utilization of manpower, better production scheduling and performance control, and a more effective personnel policy.

14.6. PREREQUISITES FOR EFFECTIVE INCENTIVE SYSTEM:

All things considered, it may be concluded that in many industries or undertakings and for a large group of operations, well-designed systems of payment by results shall yield advantages to all concerned. Many of these advantages will be realized provided sufficient safeguards are provided. Such prerequisites are:

1. The co-operation of workers in the implementation of an incentive scheme is essential because the employees somehow devise, if they do not like a scheme, ingenious ways of evading or sabotaging the plan, often with the tacit connivance of the foreman or supervisor. Worker's co-operation is necessary in:

   (i) The methods followed in measuring the results or output upon which payment is based;

   (ii) The methods followed in setting wage rates for different classed of work; and

   (iii) Appropriate safeguards concerning earnings, job security and settlement of disputes over piece-work rates and allotted time.

To prove that schemes were often introduced without workers' cooperation and consequently met with failure, we quote the following:

The practice adopted by several industrial establishments in the Mumbai region in regard to the preparation of an incentive scheme is to hire an industrial consultant and to make him work in the establishment under the cloak of secrecy, until a scheme has been finally prepared. It is only after several months that the workers of the establishment and their unions begin to suspect that some scheme is under preparation. Trade union leaders, who are not employees currently, are not even allowed to which how standards have been evolved. Naturally, the workers reject out-of hand, a scheme prepared so surreptitiously.

2. The scheme must be based on scientific work measurement. The standards set must be realistic and must motivate workers to put in better performance. Workers must provided with necessary tools, equipment and materials so as to enable them reach their standards.

3. Indirect workers, such as supervisors, foremen, charge hands, helpers, crane operators, canteen staff, store keepers, and clerical staff should also be covered by incentive schemes.

4. There should be management commitment to the cost and time necessary to administer incentive schemes properly and these must be carefully assessed before embarking on an incentive programme. There are many situations in which the potential gains are just not worth the cost and effort involved. It also means a commitment in terms of integrity to the spirit as well as the letter of the programme-having the courage to abide by it when the payout deteriorates and the honour to own up when results are not forthcoming.

5. There is great need for planning. Many incentive scheme, started hurriedly, planned carelessly, and implemented indifferently have failed and have created more problem for the organization than they have tried to solve. This was what happened to the three big plants of Hindustan Steel (now SAIL), where an incentive scheme was introduced during 1960s. Though the initial objective of raising the output of steel was achieved, problems arose regarding production of sophisticated items and improvement of the quality of products. The scheme did not function of sophisticated from the point of view of maintenance of plant and equipment, which, in turn, affected output. The performance of ancillary units like repair shop, was unsatisfactory because incentives in these shops were based on the overall steel production and not the units' own performance. Thus, the need for careful preparation for the installation of an incentive scheme.

6. The other safeguards are:

   (i) The incentive scheme should be appropriate to the type of work carried out and the workers employed

   (ii) The reward should be clearly and closely linked to the efforts of the individual or group.

   (iii) Individual or groups should have a reasonable to calculate the reward they get each of the levels of output they are capable of achieving.

(iv) Individuals or group should have reasonable amount of control over their efforts and therefore their rewards.

(v) The scheme should operate by means of a well-defined and easily understood formula.

(vi) The scheme should be properly installed and maintained.

(vii) Provisions should be made for controlling the amount paid, to ensure that they are proportionate to effort.

(viii) Provisions should be made for amending rates in defined circumstance.

(ix) Create incentives for performance and disincentives for non-performance.

(x) Set and review specific objectives for each employee periodically.

14.7. SCOPE OF INCENTIVE SCHEMES:

Although the incentive payments have a universal appeal, their application is confined to certain important industries. Stated differently, payment-by-results schemes are difficult to apply in:

1. Industries in which measurement of individual or group output is rendered difficult or impossible either by technical consideration or by psychological circumstance shich might be prejudicial to output.

2. Industries in which the control of quality is necessary and is particularly difficult, or in the case of certain classes of workers, where high quality and precision of work is of prime importance; and

3. Industries in which the work is dangerous and it is particularly difficult to ensure the observance of adequate safety precautions.

Barring the above three categories, incentive schemes can be applied to all industries. Specifically, they are being successfully employed in the textiles and metallurgical industries, the metal trades, mining, and many branches of clothing, leather and rubber industries. Incentive schemes have also been successfully applied in certain countries, and in certain circumstances in the building industry and in chemical and other industries.

Generally speaking, systems of payment by results can be most successfully employed in the large companies which can afford to employ administrative and engineering staff needed to ensure an efficient organization of production, quality and measurement of work. However, such systems frequently yield appreciable results in smaller undertakings which may, in case of need, take recourse to the services of experts for the design of incentive schemes.

It is often argued that incentive schemes are more desirable in labour-intensive manufacturing processes. Their application in fully automate plants is doubted. It may be stated that the schemes of payment by results have their role in mechanized enterprises too. But the justification comes for the wrong reasons. It would be easy for an operator to damage a CNC machine or for a programmer to damages that incentive schemes are recommended in fully automated plants.

As a rule, incentives must not be introduced in a newly set-up unit. Workers must be content with time-rated earnings, at least during the first four to five years. This time period is necessary for the unit to carve a niche for itself in the market. This being achieved, it would be easy for the unit to sell the increased output brought in by incentives. Furthermore, as was noted earlier, incentives are likely to affect the quality of output. Any defect in quality would seriously affect fortunes of the newly setup unit, particularly in its formative years.

14.8. WORKING OF INCENTIVE SCHEMES:

Incentive schemes are regarded as beneficial to both employers and workers. They are accepted as a sound technique for the achievement of greater productivity and good performance. The main advantage of any wage incentive scheme is that for a little expenditure of capital, there can be sizeable gains in productivity; the gestation period is also small. The role of supervisors changes to that of managers of "machines and materials" from that of being "watchdogs". The workers chase the supervisors for material, tools, and other accessories, instead of supervisors chasing the workers. The experience gained in India and in other countries indicates that wage incentives have resulted in raising productivity, increasing output and earnings, reducing direct labour costs, and curtailing absenteeism. The NCL has reached the conclusion that, under our conditions, wage incentive is the cheapest, quickest and surest means of increasing productivity.

Despite certain merits of incentive schemes, their actual working is not quite happy. Some critics point out that the output of modern industry does not depend so much on individual human efforts and on the capacity of machines and on good organization. The most effective incentive, they claim, is a combination of good regular wages, good working conditions, and good human relations. There is a tendency for the quality of products to deteriorate unless steps are taken to ensure the maintenance of quality through a stricter system of checking and inspection. Their application in some cases has ot only failed to increase production over a period of time but has caused an actual reduction in employee productivity. One company, for instance found that a substantial increase in pay through wage incentive systems merely resulted in higher absenteeism restricted output and lower work standards.

Some studies indicate that incentives schemes have a dubious value for increasing output. It may generate tensions among the different parts of an organization. Such tensions often create difficult managerial problems, increase administrative cost, and may eventually affect employer-employee relations and output.

14.9. PRINCIPLES AND PROCEDURE FOR INSTALLING INCENTIVE SYSTEM:

Whatever may be the incentive scheme, its proper implementation is very important. Certain principles and guidelines are to be followed to make any incentive scheme more effective and workable. These are:

1. Situational characteristics and constraints of an organization should be analyzed and recognized before an incentive scheme is introduced. These constraints may relate to technology, labour market, product market, raw materials, work standards, and structural factors.

2. The incentive plans should be devised with great care and foresight to enable workers to reasonably understand the foundation and rationale upon which their incentive earnings are based.

3. The workers should be taken into confidence from the beginning and all the features of the proposed scheme should be carefully explained to them in advance. The incentive formula should not only be understandable but should also establish some direct relationship between the earnings of the employee and the quantity and quality of his output. Further, provision should be made for the participation of workers' representatives in the introduction and implementation of the system in an atmosphere of good industrial relations.

4. As wage incentives are intended to reward differential performance, it should not be used as compensation for low wage. They should not become a substitute for general increase in base pay.

5. Production processes, job methods, plant layout, equipment, and material should be improved before the commencement of a wage incentive scheme. The organization should engineer each task to determine the base method, then set standards based upon that best method, and finally instruct workers to follow the same.

6. If any changes in methods study, work measurement, and job evaluation are contemplated, workers should be trained in those new methods.

7. The incentive scheme should cover as many employees as possible to do away with market inequities in earnings.

8. If these are serious irrationalities in the pay packet or wage structure, they should be corrects before the scheme is actually introduced.

9. The incentive earnings should be sufficiently generous to convince employees that they are being adequately paid for their extra effort.

10. The basis for sharing gains of productivity should be fair to employees and are to be worked out in agreement with unions.

11. A periodic review of the working of the scheme should be undertaken if the scheme is to retain its dynamic character and with a view to applying timely correctives.

12. If expertise for designing and implementing the incentive scheme is not available in an organization, advice and assistance of an outside expert or a consultant should be taken. An incentive scheme, if not properly worked out and implemented, can do more harm them good.

13. If the choice for increasing production lies between the system of overtime and incentive bonus, the latter should be preferred. Overtime induces workmen to earn more by slackening their pace of work during the scheduled hours. Thus, it represents a form of disguised unemployment.

14.10. RECOMMENDATIONS OF THE NATIONAL COMMISSION ON LABOUR:

Employers throughout the world continue to press for the more extended use of wage incentive Plans. The drive for such plans is based primarily upon the belief that wage incentives lead to:

1. Greater output;

2. Lower cost per unit of production;

3. Higher earnings for employees and supplementary advantages in the way of reduced absenteeism, easier supervision, and so forth.

The NCL has formulated a number of guidelines for the introduction of incentive schemes. These are

1. Employers and workers should formulate a simple incentive system at the unit level and implement it on some agreed basis through collective bargaining. In every case, introduction of incentives schemes should be preceded by an agreement with trade unions.

2. In evolving wage incentive schemes, it should be ensured that these do not lead to rate-cutting. The workers' normal wages should be protected where it is not possible for him under circumstances beyond his control to earn an incentive.

3. Individual or group incentives can be framed to cover both direct and indirect groups of worker.

4. An incentive scheme cannot be evolved without a work study undertaken with the co-operation of workers. Nevertheless, it should always be open employers and workers to evolve a scheme by agreement or on any other acceptable basis.

5. Efforts should be made to reduce time rated categories to the minimum. This will ensure that all employees have an equal chance to increase their earnings with increase in productivity.

6. Wage incentives should generally provide extra earnings only after a mutually agreed level of efficiency has been achieved.

7. To ensure quality of production, incentive payments should be generally allowed only if the output has been approved on inspection by the management. Relevant norms in this connection should be laid down and made known to workers.

8. Incentive earnings should not fluctuate very much. This requires a certain degree of planning so that material delays, machine breakdowns, etc., are controlled.

9. The scheme should itself safeguard adequately the interests of the works if he is forced to remain idle due to circumstances entirely beyond his control such as non-supply of raw materials, and machine breakdown.

10. Apart from financial incentives, non-financial incentives like better security of employment, job satisfaction and job status have also a place in increasing productivity.

In short, to be successful, a wage incentive plan must be carefully planned, properly installed, and administered in conformance with sound ethical principles of human relations. Any plan, hastily adopted, improperly installed, carelessly administered, or basically unsuited to an individual company cannot succeed. Certain principles or essentials to be borne in mind while installing of an incentive programme are: (i) the plan must simple; (ii) the plan must be equitable (iii) the plan must provide an incentive (iv) the plan must be based on sound job standards (v) the plan must have the backing of the employees and management (vi) the plan must have an in-built provision for a review; and (vii)the plan must not be used to induce workers to work so fast that they are unduly fatigues and their health suffers.

14.11. INCENTIVES AND MOTIVATION:

The incentives are external to the individual and thus, differ from a motive which from his/her internal drives. It implies that management incentives rather than "motivates" people in organizational settings. The process of incentive enables the management to develop their motivation and link it with organizational goals. It serves as a means of satisfying some of their basic needs and thus, motivating them to spend energy in several forms. However, incentives are considered by them in comparison with other characteristics of the work situation rather than independently. Indeed, there is interplay among different types of financial and non-financial incentives and they can be considered within the framework of cognitive dissonance. The cognitive dissonance implies that when the divergence between their input and outcome becomes excessive, people tend to change the situation in some for,. Accordingly, when the outcome of their work is not perceived as being consistent with their input, they may be de-motivated. Explicitly, incentive systems motivate performance when certain specific conditions exist in organizational settings, and they are perceived to be linked with effective performance.

14.12. LINKAGE OF INCENTIVES TO PERFORMANCE:

However, linkage of incentives to performance necessitates an understanding of appropriate measures of performance and specific types of incentives relevant to particular individuals, ability to control their magnitudes which the individuals receive and existence of a climate of trust and confidence in the organization so that people perceive a distinct connection between incentives and their performance. Although incentive compensation is a significant motivator in itself, it can also be used in a supportive way in relation to other motivators in the behavioral and environmental domains. Of course, individuals tend to work more whenever they are confronted with a crisis, or when their work is critical to success of a project. However, it is also supportive to understand that they are getting paid commensurately with the way they raise to the challenge or the crises. Explicitly, incentive compensation, irrespective of other considerations, involves prompt pay-offs and provides more mileage in terms of improved performance than other components of the total package. As movement in a salary range requires both ability and length of service and is based on long-range judgments of performance, one. Likewise, utilization of fringe benefits for improved results is difficult as well as provides little incentive pull.

14.13. IMPROVING THE ROLE OF INCENTIVES:

Notwithstanding the above delimitations, recent behavioral science literature embodies enough guidelines to improve their role. Thus, Lawler formulates a set of propositions relating to the determinants of satisfaction of individuals and characteristics of effective rewards which must be taken into account in designing any compensation (especially incentives) programme in an organization. The propositions relating to the determinants of satisfaction of individuals are as follows: (1) satisfaction with an incentive is a function of both how much people receive and how much they feel should be received (2) their feelings of satisfaction are influenced by comparisons with what happens to others (3) overall satisfaction at work is determined by how satisfied people are with both the intrinsic and extrinsic incentives they receive from their jobs (4) people differ widely in their desire for incentives and in how significant the different incentives are to them, and (5) several extrinsic incentives are significant and satisfying only because they lead to other incentives.

Likewise, the propositions relating to the essential characteristics of an incentive system in the organization are: (1) the organization must provide enough incentives so that basic needs of people are satisfied (2) the incentive levels in the organization must compare favorably with those in other organization, (3) the available incentives must be distributed in a way that people have a perception of equitable distribution In the organization, and (4) the incentive system must deal with organization members as individuals and thus, must take into account differences among people in what incentives they want.

When the above determinants of satisfaction of people and characteristics of incentives are obtained in organization settings, they are likely to effectively perform the following functions: (1) motivate people to join the organization, (2) motivation them to come to work, (3) motivate them to perform effectively, and (4) reinforce the organization structure by specifying their positions in the organization.

14.14. CLASSIFICATION OF INCENTIVE SCHEMES:

Incentives may broadly be classified into monetary or non-monetary. Monetary incentives have an important contribution to make within the total motivation pattern. They provide extra-financial motivation, by rewarding the worker over and above his regular remuneration for performing more than the targeted work. Some of the financial motivations are overtime wages, higher basic wages, incentive bonus, merit increments, suggestion rewards, various allowances, promotion and fringe benefits.

These incentives can be further sub-divided into various kinds. These kinds can be explained with the help of the figure below:

Figure 14.14.1. Types of Incentives

Figure 14.14.1. Types of Incentives

Financial or Pecuniary Incentives	Non-financial Incentives
1. Wages	1. Job Security
2. Salary	2. Recognition
3. Premium	3. Participation
4. Bonus	4. Pride in Job
	5. Delegation of Responsibil
	6. Quick Promotion
	7. Facilities for Developmen
	8. Labour Welfare Amenitie

The various kinds of incentives are discussed below:

1. Financial Incentives

Financial incentives or pecuniary incentives are the most original of all the incentives. It is given in the form of money. The financial incentives still form the most important influencing and motivating factor up to a certain limit. Because it is only by virtue of the monetary compensation that the workers can satisfy their fundamental needs such as food, clothing, shelter etc. The financial incentives may be either direct or indirect. Direct incentives include wages, bonus and other incentives directly given to the workers in the form of cash. Indirect financial incentives include subsistence allowance expenses, medical expenses etc.

2. Non-financial Incentives

Non-financial or non-pecuniary incentives include all other influences planned or unplanned, which stimulate exertion. Mere monetary incentive cannot help the management in solving all the problems of industrial unrest. Further additional cash wage may also tempt the workers to misuse the money in vices like gambling, drinking etc. Under such circumstances, the non-financial incentives have a significant role to play. Such incentives create a healthy atmosphere and change the mental outlook of the workers. They make the working class more stabilized and economically sound. Thus, in short, the workers by virtue of the non-financial incentives are enabled to enjoy a richer and fuller life. Experiences of foreign countries particularly countries like Britain, America and Japan have shown that there is a high degree of positive correlation between non-financial benefit schemes and labour productivity.

Examples of Non-Financial Incentives

Non-Financial Incentives can take a variety of forms. Some of the popular ones are given below:

1. Job Security: The management must try its best to create a sense of job security. There should be no risk of retrenchment, demotion and termination. Experiences have also shown that the productivity is less in those concerns where workers have no feeling of safe and secure. But it is high in those concerns where they have a feeling of job security.

2. Recognition: Recognition of work is the essence of securing good work. Efficient people would naturally like to get recognition for their skill and excellence in their work. Such recognition can do many things that what a cash reward can do. Of course it is not practicable for the superiors to praise everybody for everything done by them. But the technique of praise must be practiced as far as possible.

3. Participation: Workers feel more satisfied when they are given an opportunity to raise their voice in handling the affairs of the enterprise. Since they actually take part in the decision-making their co-operation is assured.

4. Sincere Interest in Subordinates as Individual Persons: The workers must be made to feel pride in their job. Various techniques can be employed to develop pride to work. Food products, dynamic leadership, fair treatment, ethical conduct etc. can effectively stimulate the workers pride in their job and in the firm.

5. Pride in job: The workers must be made to feel pride in their job. Various techniques can be employed to develop pride to work. Food products, dynamic leadership, fair treatment, ethical conduct etc. can effectively stimulate the workers pride in their job and in the firm.

6. Delegation of Responsibility: Delegation of rights and responsibilities to execute a given task often proves to be a strong motivating factor. By delegation the superior trusts his workers and stimulates them to show better results.

7. Other Incentives: Other incentives like quick promotion, provisions of facilities for development and training, provision of labour welfare amenities etc. also have a significant role to play in motivating the employees.

Merits of Incentives

The following are the advantages derived by providing incentives to employees:

1. **Higher output:** By providing incentives to his employees, the employer is able to induce them to work better. This leads to higher output.

2. **Greater profits:** Needless to say, higher output results in greater profits for the business. This happens in two ways. First, the cost per unit becomes less and second, the enterprise is able to keep the selling price low and this result in greater sales.

3. **No problem of idle time:** In an organization where no proper incentives are available for the workers, the tendency will be to while away the time. When suitable incentives are available, the workers become time conscious. They begin to see every minute in terms of money.

4. **Supervision does not pose any problem**: When suitable incentives are available, the workers become duty conscious. The need for close supervision, thus, does not arise.

5. **Efficient workers are able to earn more:** Such of those workers who are highly efficient are able to earn more by way of performance bonus, higher commission and so on.

6. **Possible to identify inefficient and dull workers:** If, in spite of the incentive schemes, some workers are able to earn only their normal wage, it should mean that they are basically dull. The employer, therefore, has to decide whether to retain them or subject them to rigorous training.

7. **Rate of labour turnover is bound to be low:** If adequate incentives are available to the workers, they may not have a feeling of dissatisfaction. Such workers are sure to have greater work commitment and therefore may not leave the organization. The rate of labour turnover, as a result, is bound to be low.

*8***. Reduction in complaints and grievances:** As the organization makes available suitable incentives to the workers, they may not have anything to complain about. This leads to reduction in complaints and grievances.

14.15. PROBLEMS ARISING OUT OF INCENTIVES:

The following problems are bound to arise while implementing an incentive plan:

Quality of work may suffer:

The workers, those in the production department in particular, may give undue importance to the quantity of output produced neglecting the quality of output. Such a problem can be overcome only if the organization has a perfect system of quality control.

Inter-personnel relationships may suffer:

Only those employees who are really efficient will be benefited out of incentives. This may promote ill feelings among the employees of an organization.

Wear and tear of machines may be more:

As the employees are keen on increasing the output all the time, they may handle the machines carelessly. This increases the wear and tear of machines.

Health of the workers may get affected:

Some workers tend to overwork in order to earn more and this may affect their health.

Increase in accidents:

There is always a preference to step up output disregarding even safety regulations and this may increase the rate of accidents in the workplace.

Increase in paper work:

Proper administration of any incentive scheme involves lot of paper work. It necessitates the maintenance of proper records and books.

Requirements of a sound incentive plan:

A good incentive plan shall fulfill the following requirements:

Trust and confidence:

The success of any incentive plan depends on the existence of an atmosphere of trust and confidence between the workers and the management. In the absence of such an atmosphere, the workers may resist any such proposal by the management.

Consensus required:

The management should not take a unilateral decision while evolving an incentive scheme. Consensus between the workers and the management is necessary for the success of the plan.

Assured minimum wage:

Payment to any worker should not be totally related to his performance. Every worker should be assured of a minimum wage notwithstanding performance. Only then the workers would have a sense of security.

No scope for bias or favoritism:

The standards set under the incentive plan should be based on objective analysis. It should not expect too much out of the employee nor should it give scope for bias or favouritism.

Simple to operate:

The incentive plan should not involve tedious calculations. It should be so simple that the worker will be in a position to work out his total earnings himself.

Beneficial to both the workers and the management:

The incentive plan should be beneficial to both the workers and the management. From the management's point of view, it should be cost effective. From the workers' point of view, it should offer return, at a rate higher than the normal rate of wages, for the extra efforts made by them.

Sound system of evaluation:

A perfect system of evaluating the employee's performance should be created in the organization. The results of evaluation should be made known to the employees at the earliest.

Redressing grievances:

Grievances and complaints are bound to arise whenever any incentive plan is in vogue in the organization. Proper machinery should be installed for the quick handling of all such complaints.

Review:

The progress of the incentive scheme should be periodically reviewed. Only then it would be possible to notice and remove defects, if any, in the plan.

4.16. SUMMARY:

The term 'incentive' is gradually acquiring a wide perspective so as to include all possible factors, besides economic gain, which can possibly motivate human beings towards performance. In fact in the Western countries, which have acquire high level of economic development, particularly in the U.S.A., it is being felt that economic gain is ceasing to be a source of motivation and greater emphasis is being placed on non-economic factors, such as status, position, emotional satisfaction, sense of participation etc. under Indian conditions, for obvious economic reasons and very low level of living, economic gain still continues to be the main motivation factor, particularly at workers' level. As such the term incentive in the context of conditions as in India is used in terms of monetary gains. An incentive scheme may be called a monetary incentive scheme it involves "giving a worker an opportunity to earn something more in exchange for more productivity.

14.17. KEYWORDS:

Wage Incentive

Remuneration

Deterioration

Performance

Management

14.18. SELF ASSESSMENT QUESTIONS:

1. What is meant by wage incentives? Give attributes of a good incentive plan.
2. Both monetary and non-monetary incentives are necessary for inducing worker to do more work.
3. Is there any relationship between incentive system and motivations? Examine the potential advantages and disadvantages of incentives.
4. What is the significance of incentives? Describe the different types of incentives.
5. Are incentives relevant in India Industry? Suggest measures to effectuate them at enterprises level.
6. Define 'incentives'. Bring out their advantages and limitations.
7. Bring out the perquisites for the success of incentive payments.

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Lesson-15

WAGE INCENTIVE SYSTEMS IN INDIA

15.0 OBJECTIVE:

After reading this lesson, you should be able to:

- Understand the Features of Incentive systems
- Indentify the Types of Incentive Schemes in Indian Industries
- The Application of Incentive Schemes in India Industries
- Describe the Steps Involved in Installing an Incentive Plan

STRUCTURE:

15.1 Introduction

15.2 Need for wage incentives in India

15.3 Features of Incentive Payments in India

15.4 Installing an Incentive Scheme

15.5 Categories of incentive plans

15.6 Group Incentive Plans

15.7 Incentives for Indirect Workers

15.8 The Findings of Selected Studies on Incentives: The Findings of Labour Bureau

15.9 The Findings of NPC

15.10 Incentive Systems in Public Sector Undertakings

15.11 The Viewpoints of Wage Boards and NCL

15.12 The Viewpoint of Subramanian

15.13 Summary

15.14 Keywords

15.15 Self Assessment Questions

15.16 Further Readings

15.1 INTRODUCTION:

In our country, the role of financial incentives as a primary tool for motivating workers cannot be over emphasized. Besides, the necessity for raising the productivity of Indian Labour is also getting due attention. Different five-year plans have recommended the introduction of incentive schemes under certain conditions. The need for introducing wage incentive schemes in our country has been felt because of: (a) the efficiency of the Indian worker is very low, and as such the wage incentives can lay an important part in improving his efficiency; and (b) the average Indian worker is financially poor, and therefore, incentives are likely to tempt him to work better. The most widely prevalent incentive scheme in Indian industries is the piece rate system. Apart from this there is also the system of payment of production bonus, usually at a differential rate for the output produced in excess of the normal output for a unit of time. Further, there are group incentive plans, or individual incentive plans, or a combination of both. One or the other schemes have been applied extensively in many industries in our country, particularly in textile, metallurgical, the metal trade, mining, leather and rubber.

A survey covering the mining and manufacturing sectors found that 45 percent of the units surveyed had incentive payment schemes of one sort or another. Of these, 76 per cent were group incentive schemes, 22 per cent were individual incentive schemes, 8 per cent were piece rate schemes with a guaranteed minimum and the remaining 14 per cent were classified variously as multi-factor schemes, attendance bonus schemes, and indirect workers' incentive schemes, and so on. In India, the introduction of incentive payment in a vast number of medium and small scale industries may result in improving the utilization of equipment and manpower and given an impetus to productivity, result in higher earnings to the workers, and bring down costs of the products.

Incentive is an act or promise for greater action. It is also called as a stimulus to greater action. Incentives are something which is given in addition to wagers. It means additional remuneration or benefit to an employee in recognition of achievement or better work. Incentives provide a spur or zeal in the employees for better performance. It is a natural thing that nobody acts without a purpose behind. Therefore, a hope for a reward is a powerful incentive to motivate employees. Besides monetary incentive, there are some other stimuli which can drive a person to better. This will include job satisfaction, job security, job promotion, and pride for accomplishment. Therefore, incentives really can sometimes work to accomplish the goals of a concern. The need of incentives can be many:

1. To increase productivity,

2. To drive or arouse a stimulus work,

3. To enhance commitment in work performance,

4. To psychologically satisfy a person which leads to job satisfaction,

5. To shape the behavior or outlook of subordinate towards work,

6. To inculcate zeal and enthusiasm towards work,

7. To get the maximum of their capabilities so that they are exploited and utilized maximally.

Therefore, management has to offer the following two categories of incentives to motivate employees:

1. **Monetary incentives:** Those incentives which satisfy the subordinates by providing them rewards in terms of rupees. Money has been recognized as a chief source of satisfying the needs of people. Money is also helpful to satisfy the social needs by possessing various material items. Therefore, money not only satisfies psychological needs but also the security and social needs. Therefore, in many factories, various wage plans and bonus schemes are introduced to motivate and stimulate the people to work.

2. **Non-monetary incentives:** Besides the monetary incentives, there are certain non-financial incentives which can satisfy the ego and self- actualization needs of employees. The incentives which cannot be measured in terms of money are under the category of "Non- monetary incentives". Whenever a manager has to satisfy the psychological needs of the subordinates, he makes use of non-financial incentives. Non- financial incentives can be of the following types:-

   a. **Security of service-** Job security is an incentive which provides great motivation to employees. If his job is secured, he will put maximum efforts to achieve the objectives of the enterprise. This also helps since he is very far off from mental tension and he can give his best to the enterprise.

   b. **Praise or recognition-** The praise or recognition is another non- financial incentive which satisfies the ego needs of the employees. Sometimes praise becomes more effective than any other incentive. The employees will respond more to praise and try to give the best of their abilities to a concern.

   c. **Suggestion scheme-** The organization should look forward to taking suggestions and inviting suggestion schemes from the subordinates. This inculcates a spirit of participation in the employees. This can be done by publishing various articles written by employees to improve the work environment which can be published in various magazines of the company. This also is helpful to motivate the employees to feel important and they can also be in search for innovative methods which can be applied for better work methods. This ultimately helps in growing a concern and adapting new methods of operations.

   d. **Job enrichment-** Job enrichment is another non- monetary incentive in which the job of a worker can be enriched. This can be done by increasing his responsibilities, giving him an important designation, increasing the content and nature of the work. This way efficient worker can get challenging jobs in which they can prove their worth. This also helps in the greatest motivation of the efficient employees.

   e. **Promotion opportunities-** Promotion is an effective tool to increase the spirit to work in a concern. If the employees are provided opportunities for the advancement and growth, they feel satisfied and contented and they become more committed to the organization.

The above non-financial tools can be framed effectively by giving due concentration to the role of employees. A combination of financial and non- financial incentives help together in bringing motivation and zeal to work in a concern.

Positive Incentives: Positive incentives are those incentives which provide a positive assurance for fulfilling the needs and wants. Positive incentives generally have an optimistic attitude behind and they are generally given to satisfy the psychological requirements of employees. For example-promotion, praise, recognition, perks and allowances, etc. It is positive by nature.

Negative Incentives: Negative incentives are those whose purpose is to correct the mistakes or defaults of employees. The purpose is to rectify mistakes in order to get effective results. Negative incentive is generally resorted to when positive incentive does not work and a psychological set back has to be given to employees. It is negative by nature. For example- demotion, transfer, fines, penalties.

15.2 NEED FOR WAGE INCENTIVES IN INDIA:

The need for wage incentive schemes in India is felt due to the following reasons:

(i) The efficiency of the Indian worker is very low, and needs to be raised. Wage incentives can play an important part improving his efficiency.

(ii) The average Indian worker is financially very poor. Financial incentives therefore are likely to temp him to work better.

(iii) India is at a low level of technology, and wage incentives can help in promoting the use of electronic devices.

(iv) A proper application of wage incentive schemes can so affect the prices that the community would be benefited.

(v) In the national interest, it is felt that wage incentive schemes should be applied to all economic activities.

15.3 FEATURES OF INCENTIVE PAYMENTS IN INDIA:

Introduced in 1946, incentive payments have become highly popular in our industries. They are as common as monthly wages and salaries. But the schemes in operation defy any generalization because no two plants follow an identical scheme. The schemes differ from industry to industry, and from plant to plant within an industry. Some of the incentive schemes described by the ILO are followed here, but not in their original from. They have been modified to suit the local requirements. This is necessary because the implementation of incentive schemes, in their original form, necessitates work measurement and standardization of operations which, in many cases, are not possible in our industries.

Thus, the features of incentive payments are:

1) Though incentives are as old as industries themselves, it was only in 1946 that they were introduced in our country. Even to this day, the incentive schemes are in their infancy.

2) In most industrial establishments, the introduction of incentive schemes has not been preceded by work studies, consultation with workers' representatives and rationalization of wage structure through job evaluation.

3) Incentive schemes differ from industry to industry and from plant to plant within an industry.

4) Most incentive schemes in operation fall under one or the other of the four classes mentioned by the ILO. But the schemes are fine-turned to suit the requirements of the organization.

5) The schemes in public sector plants have an extremely varied coverage, some applying only to day-rated employees while other are being made applicable right up to the top management.

6) Inflation has reduced the motivational effect of incentives. Hence, incentives have to be substantial, if workers are to be motivated for higher efficiency and greater output.

7) In many cases, incentives seem to have achieved their objectives, that is increased productivity and enhanced earnings.

15.4 INSTALLING AN INCENTIVE SCHEME:

Incentive programs are not new: weren't we rewarded if you brought home a good report card or cleaned our room? That, in its most basic form, is an incentive program — rewarding good behavior.

However, employee incentive programs tend to compensate those employees who go "above and beyond" their typical duties and excel in ways that help the company achieve a higher profit margin, make more sales, garner more leads, etc.

An incentive also gives the employee a more personal stake in the company's mission; if the company excels, the employee benefits.

Depending on our company's goals, an incentive program can push workers to perform more efficiently, according to Victoria Downing, president of Remodelers Advantage and a regular REMODELING columnist. "It's a carrot to get people to do their work faster and better," she says, adding that one of the trickiest parts about incentives is being sure the goal is clearly understood and thinking through how it will affect the whole company.

There are as many types of incentive program as there are uses for duct tape. Depending on what you hope to achieve, you have to decide which type works for your company and your employees. According to Jennifer Loftus, national director at Astron Solutions, a New York–based human resources consulting firm, there are three main categories for incentive plans: individual, group, and company. "Individual plans reward each employee based on their own merits and can be tailored to suit the employee," she explains, adding that the rewards can range from cash or gift cards to trips, tools, and so on.

Group plans are for individual work groups. Each group would need to adhere to a set standard or measure. "For every single employee, there has to be a line of sight," Loftus says. "An employee must understand how his performance affects the company's goals."

The companywide plan is typically a standard profit-sharing program: if the company meets — or exceeds — its goals for the year, quarter, or month then the entire company gets a piece of the action.

Loftus says that while company-wide plans weave in very nicely throughout an organization, some employees may still not have that clear line of sight as to how their job affects the company's overall profitability. "If an employer wants to send a message that 'We are a team,' an organization-wide incentive or profit-sharing plan is best," she says.

It's not unusual to reap unexpected rewards when we institute any type of new management program for our business. Incentive programs have the potential to provide a wealth of unintended consequences. When Bob Ender at Dream-Maker Bath & Kitchen instituted the incentive programs for his sales and labour teams, he realized some surprising benefits.

· **Equitable pay structure:** Now there's one pay structure across the board, according to Ender. "So there's no bickering amongst employees and no animosity because everyone's on the same pay scale," he says.

· **Increased customer satisfaction:** In an industry notorious for running jobs longer than estimated, Dream Maker consistently beats deadlines, Ender says, adding that this has led to improved customer satisfaction numbers in his Guild Quality survey results.

· **Better cost control:** Because deadlines are being met, there are fewer unplanned man hours to pay for. Idle time and lumber runs are also down.

· **Improved estimating:** "Because the database is improved, we see less general slippage from a company standpoint and therefore we're seeing fewer change orders," Ender says. This not only makes his clients happy, it also leads to more thorough proposals by the sales team.

· **More checks and balances:** Now the workers keep an eye on one another's progress because they don't want someone's lackluster performance to affect their own compensation.

Installing a scheme of payment by results must proceed on the following lines:

1) Define the objectives of the payment system and, if necessary, challenge the assumptions held about the purpose of the system and how it should operate.

2) Collect facts about the existing system-the structure, the types of payment schemes in use, the number of people paid under each arrangement, the levels of earnings in different occupation, and the make-up of earnings, including overtime payment.

3) Analyze the circumstances in which the payment system operates.

4) Compare the existing or proposed arrangement against the criteria for evaluating system listed above.

5) Analyze the effectiveness of the pay structure and payment systems by:

   i. Comparing the results achieved with the objectives of the system under such heading as ability to attract and retain staff, effect of productivity, and effect on management employee relationships.

   ii. Identifying particular problem areas where the system is producing anomalies in pay or earnings between occupations or units, where the requirements of the equal-pay legislation are not met or where rates of pay are not competitive with local going rates.

6) Consider conducting an attitude survey to obtain the views of workers, rate fixers and supervisors about the present system and the changes need to be made.

7) Consult as required with unions and employees on the present arrangements and what needs to be done about them.

8) Conduct pay surveys as required to establish local market rates.

Tips for developing an incentive structure:

1. **Creating an appropriate and optimal mix of incentives of different types:**

   a. **Financial incentives** can be important, but don't always work and are most effective if combined with non-financial incentives

   b. In particular **merit based schemes** for recruitment, promotion and professional development opportunities are effective incentives. Merit incentives do not have to be formal – simple recognition of effort and results can be highly motivating. Pride, prestige and public recognition are also powerful incentives.

c. **Accountability** is another non-financial incentive. The external environment can be both the source of 'demand-side' calls for good performance and accountability. There are many opportunities to introduce accountability incentives linked to service standards and customer satisfaction, for beneficiaries groups, management, local or national politicians, and or donors

d. Another type of non-financial incentive is **benchmarking and competition**, to stimulate healthy competition between different work units.

e. **Training** needs to be used with caution as it can become a perverse incentive

f. It is important to be careful of unintended negative consequences.

2. **Linking incentives and good human resource management:** a key factor in improving public sector performance is to have in place incentive structures that attract, retain and motivate staff and hold them accountable for their performance. Internal incentives therefore need to be used in conjunction with staff management and performance processes that are embedded in the organizational culture and how performance is rewarded and punished.

3. **Targeting**: who is most likely to contribute towards sustainable capacity if appropriately motivated and rewarded?

4. **Sequencing**: some incentives can be dealt with quickly at an operational level, but some need policy level change that will take time to resolve, so it is important to sequence the introduction of incentives accordingly.

5. **Attention to culture and context**: the enabling environment is highly pertinent because it can be the most powerful source of both formal and informal incentives that either provide or block capacity development and the source of incentive resources. Where officially sanctioned and supported formal incentives are missing, the situation often creates informal incentives that work against capacity development

6. **Creativity**: small expenditure on activities like team building or workplace upgrading that are not usually thought of as capacity development can create the conditions for capacity development to happen.

15.5 CATEGORIES OF INCENTIVE PLANS:

Incentive plans are used to motivate employees to increase production. According to the business resource Business Town, employees given an incentive plan tend to feel more attached to the company's success and may work harder to help achieve it. Incentives can come in many forms. Before you formulate your motivational program, it would help to understand different types of incentive plans.

A stock option is an incentive offered to employees that want to invest their money into the company stock by purchasing stock with pre-tax money. According to HR Guide, employees that participate in a stock option incentive plan are able to defer paying income tax on the gains realized by their stock purchases until the stock is sold. The company itself does not get any kind of tax break by offering a stock option incentive, but it does reap the benefits of selling more stock.

According to the Society for Human Resource Management, one type of incentive plan for executives is known as the performance unit. In the executive's agreement there is a schedule of financial milestones that the company must achieve for the executive to get awarded a pre-determined amount of units. The amount of a performance unit varies by company. Performance units are paid out based on a schedule agreed to by the executive and the company.

The bonus pay structure is common in professions such as sales, marketing and production. When the employees reach a predetermined goal, the company may create an incentive plan that pays a bonus for going beyond that goal. For example, if a manufacturing plant has a goal of 100 units in a month, the company may offer to pay each employee a bonus for each unit manufactured beyond 100 in that month.

Individual incentive plans and group incentive plans both have a similar goal. They strive to provide an incentive that will drive the right kind of performance for the company. For the company to determine the best incentive options, they must first know their goals and ensure those goals are within the individual's ability to impact. In a BLR webinar titled "Compensation 101: Essential Secrets and Strategies for HR Professionals," Paul R. Dorf outlined some of the considerations when determining whether individual or group incentive plans are most appropriate.

Under this plan, earnings are directly related to the performance of the individual employee, Individual incentives may be based on time or output. In time based plans, a standard time is determined and incentive is paid if an employee completes the job in less than the standard time. In Output based plans, a standard of output determined and an employee produce more than the standard output is given incentive.

Output linked incentives are of the following types;

1. Earnings varying in proportion to output.
2. Earnings varying proportionately less than output.
3. Earnings varying proportionately more than output.
4. Earnings varying differently at different levels of output.

1. Individual Incentive Plans: Individual incentive systems attempt to relate individual effort to pay. Individual incentive plans are based on meeting work-related performance standards, such as quality, productivity, customer satisfaction, safety, or attendance. They are most appropriate when:

- Performance can be measured objectively

- Employees have control over the outcomes

- Plan does not create unhealthy competition

Individual incentive plans require monitoring, and it is important to remember that the incentive scheme is not a substitute for good management.

Spot bonuses can also be used for individuals to show appreciation or give recognition for a job well done. This can be a reward for developing new skills, contributing new ideas, obtaining licenses, or finishing projects early. Typically, a spot bonus is given as a one-time discretionary payment. These are most prevalent among non-executives.

Conditions necessary for the use of individual incentive plans are as follows:

1.Identification of individual performance: The performance of each individual can be measured and identified because each employee has job responsibilities and tasks that can be categorized from those of other employees.

2. Independent work: Individual contributions result from independent work and effort given by individual employers.

3. Individual competitiveness desired: Because individuals generally will pursue the individual incentives for themselves, competition among employees will occur. Therefore, independent competition whereby some individuals "win" and others do not must be desired.

4. Individualism stressed in organizational culture: The culture of the organization must be one that emphasizes individual growth, achievements, and rewards. If an organization emphasizes teamwork and cooperation, then individual incentives will be counterproductive.

Individual Incentive Plans are also two types. These are

1. Time- based Plans

2. Output- based Plans

Figure 15.5.1. Individual Incentive Plans

Figure 15.5.1. Individual Incentive Plans

Time-based Plans:	Output-based Plans:
1. Hasley's Plan	1. Taylor's Differential Piece Rate Plan
2. Rowan's Plan	2. Merrick's Multiple Piece Rate Plan
3. Emerson's Plan	3. Gnatt's Task Plan
4. Bedeaux's Plan	

15.5.1 Time-based Individual Incentive Plans

15.5.1.1 Halsey's Plan

F.A.Halsey, an American engineer, introduced this plan. Under this plan, standard time is determined for each job. A worker who completes the job by taking the standard time or even exceeding it is paid normal wages calculated at the time rate. In case, he completes the job in less than the standard time, he is given bonus equal to 50% of the money value of the time saved.

The bonus payable to the worker and his total earnings, under the Halsey's plan, are calculated as follows:

Bonus = 50% (Time Saved x Time Rate)

Total Earnings = Time Rate x Time Taken + Bonus

Merits of Halsey's Plan

The following are the plus points of Halsey's plan:

1. It is simple to understand.

2 The workers are assured of a minimum wage.

3. The employer and the worker share equally the benefit resulting from savings in time.

4. The plan encourages workers to be more efficient in their work.

Demerits

Halsey's plan, however, suffers from the following limitations:

1. The efficiency of the worker is rewarded to the extent of50% only.

2. The time saved is wholly due to the efficiency of the worker but the management grabs 50% of the resulting benefit.

3. The plan does not say anything about, the quality of the work done.

15.5.1.2 Rowan's Plan

James Rowan devised this plan. Under this splan, the manner of calculating bonus is slightly different from that under the Halsey's plan. Bonus, under Rowan's plan is calculated as follows:

Bonus = % of Time saved x Time Wage

Standard Time

Total Earnings of the worker = Time Wage + Bonus

Merits

The following are the positive aspects of Rowan's plan:

1. Minimum wage is guaranteed to all workers.

2. When compared with Halsey's plan, bonus under Rowan's plan is more although the basic time wage is the same under both the plans.

3. The plan provides a check against over-speeding by workers. As the worker saves more time, his bonus and total earnings only begin to decline. In the above illustration, suppose, the worker completes his task within one hour, i.e. he saves 4 hours, his bonus will only be Rs.16. He earns the same bonus of Rs.16 by completing the task in 4 hours, saving just one hour.

Demerits

The drawbacks of Rowan's plan are given below:

1. It is not as easy as Halsey's plan is.

2. The earnings of the worker become less as he saves more time. This discourages efficient workers.

15.5.1.3 Emerson's Efficiency Plan

Herrington Emerson devised this plan. Under this plan too minimum wage is guaranteed to all workers. Payment of bonus, however, is related to the efficiency of the workers. Efficiency is determined by the ratio of time taken to standard time. Usually, a worker is given bonus only when his level of efficiency, in terms of percentage, is above 66.67%.

Earnings= (Time taken × Rate per hour) + (% of Bonus × Time taken × Rate per hour)

Merits

The following are the advantages of Emerson's efficiency plan:

1. Minimum wage is guaranteed.

2. It pays bonus to workers based on their level of efficiency.

3. The 66.67% or two-third efficiency criterion is within the reach of many workers.

Demerits

The disadvantages of the plan are as follows:

1. It is not a straight-forward approach to determining bonus.

2. If the standard time allowed itself is low, it may not be possible for many workers to fulfill the efficiency criterion laid down under the plan. .

15.5.1.4 Bedeaux's Plan

Charles Bedeaux devised this plan. Under this plan, the standard time and time taken for each job is reduced to minutes, and each minute is referred to as "B", i.e., one hour is the same as 60 B's. The bonus and total earnings of the worker, under the plan, are calculated as follows:

Bonus = 75% (Standard Time - Time Taken) x Time Rate

Total Earnings = Time Wage + Bonus

Merits

The benefits of Bedeaux's plan are:

1. It guarantees minimum wages to the workers.

2. It enables efficient workers to earn more.

3. The benefit of three-fourth of the time saved is given to the worker.

Demerits

The weaknesses of the plan may be stated as follows:

1. The unit name of 'B' in place of the 'minute' does not make the plan altogether different.

2. The entire benefit of time saved by the worker is not passed on to him.

15.5.2 output-based individual incentive plans

15.5.2.1 Taylor's Differential Piece Rate Plan

F. W.Taylor, who is known as the *Father of Scientific Management,* developed the differential piece rate plan. Under the plan, two piece rates are laid down –

(i) A lower rate for those workers who are not able to attain the standard output within the standard time; and

(ii) A higher rate for those who are in a position to produce the standard output within or less than the standard time.

Under the plan, standard time for every work is determined on the basis of time and motion study. Two rates of payment are determined high rate and low rate. Workers completing their work within or before standard time are paid according to the high rate and workers completing work in more than standard time are paid at low rate.

Taylor's differential piece rate plan has the following components:

(i) Standard Output.

(ii) Standard Time

(iii) A Lower Piece Rate and

(iv) A higher Piece Rate

Merits

The following are the merits of Taylor's differential piece rate plan:

1. It is easy to understand and simple to operate.

2. It enables efficient workers to earn more.

3. Workers not reaching the standard are paid at a lower rate. Such people, thus, are punished for their inefficiency. This protects the interests of the organisation.

Demerits

The limitations of Taylor's plan are given below:

l. It does not guarantee minimum wage. This creates a sense of insecurity for the workers. .

2. There may be ill-feelings among workers in view of the differential piece rates.

3. The quality of the output is ignored.

15.5.2.2 Merrick's Multiple Piece Rate Plan

Under this plan too a standard task is set for the workers. But unlike Taylor's plan that provides for two differential rates, Merrick's plan contemplates three rates as shown below:

(i) Workers producing less than 83% of the standard output are paid at a basic rate.

(ii) Workers producing between 83 % and 100% of the standard output will be paid 110% of the basic piece rate.

(iii) Those producing more than the standard output will be paid at 120% of the basic piece rate.

Merits

The merits of the plan may u~ stated as follows:

1. It is an improvement over Taylor's plan.

2. It has greater flexibility.

3. It offers greater scope for efficient workers to earn more.

Demerits

The following are, probably, the drawbacks of the plan:

1. It is a complicated plan.

2. Even a worker achieving 83% target is branded as a poor performer.

15.5.2.3 Gantt's Task Plan

H.L. Gantt devised this plan. This plan guarantees minimum daily wage. Its special feature is that it combines time rate, piece rate and bonus. A worker who is unable to produce the standard output receives only the time wage. He becomes eligible for bonus only when he attains or exceeds the standard output within the standard time. The rate of bonus varies between 20% to 50% of his/her wages.

Output	Payment
Below standard	Guaranteed time rate
At standard	120% of time rate
Above standard	120% of time rate

Merits

The plus points of Gantt's task plan are:

1. It has, as mentioned above, time wage, piece rate and bonus. It is, therefore, a three-in-one scheme.

2 It guarantees daily minimum wage.

3. It provides enough opportunities for efficient workers to earn more.

Demerits

The weaknesses of the plan are:

1. It is not easy to understand.

2. The fluctuations in the output levels, of different workers not attaining the standard, are ignored and they all receive the same daily minimum wage. In the illustration given above, if two workers produce 6 units and 8 units respectively (against standard output of 10), each is assured a daily wage of Rs.50.

15.6. GROUP INCENTIVE PLANS:

Group incentive plans are initiatives designed to encourage and reward exceptional levels of professional achievement. You can use incentives in your small business as motivators for staffers to work collectively to earn monetary and non-monetary rewards. It is also a way for small business owners to boost overall productivity and earnings while simultaneously rewarding employees for a job well done. The objective of team incentives is to encourage group goal-setting, collaboration and group work.

Group incentive wage plans motivate the group to produce more under individual incentive plans, bonus is paid to the workers on the basis of individual performance and the amount of bonus payable to a worker is not affected by the performance of another or other workers. But there are certain situations where it is difficult to measure the output of an individual worker conveniently or the performance of one worker is affected by the performance of other workers. In such situations, group incentive bonus schemes are introduced. Under this scheme, bonus is made payable to all the workers on a collective basis. This bonus is promised by management in advance of the commencement of work for securing in effective teamwork. In all cases, a fixed standard of performance is established and the bonus is given for the results shown over the standard performance.

There are different types of group incentive schemes. Important among them are as follows:

(1) Priest man Plan: This system of wage payment was first used by Priest man's of Hull in 1917. It is applied to workers who work in groups. It provides for payment of group bonus in addition to the ordinary time rate to the individual workers. Thus if during a year, an enterprise is able to reach the predetermined standard output or exceed the previous year's output, workers are paid increased wages in the same ratio in which output has increased. For example, if in 1990, the output per worker-hour was 10 units and in 1991, it rises to 11 units per worker-hour, the wages in 1991 would be 10% higher than those in 1990. An advantage of the system is that it brings about team-spirit among the workers of a group. If the group as a whole works well, this is bound to add to overall output of the enterprise and in that case all the workers would stand to benefit.

But its disadvantage is that it may be insufficient to motivate individual workers, particularly these who possess greater skills and experience.

(2) Scanlon Plan: Named after Mr. Joseph Scanlon of United States; this plan is the most popular for shaving the gains from increase in productivity. It provides for payment of 10% participating bonus for every 10% increase in productivity. The benefit is extended to all employees except the members of top management.

Under the plan, workers are not paid the entire amount of bonus earned by them in any month. One half of the first 15% of such bonus is set apart for the creation of a reserve fund. This fund is used to neutralise the effects of any fluctuations in labour costs. In case a part of such fund remains unused, it too is distributed among the workers in the last month of the year and then a new fund is a created for the New Year.

(3) Productive Bargaining: Management and workers of an enterprise may reach an agreement under which workers agree to give up unproductive wasteful practices such as go-slow and work to rule and in return, the management agrees to link the wages and concessions of increase in productivity. For this, it is necessary that there should be a strong trade union to force the workers to honour the agreement. In case there are too many unions not cooperating with one another such agreement has little chance of succeeding.

(4) Co-partnership: Under this certain employees are given the option of buying the shares of the enterprise at reduced price in installments. The employees are chosen on the basis of seniority or wage levels. Its assumption is that as a shareholder of the company. An employee is likely to show greater understanding of the company's viewpoint and behave more responsibly. As for management, it can cite such schemes as proof of its enlightened outlook and thus brighten the public image of the enterprise.

(5) Profit sharing: It is an agreement (formal or informal) freely entered into, by which an employee receives a share fixed in advance of the profits. In other words, Profit sharing is the most popular method rewarding the employees. Under it, the employees are paid in addition to the regular wage, a particular share of the net profits of the business as incentive.

Characteristics of Profit Sharing

The key features of profit sharing may be stated as follows:

1. It is based on an agreement between the employer and the employees.

2. It is a payment made after ascertaining the net profits of the business. It is not therefore, a charge on profits.

3. The amount paid to the employees is over and above their normal pay.

4. The amount to the paid is determined based on some agreed formulas.

5. The payments based on seniority and wage level of individual workers.

Merits of Profit Sharing

The advantages are profit sharing are as follows:

1. Better employer-employee relations - This is possible, as the employer is ready to share the profits of the enterprise with his employees.

2. Increase in productivity -The employees make every possible effort to increase productivity because they know very well that higher profits for the enterprise would mean higher bonus for them.

3. Better living standards - It helps to increase the living standards of the employees as the amount received is in addition to the usual wages.

4. Reduced costs of supervision - The workers themselves are duty conscious and, therefore, they need no close supervision. Thus, costs of supervision are reduced.

5. Promotion of team spirit - The employees know the importance of Teamwork, as only such an effort would result in higher output.

Limitations of Profit Sharing

The limitations of profit sharing are as follows:

1. Regular income not assured: Payment to workers, by way of profit sharing, at a particular rate depends upon the profits of the enterprise. If the enterprise makes low profits or incurs losses, it will not be in a position to pay bonus as agreed.

2. Suppression of profits: Attempts may also be made to suppress true profits so that the employees need not be paid their share. This is done by manipulating accounts.

3. No inducement: Payment under the profit sharing scheme will be made to the employees once or twice a year when accounts are closed. Such, payments at longer intervals may not really motivate employees. Daily or weekly incentive payments are far more superior to profit sharing.

4. All workers paid alike: Payment to workers under profit sharing is made without considering their relative level of efficiency. This amounts to doing injustice to those who have really made target attainment possible.

15.7 INCENTIVES FOR INDIRECT WORKERS:

Indirect workers such as crane operators, helpers, charge hands, canteen staff, security staff, employees in purchasing, sales and accounts, and maintenance staff also deserve incentives at par with direct workers. Incentives should be paid to such workers either on the ground that they contribute to the increased production which the direct workers may achieve or on the ground that their work has increased because of increased production, or both. Such payments are desirable to avoid dissatisfaction and dissension among the workers in a plant, or even strikes, which may result if indirect workers are paid at time-rates while direct workers receive substantial bonus.

The payment of bonus to indirect workers poses a serious problem because the output of many of them cannot be accurately measured. For example, it is extremely difficult to measure the output of maintenance staff, security personnel, or canteen employees, through it is possible to assess the performance of inspectors, sweepers and packers.

But whether the output of indirect staff can be measured or not, a single system of bonus payment is made applicable to all of them. In some cases, the bonus is calculated according to some agreed percentage on the output of the plant or of a department. In others, the bonus is a specified percentage of the incentives of all or some of the direct workers. Much management, however, prefer to apply a merit-rating system to indirect workers, which rewards these workers for other qualities, in addition to their output.

15.8 THE FINDINGS OF SELECTED STUDIES ON INCENTIVES:

THE FINDINGS OF LABOUR BUREAU:

The Occupational Wage Survey conducted by the Labour Bureau in 1958-59 revealed that 31.8 per cent of workers in factories and industries, 75.4 per cent in plantations and 57.8 per cent in mines were engaged on piece-rate system connected with an incentive scheme. This system was limited to industries and occupations where the output of the worker or a group of workers can be measured with reasonable accuracy, and quality of the product can be controlled to a satisfactory extent. As another study conducted by the bureau on incentive schemes operating in industrial units during 1956-57 indicates, these schemes prevailed mostly in iron and steel, aluminum, engineering, cement, paper, cigarette, textiles, chemicals and chemical products, mining and glass industries, and they mostly started during or after 1946. In more than half of the units under study, these schemes were formulated in consultation with the concerned workers. The group system of incentive payment was more frequently used than individual incentives, ‘n large organizations especially in iron and steel, aluminum, paper, and match industries, there was linkage of incentive payments with the total production of the plant or the organization as a whole. There also prevailed incentives schemes related to the productivity of individual workers or groups of workers in engineering and cigarette manufacturing industries. In addition, gold mines, some glass and cement factories, and printing presses were marked by incentive, bonus to workers for performance beyond the prescribed norms. There was also a practice of differentiating production workers from non- j production workers in terms of incentive bonus. Even where both types of workers were entitled to incentive bonus, the rates for non-production workers were lower than production workers. The j period of payment of incentives ranged from a fortnight to a year depending upon the nature of the incentive scheme.

15.9 THE FINDINGS OF NPC:

The National Productivity Council (NPC) conducted a survey to explore the status of incentives in Indian industry in the mid-sixties. Out of 1,000 undertakings selected for survey, 85 responded to the questionnaire. Of these 85 organizations, 60 had some kind of incentive scheme and covered varied industries such as light and heavy engineering, textiles, aluminum, chemicals and mining. Nearly one-third of these organizations possessed a straight piece-rate system without a “fall back” wage, while the remaining two-thirds of them had the piece-rate system with a “fall back” wage. Nearly one-third the undertakings provided incentives to all workers, whereas two-thirds of them limited incentives to production workers. In all cases, the incentive bonus was linked to output. Other factors which were considered in calculating incentive bonus included quality, regularity in attendance, waste reduction and reduction in breakdown repairs.

15.9.1 ANOTHER STUDY’S FRINGE:

A study conducted by Sethuraman and Muthu krishnan to analyze the impact of monetary incentives on productivity indicates that incentive schemes exerted a positive impact on productivity, labour cost and industrial relations. They concluded that “money” had a “salutary” effect on production.

15.10 INCENTIVE SYSTEM IN PUBLIC SECTOR UNDERTAKINGS:

A team of Russian experts assessed the relevance of incentive schemes for public sector undertakings in 1960. As the study revealed, the wage system in the public sector organizations was based on the length of service of the workers rather than on their efficiency and thus, there prevailed divergent wages for doing the same quality and quantity of work. The team recommended reduction of wage divergence for similar occupations and linkage of wages with the workers’ levels of skill and the complexity of equipment operated by them. It stressed the need for a gradual switch over to a system of payment based on quality, quantum of labour and skill for all workers and progressive withdrawal of the system of fixing wages on a seniority basis. The team also recommended payment of bonus to all personnel including engineers and technicians, and administrative persons involved in it. It also suggested the need for creation of a fund out of the profits and savings stemming from increased production equipment. A study cited by National Commission on Labour revealed that productivity had been progressive increasing and unit costs falling in the Chittaranjan Locomotive Works where incentive schemes were operating since 1954.

‘Lobo’ while describing the incentive scheme in Visvesvaraya Iron and Steel Industry Ltd. (VISL) points out that the system of incentives adopted in public sector enterprises in India has been usually such that it resulted in provided a flat rate of additional wages mostly based on production. But the problem faced by the government is that if incentives in the form of bonus are given at a certain rate to one industry, the workers of other industries demand the same, and invariably the story ends with the government yielding to such demands and declaring bonus at a certain rate for all workers irrespective of productivity of the individual industry. With such as policy, bonus ceases to be a bonus.

At the time of the study there were three bonus schemes in force in VISL including the production bonus scheme and a scheme of incentive bonus. The production bonus scheme provides for a minimum bonus of 2 per cent on the level of production reaching &0 per cent. The bonus is increased to 8 per cent if the level of production approaches 102 per cent and to 18 per cent if the level reaches 120 per cent. This is supply presented by a special incentive bonus scheme to provide for production exceeding 120 per cent.

The workers in the maintenance departments and those directly related to the production departments are entitled to the full production bonus as per norms. Employees of semi-production and service departments receive 25 per cent of plant average bonus. However, all employees of VISL are covered by the production bonus scheme including those in the general administration and township. The vertical coverage extends up to the head of the department. There are certain ceilings on the total quantum of bonus payable to the officers.

In addition to the above two schemes, there prevails a third scheme of incentive bonus. It was introduced in 1963 on the basis of manpower studies to provide an incentive for improving manpower performance of the departments. It involves payment of bonus in terms of the improvement in the performance index which forms a ratio between the standard and hours and the actual man hours.

Apart from the above three schemes, there is also a provision for attendance bonus paid at the rate of Rs.1.60 per day and Rs.2 per night. This scheme was introduced in 1S52 for specified categories of employees. Now withstanding this scheme, it may be noted that there is a 30 to 40 per cent rate of absenteeism in VISL as compared to the Karnataka State's average annual rate of absenteeism of 16.6 per cent. The reason is that nearly 50 per cent of the employees own agricultural lands in nearby places, while a considerable percentage of them have some kind of business in the town of Bhadravathi. It is interesting to note that eve a movie-hall owner is working in the time office of the enterprise.

15.11 THE VIEWPOINTS OF WAGE BOARDS AND NCL:

The first wage Board for the cotton textile industry observed that both the employers and the employees disliked any system of progressive rates of incentives. They were satisfied with the prevailing system of piece-rates which embraced 50 per cent of the workers. The wage boards for sugar and cement industries found little scope for incentive wage system. While the coal wage board did not recommend the extension of the piece-rate system because of "certain inhabitation factors in the very nature of production in the industry", extension of the piece-rate system was recommended by the wage boards for jute, rubber, coffee and tea.

The National Commission on Labour makes the following recommendations with respect to incentives : (1) the application of incentive schemes has usually to be selective and restricted to industries and occupations where it is possible to measure in an agreed basis, the output of workers or a group of concerned workers and maintain a substantial amount of control over its quality, (2) incentive schemes have to embrace as many employees of an enterprise as possible and need not be limited only to operatives or direct workers - the extension of incentive schemes to the supervisory personnel can exert a marked impact on improvement of efficiency, (3) a careful selection of occupations should be made for launching incentive schemes with the help of work study teams commanding the confidence of both the employer and employees, (4) the incentive scheme is required to be simple so that workers are able to understand its full implications, (5) the employers need to ensure that external factors such as non-availability of raw material and components, transport difficulties and accumulation of stocks do not exert an unfavorable impact on incentive schemes, and (6) production has to be organized in a way which does not provide incentive wage on one day and unemployment on the other day - there should be a provision of a fall-back wage as safeguard against it.

15.12 THE VIEW POINT OF SUBRAMANIAM:

Subramanian provides a summary of the major conclusions and observations on incentive systems in India. As he observes, incentive systems, in properly designed, can improve productivity, enhance workers' earnings and minimize production cost. Introduction of incentive schemes can bring about effective utilization of human resources. However, these schemes should not introduce in haste. There are several prerequisites to the effective installation and operation of payment system by results.

1. It should be developed and introduced with the involvement of the workers concerned in harmonious climate of industrial relations.

2. Work study should precede the installation of incentive programme.

3. The wage structure should be rationalized on the basis of job evaluation before devising an incentive plan.

4. The objectives to be accomplished through incentives should be defined and accordingly, an attempt should be made to select a scheme which is most suitable to accomplish them.

Frequently, "system with workers' earnings varying proportionally less than output" appear suitable under present conditions. Incentive bonus should be paid if production increases as a result of extra human efforts rather than in a view of technological improvement. The piece-work plan, the standard hour plan, the Halsey plan and the Rowan plan are largely most suitable under various conditions. Study of effectiveness of prevailing system is hampered in view of inadequate information about them. Most of the employers have not yet realized the significance of seeking worker cooperation in formulating incentive systems. There is substantial scope for the extension of incentive systems to several other categories of workers not yet covered as well as for making the present schemes more effective.

In several industries, there are loose standard and excessive incentive payments because they are not based on work study. Frequently, incentive payments are based upon the total output of the plant. In public sector enterprises, application of incentives is varied ranging from rank-and-file daily wage employees to top management. This indicates a need for uniformity in such schemes. Further, in public sector organizations, attempts should be made to identify smaller groups, the performance of which can be assessed to provide a basis for payment of incentives. Effort should be made by state agencies to collect data about the working of the present schemes to develop typical plans for the major industries. The factors responsible for low cooperation between labour and management should be analyzed and communicated for improvement purposes. The labour cooperation can be accomplished by organizing an appreciation course for union members. Before the installation of incentive schemes, an attempt should be made to raise productivity by using ad hoc financial inducements. In view of high inflation, substantial amounts of incentive are required to stimulate the efforts of human resources. However, incentives should not be paid at the cost of the consumer and tax payer. Effective measures should be taken to use appropriate types of incentive to accomplish desired results and redress workers' grievances stemming from the working of these systems.

15.13 SUMMARY:

Employees are paid incentives in addition to wages and salaries. Incentives are linked to performance. This leads to better motivation among employees. Reduced cost, reduced supervision, reduced scrap and the like are the other benefits of incentives. There are problems, nevertheless. Quality of the products is likely to decline. Introduction of an incentive scheme is difficult, too. Jeaslousies creep in among workers. Problems associated with incentive schemes may be overcome and the plans may be made to serve their purpose, provided several safeguards are taken. Consultation and co-operation of workers are only examples of such pre-requisites.

ILO classifies incentive schemes into four categories : (i) schemes in which earnings vary in proportion to output, (ii) schemes where earnings vary proportionately less than output, (iii) schemes where earnings vary proportionately more than output, and iv) schemes where earnings differ at different levels of output.

There are incentive schemes for direct workers who work in batches, as well as for indirect workers. Incentive schemes are highly popular in Indian industries. Schemes that are in operation fall into the classification made by the ILO, but the schemes are fine-tuned to meet individual organizational requirements; installation of incentive schemes involves 12 steps. The schemes need to be reviewed every 10 years.

15.14 KEY WORDS:

Accelerated Premium systems	Barth Variable Sharing Plan
Bedaux scheme	Emerson's Plan
Gantt Task system	Halsey plan
Incentive systems	Merrik Differential plan
Payment by Results	Piece-rate
Piece work	Rowan plan
Standard Hour	

15.15. SELF ASSESSMENT QUESTIONS:

1. Explain the different types of incentive systems.
2. Bring out the steps in the introduction of incentive payments.
3. Bring out the salient features of the incentive schemes followed in Indian industries.
4. Debate on the assertion "If selection and placement decisions are done effectively, individual performance should not vary a great deal, therefore, an incentive system is not necessary".

5. Do you believe that an employee's behaviour is always influenced by the rewards expected? Discuss.

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LESSON- 16

LINKING WAGES WITH PRODUCTIVITY

16.0 OBJECTIVE:

After reading this lesson, you should be able to:

Study the significance of Linking Wages with Productivity.

Know the Important ways for Linking Wages with Productivity.

Visualize the Linking Wages with Productivity in Indian Experience.

STRUCTURE:

16.1 Introduction

16.2. Recent Issue of Linking Wages with Productivity

16.3. Significance of Linking Wages with Productivity

16.4. The Important Ways for Linking Wages with Productivity

16.4.1. Controlling performance for the wages paid

16.4.2. Linking Statutory Bonus with Productivity / Profits

16.4.3. Incentive Bonus

16.4.4. Productivity Bargaining

16.5 Recent Trends and Developments

16.6 Linking Wages with Productivity - Indian Experiences

16.7. Improving Productivity

15.8 Report of the Study Group for Productivity

16.8.1 Task Charges

16.8.2 Task Redesign

16.8.3 Work Flow

16.8.4 Automation

16.8.5 Office Design

16.9 Summary

16.10 Keywords

16.11 Self Assessment Questions

16.12 Further Readings

16.1 INTRODUCTION:

Once of the most effective ways of enhancing organisational performance is to link wages with productivity. **The** I.L.O. defines productivity as the ratio of the output of wealth produced and the input of resources used up in the process of production. Thus productivity can be increased by conserving and optimizing the use of all inputs, be they labour, capital, raw material or energy. Productivity is the net result of combination of all these inputs in the best possible way.

16.2 RECENT ISSUES OF LIKING WAGES WITH PRODUCTIVITY:

Annual wage increments should be restricted to increase in value added productivity. This is the crux of company's ability to pay. It is used extensively by Japanese industry as a corporate tool to evaluate the ability to pay and in wage determination. Wage hikes not linked to productivity trigger inflation; this in turn results in a deteriorating standard of living. In South Korea, economic growths lackened because wage increases were higher than increases in productivity. In order to stabilize the cost of living and maintain high growth, a wage price spiral must be avoided.

An enterprise creates wealth by adding value. It uses raw materials, capital and labour only as inputs to create a product with additional value. Therefore, the primary objective of any company is to add value, to continue to do so and to constantly increase the value it adds. This value added will then be distributed among the various contributors to the productive activities which went into its creation. Various costs are incurred when a company adds value in its operations. Some of these are direct operating costs - the cost of labour, capital, raw materials, and so on. And then there are other costs, not directly connected to the enterprises' operations like excise and other government imports.

Some misconceptions about productivity are to be cleared:

1. Productivity does not signify more production;

2. It does not mean making the manual worker work harder;

3. It does not result in working longer hours or more number of days;
4. It does not mean regimentation, austerity and less variety to the customer;
5. It is not confined to factories and manufacturing organizations alone;
6. It is not merely for the shop floor or the office desk;
7. It is not somebody else's job; and
8. It does not normally lead to retrenchment or redundancy.

16.3 SIGNIFICANCE OF LIKING WAGES WITH PRODUCTIVITY:

Linking wages, at least a significant part of it, to the changes in productivity is of vital concern to managements. Wage increases unrelated to improvements in productivity or efficiency would only add to costs which may be reflected in the prices of products. From the point of view of employees, an indiscriminate upward movement of wages (or payment of monetary wage- supplements) may prove less beneficial. Inflationary pressures following such increases would almost certainly neutralize the initial gains. Where increase in productivity out-strips increase in wages or compensation, all the benefits of higher productivity obviously go to the employer. But where wages do not grow in correspondence with productivity but overtake increases in productivity, there is every possibility of a wage-push inflation being triggered off. Basically, there is a link between the standard of living and productivity - higher the productivity, higher the standard of living.

The basic difficulty in productivity relates to measurement of the contribution of each factor or production. When the question of sharing productivity is discussed, the two main stumbling blocks are, first the formulation of an acceptable means of measuring increases in productivity in general and labour productivity in particular, and second, devising a fully acceptable formula for fixing the share of labour and capital in the increased productivity. With the increase in production due to capital intensity and technological sophistication, the problem of measuring the contribution of each factor assumes larger dimensions. The numerous complications in measuring productivity and sharing the gains there from have to be sorted out.

It is now generally accepted, in theory, at any rate, that the fruits of new technology should be shared between the various elements involved in the production process, so that on the one hand, the workers are not to be denied a share, while on the other, they are not entitled to claim the Whole of the credit for an increase in output that depends in large measure on the inventiveness of others, on managerial skill, and on the investment of capital in new technology.

16.4 THE IMPORTANT WAYS FOR LINKING WAGES WITH PRODUCTIVITY:

The elements of pay packet which are amenable to linkage with productivity and performance are: (a) profit bonus; (b) basic wage; (c) incentive wage; and (d) overtime wage. The numerous ways of linking wages with productivity are discussed below.

16.4.1 CONTROLLING PERFORMANCE FOR THE WAGES PAID:

It implies the determination of normal output or performance and the development of a procedure for measuring performance. Performance standards may be laid down for an individual worker or a group. These standards may or may not be announced. They provide a kind of internal management control system. Consequently, line and staff officials must assume direct responsibility for administering performance standard. Discipline for inadequate performance will be an essential ingredient of this responsibility. This means that the cause for poor performance must be identified and discipline should be based on this cause. Nevertheless, performance standards must not be viewed in a static sense. Search for improved work methods, layout and flow of work must continue. The quality of supervision and staff management should be improved. Such measures will make possible an upward revision of performance standard and wages.

16.4.2 LINKING STATUTORY BONUS WITH PRODUCTIVITY / PROFITS:

Bonus as an element in the pay packet is intended to represent simultaneously: (a) a deferred wage; and (b) a profit-sharing element. It is regarded as a deferred wage, because irrespective of profit or loss, a unit falling within the purview of the payment of Bonus Act, 1965, has to pay the minimum bonus. It has also a profit-sharing element, because the percentage of bonus is supposed to be determined by the profit-sharing formula embodied in the Act. The productivity-linked bonus plan in an industrial organization will call for.

(a) Developing a procedure for measuring productivity;

(b) Determining the level of productivity beyond which the bonus is to be paid; and

(c) Determining is scale of reward which will appropriately index productivity with bonus.

Some organizations have introduced such bonus schemes in lieu of statutory profit bonus. Any such scheme has to be tailor-made to the needs and objectives of the organization concerned.

The productivity-linked bonus, though theoretically sound, may also create problems. No doubt, under this arrangement, the employers, employees and the entire economy are going to gain in case there is an upward trend in productivity. But, the point is, workers alone are not responsible for fluctuations in productivity trends. This apart, in case of low productivity, the workers may not be prepared to accept a lower bonus. Moreover, it may be easy to measure production but difficult to measure productivity and even more difficult to apportion the contribution of labour to productivity and even more difficult to apportion the contribution of labour to productivity. Further, increased production and productivity would not mean more profits as the latter is determined by market conditions which are external to the unit of production. Productivity may increase but profits' may fall if the firm is facing adverse market conditions.

16.4.3 INCENTIVE BONUS:

'While productivity - linked or statutory bonus yields an average increase in wages for the covered employees as a whole, an incentive bonus scheme is usually designed to recognize differences in performance of individuals or small groups. The scheme provides for monetary payment and rewards for differential performance. The basis for sharing gains is determined by agreement with the unions. The extra payment is made out of savings in costs, which are made possible by performance above the existing level.

16.4.4 PRODUCTIVITY BARGAINING:

Productivity bargaining is a negotiation undertaken by employers' associations and unions into which a specific productivity element is injected. It indicates the process of striking a deal between the two bargaining parties with the object of improving productive efficiency and reward for work. It is an agreement in which advantages of one kind or another such as higher wages, increased leisure, are given to workers in return for" their agreement to accept changes in work practices, and methods of work. Productivity bargaining, however, does not mean an incentive scheme or wage increase in return for promises from union for achieving production targets. This method implies:

(a) A detailed analysis of firm's operation;

(b) The identification of Action possibilities; and

(c) Estimation of savings in costs.

The starting point for any realistic productivity agreement is an examination of the total work situation, and a comprehensive analysis of the problems therein. A detailed feasibility study needs to be carried out when a comprehensive productivity agreement is contemplated. The main elements in such a study are production analysis, sociological analysis, economic analysis, and wage analysis.

16.5 RECENT TRENDS AND DEVELOPMENTS:

Appreciable progress has been registered in productivity bargaining in countries such as the USA, Germany, Britain and France. An important and well-known productivity agreement, which has served as a model for others is the Fawley Productivity Agreement. It was concluded in July 1960 between the management of the ESSO refinery at Fawley, near Southampton, in the UK and the local representatives of the trade unions of the workers for the purpose of augmenting productivity and introducing work incentives. In essence, these agreements might be called a "productivity package deal" which embodied the company's elaborate measures of work' incentives and innovations, such as 40 percent increase in wage rate of all categories of employees in return for the acceptance of some well-defined working practices introduced by the management for improving labour productivity.

Like other usual collective agreements, the Fawley agreements were concluded for a period of two years and the agreements were, signed after five months of protracted negotiations. Prior to the negotiation, the 'Blue Book' containing the proposals of changes were referred to the union by the management.

An outstanding feature of the Fawley agreement was that it offered a 40-hour week and upto 45 per cent increase in wages, if certain conditions relating to productivity were satisfied. These conditions were reduction in overtime, elimination of craft demarcation, doing away with rest-pauses in work such as tea break, walking time and washing time. The agreement also provided for abolishing special payments like heat money, dirt money, and so forth. The direct outcome of this agreement was that within a period of two years, productivity registered a 50 per cent increase, apart from a reduction in overtime from 18 per cent to 8 per cent. The publicity given to productivity bargaining since the announcement of the ESSO agreement at the Fawley refinery, and the subsequent attention it has received, have had a number of effects, perhaps the most important is the change in attitude to industrial relations.

The Fawley was followed by many other similar agreements at ESSO Mill for haven Refinery. Imperial Chemical Industries Ltd., British Oxygen Company and Alcan Industries Ltd., among others. The growth of productivity agreements in America was a close parallel to British experience. It is only recently that productivity bargaining has gained recognition and usage in India. In several agreements, references have been made to productivity. The usual criticism that productivity cannot be measured, however, has not prevented many organizations to go ahead in this direction.

An extract from the Memorandum of Agreement, National joint Committee for the Steel Industry, regarding productivity is reproduced below:

Both the parties recognize that steel industry should grow at a faster rate in order to meet the nation's economic needs. This would necessitate further intensification of efforts by both the parties to achieve financial viability of the industry and also to generate the required resources to meet the urgent needs to modernize the steel plants. To this end, the parties commit themselves to work together to attain higher levels of production, productivity and profitability. Joint efforts would be made continuously in the following areas:

(a) Efficient handling of raw materials and reducing wastes.

(b) Improvement in yields and reducing operating costs.

(c) Procurement of materials at economic prices.

(d) Reducing energy consumption

(e) Improving quality in all operations.

(f) Improvement in housekeeping.

(g) Necessary improvement in working conditions, health and safety of workers.

(h) Continuously adopt better working practices.

(i) Reducing unauthorized absenteeism.

(j) Improving customers' service and delivery.

(k) Improve effective utilization of all resources including human resources.

(I) Attain 95-100 per cent capacity utilization in each steel plant.

Redeployment, retraining consistent with skill, dignity and earnings of employees, would be necessary in the context of modernization and changing requirements of the industry.

It is recognized by both the parties that discipline at all levels is essential for the smooth functioning of the steel plants. They, therefore, assure full cooperation for maintaining discipline and optimizing production and productivity.

Based on the above parameters, each plant will mutually identify areas of wasteful practices and expenditure with a view to devising specific measures for increasing operational efficiency and reducing costs.

Another extract from the Memorandum of Settlement", of Tata Engineering and Locomotive Co. ltd. (TELCO), Jamshedpur, regarding productivity is given below:

The union and the management agree that TELCO can remain vial only through improved standards of productivity throughout the Jamshedpur works and by optimizing utilization of plant, equipment and human resources. Both parties recognize that is will be essential to utilize "State of the Art" of the latest technology available in manufacturing methods in order to remain competitive, and both will work jointly to ensure that the company remains modern, current and maintains the highest standards of productivity.

The union recognizes that adherence to production quotas or any restrictive practice which inhibits production and productivity should be removed in the interest of the company and its employees.

The union recognizes that the productivity principle is based on the concept of return ability with respect to input and agrees to work jointly with the management to ensure that *an* improvement in productivity at the rate of 10 per cent in terms of output per man per year is achieved. In order to achieve this productivity level, the union will work with the management to remove all restrictive practices which come in the way of increasing productivity of plant and equipment.

All technical, clerical and other indirect employees working in areas like maintenance, inspection, shop cleaning, sanitation and hospitals, will also achieve the targeted levels of productivity in their respective areas. They will also make commensurate efforts to help enhance productivity.

The union accepts that an individual's unwillingness or inability to attain targeted performance levels retards the improvement in overall performance. The union, therefore, agrees to cooperate with the management in counseling and training such individuals whereby they can achieve targeted performance Levels.

The union also agrees to support the management in its efforts to identify and eliminate wasteful practices and to improve quality through replacement of out-dated methods, equipment tooling and systems with more effective and efficient alternatives.

The union and the management recognize that participation of employees in "small group activity" will go a long way in promoting goals of productivity, quality of product, and quality of work life. The parties, therefore, agree to encourage employees in their role for achieving their goals through participation in small group activities.

The management and the union believe that quality is produced and not inspected. Hence, joint efforts will be made for self-certification of products by concerned employees backed by an effective feedback system so as to ensure products and services of the highest quality.

The union and the management agree that special attention needs to be paid and results achieved in the following areas through joint efforts of both parties: (i) Full capacity utilization of each plant I equipment I facility, (ii) Improved / effective utilization of resources, including human resources, (iii) Optimizing energy consumption, (iv) Improving quality in all operations and of products, (v) Efficient handling of raw materials and reduction of wastages, (vi) Improvement in yields and reduction of operating costs, (vii) Improvement in housekeeping (viii) Improvement in environment, (ix) Continuous adaptation of better working practices, (x) Reducing unauthorized absenteeism, (xi) Improving customers' services and delivery.

The union and the management agree to discuss each of these issues in detail department- wise / division-wise and arrive at specific targets and to jointly implement plans to achieve the same.

For attaining productivity targets as indicated above, the management will identify non-performing workmen and will mutually negotiate with the union to plan corrective actions.

16.5 LINKING WAGES WITH PRODUCTIVITY – INDIAN EXPERIENCE :

In most developing countries including India, the productivity is not rising as rapidly as it should due to various reasons. The crux of the problem is that productivity must grow faster than prices as well as wages in order to bring about a more rapid expansion of investment, output and employment.

Our five year plans, recommended the introduction of incentives to promote labour productivity, reduce unit cost of production and ensure minimum wages. However, we do not find any accepted uniform approach to productivity-wage relationship in India. The employers' and workers' organizations did not follow any consistent approach to productivity criterion. The wage fixing authorities also do not appear to have given importance to productivity factor. Wages are increasing, while in many vital sectors of the economy, productivity is either falling or remaining constant. Based on purchasing power parity, the labour productivity in India compares unfavorably even with the neighboring Asian countries. However, Indian workers productivity has been gradually increasing since 1950 in almost all sectors.

Dr. S.C. Srivastava studied the relationship between wages, profits and productivity in selected industries in India during 1950-64. His study revealed that in the cement and cotton textile industry, there was a strong correlation between total value added and wages paid to the workers. Total wage bills in these industries bore a linear relationship with value added. Its trend value was positive. The study also revealed that in the case of cement industry there had been a six-fold increase in the average money value of the benefits and privileges from 1950 to 1964. The corresponding value for the match industry was 1.25, 4 for paper and paper boards, 5 for sugar, 24.5 for cotton, 8 for woolen, 6.5 for jute and 5 for iron and steel industry.

16.6 IMPROVING PRODUCTIVITY :

Productivity is a measure of efficiency with which resources both human as well as material are converted into goods and service. Faster rate of economic growth can be ensured through excellent production and higher productivity in all branches of economic activity. Human resource being an important input, their productivity plays a significant role in determining the overall economic growth of a nation. Apart from the level of human skills, the quality of raw materials and the technology employed are also responsible for productive human resources.

One of the most effective ways of enhancing organisational performance is by increasing productivity. The international Labour Organization defined productivity as the "ratio of the output of wealth produced and the input of resources used up in the process of production". The American Productivity Centre defines productivity as the efficiency with which an organization uses its labour, capital, material, and energy resources to produce its output.

16.8 REPORT OF THE STUDY GROUP FOR PRODUCTIVITY:

The Report of the Study Group for Productivity and Incentives, constituted by NCL, defines it as the process of optimizing / maximizing the economic utilization of ail available resources and investigating and utilizing the best known resources, as also creating new resources for different activities, be they industrial, commercial, agricultural services or any economic activity. Thus, productivity is the net result of a combination of inputs-men, machines, and capital - in the best possible way. Productivity which relates to men or labour is called labour productivity and is usually measured as the ratio of output to labour inputs. It is the output per unit of labour employed, reckoned in terms of man-hours or man-days.

There are some common misunderstandings about productivity. Quite frequently, productivity and production are treated as one and the same. Productivity is not production; it is a ratio between output and input. The two vital aspects of productivity are efficiency and effectiveness. Productivity is the key to profitability and a way of doing things better and working smarter, not just harder. There are many ways to improve productivity.

16.8.1 TASK CHARGES:

What people do at work has two significant effects on productivity. One impact is a result of how the worker reacts to the job or tasks itself and the other impact is the arrangement of the separate tasks distributed among the other impact is the arrangement of the separate tasks distributed among the employees and departments in the organization in order to produce the final product. Whereas the first effect is through task design, the second is through the work flow.

16.8.2 TASK REDESIGN:

The first job redesign approach that can be used to improve productivity is called job enrichment. However, job enrichment is limited in its impact on employees because it can only serve design overcomes some of these limitations. The socio-technical approach rests on the notions that jobs are manmade inventions designed to suit a number of technical and social systems needs and are constantly changing. The objective of the socio-technical design such as the famous one at Volvo is to bridge the two aspects (technical and social) so that the resources of the two are optimally used to co product an outcome that is desired by the employees of the organization.

16.8.3 WORK FLOW:

Work flow changes result in improved productivity based largely on' the principles of industrial engineering and organization design. This can be applied in the office, factory, and also to white collar service work as well as blue-collar manufacturing work.

16.8.4 AUTOMATION:

Automation is so significant that is likely to be a major contributor to improving productivity. Automation is especially critical since it has the potential of changing the nature of so many jobs and in creating many new jobs. Automation will soon change the face of factories and offices. Computer-controlled systems are being introduced that are likely to replace human beings on plant floors and improve productivity and profitability. Automated equipments are also moving into offices. As such factories and offices will never be the same.

16.8.5 OFFICE DESIGN:

The physical environment influences employee performance and quality of working life. Office design shall allow employees to have some privacy, and some time to work uninterrupted. An entire office department, division or company can help make ail employees successful when they observe quiet time as a unit. Everyone should be included in the process of office design. When all employees in the office are making a special effort to do their work quietly and not bother their co-workers, the level of internal office interruptions is greatly reduced. External interruptions are to be minimized wherever possible. The greater the number of interruptions that are eliminated during the quiet period, the more work will be successfully accomplished.

While it is important to be acquainted with the individual techniques or programmes to improve productivity, it is necessary to realize that programmes for productivity improvement rarely work well in isolation. They work best under conditions where:

(a) Top management visibly supports the programmes;

(b) There is a philosophy of productivity improvement;

(c) Employees are adequately trained;

(d) Employees are fairly rewarded;

(e) Employees are involved and receive feedback; and

(f) Appraisal systems are seen as fair and used in compensation decisions.

In other words, productivity programmes work best only when they are part of a total management approach to productivity. These activities are:

(a) Management by teamwork and consensus;

(b) Recognition and praise by management for good work done;

(c) A willingness on the part of supervisors to listen to employees and make suggested changes if appropriate;

(d) An open-door, open-communications policy that is practiced; and

(e) A consistent application of fair and human resource-oriented personnel policies.

The benefits of a well-planned, successful productivity improvement programmes are manifold and significant. Productivity programmes benefit employers in terms of profitability and viability. A higher productivity benefits employee too as it enables them to earn more and gives them job security. In addition, consumers get a better value for their money. Productivity growth means increased profits for the organization which may be. Needed for its survival, expansion, diversification and growth.

Productivity improvement does not just happen as a miracle. It has to be planned. Technology alone will not guarantee productivity increase. It must be combined with the dynamic interaction of human skills., physical assets, and organizational and institutional settings. Productivity improvement programmes are associated with process innovation and product innovation. In addition, all employees must be given the opportunity to be involved in the productivity improvement schemes initiated by employers. Moreover, the success of any productivity improvement programme depends on a rational approach to productivity measurement. The type of measurement used varies from organization to organization and from industry to industry, although some norms are available for certain types of manufacturing and service industries.

Some may look at productivity in terms of the value-added concept. Thus, productivity is the ratio between the resources put into a process and the value of goods that come out of that process. If we can increase the value being added to some methods, then productivity improves. These methods can be reducing costs, increasing or improving effort and skill and so on. When the value added per worker is higher in an organization, it has the ability to pay higher wages. The organization must make an effort to check the value being added to the goods and services produced and explore ways to improve the value in order to be productive.

Faster rate of economic growth can be ensured through accelerated production and higher productivity in all branches of economic activity. Human resources being an important input, their productivity plays a significant role in determining the overall economic growth of a nation. Apart from the level of human skills, the quality of raw materials and the technology employed are also crucially connected with the productivity of human resource. In fact, the modern concept is that of Total Factor Productivity (TFP) in which the productivity of all factors of production is reflected - land, labour, capital and entrepreneurship. Although Indian productivity has kept up a rising trend, it has not been sufficiently high to make Indian products compete successfully in the international market. This is a cause of concern in view of the globalization of the Indian economy. There is a need both for modernizing technology so that the worker is enabled to give better productivity per unit of labour and for establishment of wage policies which are linked to productivity.

16.9 SUMMARY:

There is a strong case for a wage-productivity linkage. Necessary efforts are to be made not towards raising money wages but towards raising productivity in order to ensure steady increase in the real income of labourers. Incentive wage system plays an important part in improving productivity. Hence, productivity linked incentive schemes are to be introduced in the interest of the workers, employers and the society. However, any incentive scheme has to be adapted to the conditions of each industry and even within similar industry roam plant to plant. In the interest of higher productivity and faster economic development, a positive, dynamic, and novel approach to productivity bargaining should be adopted on a much wider scale.

16.10 KEYWORDS:

Labour

Productivity

Wage determination

Trends and Developments

Automation

Manufacturing

Total Factor Productivity

16.11 SELF ASSESSMENT QUESTIONS:

1. Explain the issues of linking wages with productivity.
2. Explain the possible ways to align the wages with productivity.
3. Write a note on recent trends in linking wages with productivity.
4. Explain preparation of report for productivity in brief.
5. Write a note on impact of wage on productivity.

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LESSON - 17

EXECUTIVE/MANAGERIAL COMPENSATION

17.0 OBJECTIVE :

After reading this lesson, you should be able to :

- Identify the Components of Executive/Managerial Compensation and describe them
- Point the unique features of Executive/Managerial Remuneration
- Argue for and against payment of higher Remuneration to Executives
- Answer effectively the issues raised in paying more to Managerial Personnel

STRUCTURE :

17.1 Introduction

17.2 Meaning and definitions of managerial/executive compensation

17.3 Executive incentives

17.4 Nature of work of executives

17.5 Executive compensation system and policy

17.6 Legal Environment of executive compensation in India

17.7 Elements of executive remuneration

17.8 Special features of executive remuneration

17.9 Methodologies-cum-strategies for managerial compensation

17.10 Relevant issues in executive remuneration

17.11 Remedies

17.12 Summary

17.13 Keywords

17.14 Self Assessment Questions

17.15 Further Readings

17.1 INTRODUCTION :

Executive/Managerial Compensation system is designed on the basis of certain factors after analyzing the job work and responsibilities. The compensation system was designed on the basis of job work and related proficiency of the employee. Managers are probably the most important group of employees in the organization. While they represent a small percentage of the workers, they represent a major portion of the cost of compensation. The managerial job is one of high stress, a great deal of variety, and the need to exercise considerable judgment. Managers are highly committed to the organization, have an action orientation, and a need to express their power motive.

Compensation programs for executive/managers are a combination of base pay and incentive pay. Managerial incentive programs are divided into short and long range. Short-range programs are typically rewards for performance in a particular year based on how well the manager did in achieving his or her goals but with a measure of overall organizational performance forming the base of the bonus pool from which these funds emanate. Long-term managerial incentives are intended to tie the executive into the organization, both so the executive will stay with the organization and continue to perform highly. Most of these plans are a variation of a stock option plan that grants stock or money, based on overall organizational worth, to the executive over a long time period. These plans are typically deferred income. Managers are also granted a variety of benefits and perquisites that are not available to other employee groups.

Managers' especially senior level managers have become very critical to organizational success. They are also in short supply, therefore, organisations are competing with each other to attract, retain and motivate leader managers for their strategic requirement. In India, too, the demands of such managers have increased manifold after the economy has been opened up.

Executive remuneration has assumed considerable importance in recent years. Salaries and perks paid to highest decision-makers in organisations are skyrocketing, and this sudden spurt in managerial remuneration is the result of economic deregulation and the consequent entry of MNCs into the country. This lesson is devoted to a detailed discussion of three aspects - (i) What and how much are the executives paid? (ii) Why are they paid hefty remuneration? (iii) What issues are involved in payment of higher remuneration?

17.2 MEANING OF MANAGERIAL/EXECUTIVE COMPENSATION

Executive Compensation means any reward given to top ranking executives such as Chairman, Vice Chairman, Executive Chairman, Managing Director, Joint Managing Director, Dy. Managing Director, Directors, Chief Technology Officer, Chief Financial Officer, Chief Operating Officer, and other upper-level managers for services and expertise rendered to an organization. It is usual the members of the "C-Suite." (A widely-used slang term used to collectively refer to a corporation's most important senior executives. C-Suite gets its name because top senior executives' titles tend to start with the letter C, for chief, as in chief executive officer, chief operating officer and chief information officer.)

Definitions of managerial compensation

- **Robert W. Kolb (2006),** "Executive Compensation refers to the total reward provided by the firms to the top level of executives in a corporation, such as the CEO, COO, CFO, and a handful of other executives who occupy the very highest level of management"

➢ **Tapomoy Deb (2009),** "Executive Compensation refers to short-term and long-term financial and non-financial rewards given to top ranking executives under a contractual, legal and contractual mandate."

Components of executive compensation

- Base salary
- Incentive pay, with a short-term focus, usually in the form of a bonus
- Incentive pay, with a long-term focus, usually in some combination of stock awards, option awards, non-equity incentive plan compensation
- Enhanced benefits package that usually includes a Supplemental Executive Retirement Plan (SERP)
- Extra benefits and perquisites, such as cars and club memberships
- Deferred compensation earnings

17.3 EXECUTIVE INCENTIVES

Organizations offer heavy incentives to executives to retain the talented workforce. The immense competition in the market has forced the organizations to officer lucrative compensation packages. Performance based incentives comes out to be the only solution for the demand-supply disparity. Incentives are more effective in the marketing segment as it results in more and more sales. The business development executives strive for more incentives and in the effort produce more business and receive heavy perks.

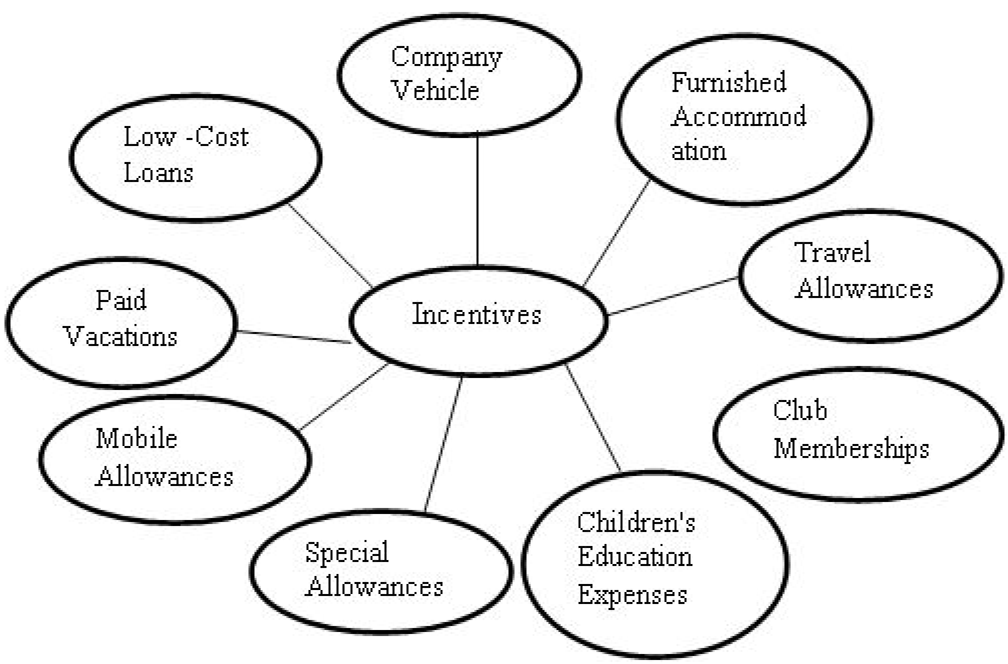

Figure 17.1 Executive Incentives

Objectives influence executive compensation

- ✓ Ensuring that the total compensation packages for executives are competitive with the compensation packages in other firms that might employ them, and

- ✓ Tying the overall performance of the organization over a period of time to the compensation that is paid to executives. It is the second objective that critics of executive compensation believe is not being met. In many organizations, it appears that the levels of executive compensation may be unreasonable and not linked closely to organizational performance.

17.4 NATURE OF WORK OF EXECUTIVES

The nature of the responsibilities of other high level executives depends on the size of the organization. In a small organization, such as independent retail stores or small manufactories, a partner, owner or general manager often is responsible for purchasing, hiring, training, quality control and day-to-day supervisory duties. In large organizations, the duties of executives are highly specialized. Some managers, for instance, are responsible for the overall working of the organization such as manufacturing, marketing, general operations, manager's plan, direct, or co-ordinate their operations of companies or public private sector organisations. Their duties include formulating policies, managing daily operations, planning the use of materials, human resources, but are to diverse and general in nature to be classified in any one area of management or administration, such as personnel, purchasing or administrative services.

17.5 EXECUTIVE COMPENSATION SYSTEM AND POLICY

Executive compensation system is very important, but the establishment of an efficient process, system and policy is challenging. Not only are the contribution and efforts of executives difficult to quantify, their decisions affecting the performance of the organization cannot always be accurately assessed. Thus, the executive compensation process, system and policy must rely upon proxies such as corporate profit or share price to assess the performance of executives. These proxies will be influenced by factors which are not under the control of executives.

The compensation system and policy in respect of executive compensation are as follows:

a) ***Legal compliance:*** Complying with relevant legislation like The Companies Act, 1964 guidelines on managerial remuneration.

b) ***Market position policy:*** Refers to where relative to compensation surveys, and organization wants to compensate its executives.

c) ***My compensation-my way:*** Refers to structuring the employment contract and conditions of employment in the most flexible way. The impact is greater than total package.

d) ***Rand hedging of compensation:*** Compensation practices designed to protect salary against a slide in currency.

e) ***Compensation committee:*** The appointed committee, usually comprising executive and non-executive directors, that decides on compensation policy and important compensation decisions such as the executive's compensation.

f) ***Compensation governance:*** The governance issues that apply to compensation including how decisions are taken and limits of authority.

g) ***Compensation mix:*** The mix or ratio between guaranteed compensation (e.g., short-term incentives, long-term incentives and share schemes).

h) ***Retention strategies:*** Strategies put in place to retain executives.

17.6 LEGAL ENVIRONMENT OF EXECUTIVE COMPENSATION IN INDIA

Given the nature of executive compensation, various committees have been set up by the government of India to suggest appropriate and effective measures for regulating executive compensation (or managerial remuneration, as mentioned in The Companies Act, 1965). The reports of Bhoothalingam Committee and Sachar Committee are noteworthy. The views of these two committees are divergent and a snapshot of their most relevant observations is given below:

❖ ***Boothalingam Committee:***

- Compensation differential between lowest and highest salary was in the range of 1:10.
- Suggested for setting up of National Pay Commission for fixing executive compensation.

❖ ***Sachar Committee:***

- Role of government in regulating executive compensation should be reduced.
- Universal norms to be prescribed for everyone to follow.
- Shareholders should be taking a decision on executive compensation.

The provisions of The Companies Act, 1956, govern executive/managerial compensation. Section 198 provides directions on executive/managerial remuneration as discussed below.

The total managerial remuneration, excluding any fees, payable by a public company or a private company which is a subsidiary of a public company, to its directors and its manager in respect of any financial year shall not exceed 11% of the net profits of that company for that financial year computed in the prescribed manner, except that the remuneration of the directors shall not be deducted from the gross profits. However, 11% ceiling is applicable for companies for one whole time director. If the number of whole time directors is more than one, then the ceiling is 5%.

Within the limits of the maximum remuneration, a company may pay a monthly remuneration to its managing or whole time director in the prescribed manner. However, if in any financial year, a company has no profits or its profits are inadequate, the company shall not pay to its directors, including any managing or whole time directors or manager, by way of remuneration any sum, exclusive of any fees payable to directors, except with the previous approval of the Central Government.

Managerial remuneration as referred to above means and includes:

- Any expenditure incurred by the company in providing any rent free accommodation, or any other benefit or amenity in respect of accommodation free of charge to directors and managers;
- Any expenditure incurred by the company in providing any other benefit or amenity free of charge or at a concessional rate to any of the directors and managers;
- Any expenditure incurred by the company in respect of any obligation or service, which, but for such expenditure by the company, would have been incurred by any of the directors and managers; and
- Any expenditure incurred by the company to affect any insurance on the life of or to provide any pension, annuity or gratuity for any of the directors and managers or his spouse or child.

A managerial person shall also be eligible to the following perquisites, which shall not be included in the computation of the ceiling on remuneration as under:

- Contribution to provident fund, superannuation fund or annuity fund to the extent these either singly or put together are not taxable under the Income Tax Act, 1961;
- Gratuity payable at a rate not exceeding half a month's salary for each completed year of service; and
- Encashment of leave at the end of the tenure.

In addition to the perquisites specified above, an expatriate managerial person (including a non-resident Indian) shall be eligible to the following perquisites, which shall not be included in the computation of the ceiling on remuneration:

- ***Children's education allowance:*** In case of children studying in or outside India, an allowance limited to a maximum of Rs. 5,000 per month per child or actual expenses incurred, whichever is less. Children allowance is admissible up to a maximum of two children;
- ***Holiday passage for children studying outside India/Family staying abroad:*** Return holiday passage once in a year by economy class or once in two years by first class to children and to the members of the family from the place of their study or stay to India if they are not residing in India with the managerial person;
- ***Leave travel concession:*** Return passage for self and family in accordance with the rules specified by the company where it is proposed that the leave be spent in home country instead of anywhere in India.

17.7 ELEMENTS OF EXECUTIVE COMPENSATION

For the purpose of remuneration, an executive is considered to be an individual who is in a management position at the highest levels. Specifically, this category includes Presidents, Vice-presidents, Managing Directors and General Managers. At the heart of most executive compensation plans is the idea that executives should be rewarded if the organization grows in profitability and value over a period of years. Because many executives are in high tax brackets, their compensation often is provided in ways that offer significant tax savings. Therefore, their total compensation packages are more significant than their base pay. Their remuneration generally comprises five elements. (See Fig 17.2) They are :

a) Executive Salary

b) Executive Bonus Plans

c) Performance incentives-long term vs. short term

d) Executive Benefits

e) Executive Perquisites

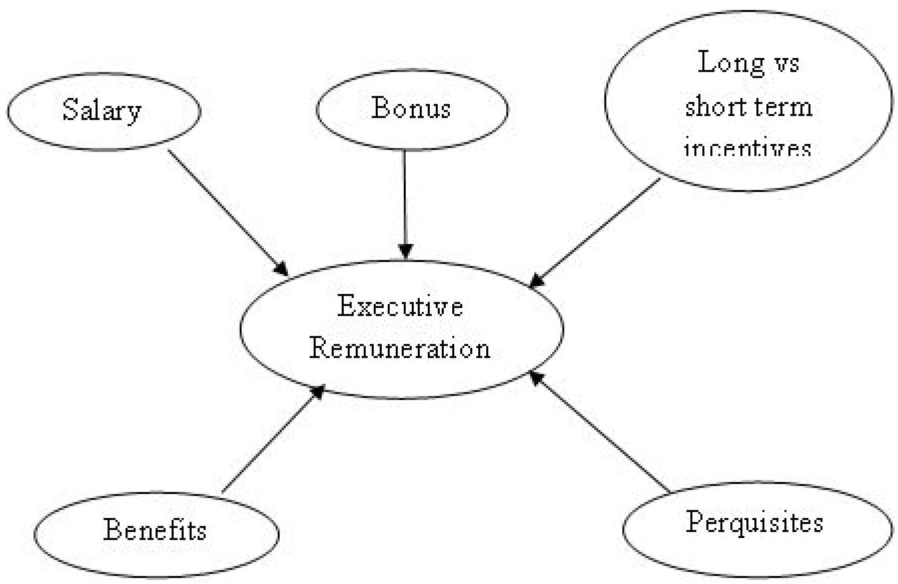

Figure 17.2 : Elements of Executive Remuneration

a) Executive salaries

Salary is the first component of executive remuneration. Salary is supposed to be determined through job evaluation and serves as the basis for other types of benefits. But job evaluation may be only a partial solution because executives must be paid for their capabilities - for what they can do - rather than for job demands. This is the reason why norms of wage and salary fixation are generally not observed while fixing salaries for executives. Salary as a component of total remuneration is not significant as it is subject to deductions at source and is also capped by government regulations. In order to make good the cuts and ceilings, executives are offered hefty incentives and attractive perks.

Salaries of executives vary by type of job, size of organization, region of the country, and industry. On average, salaries make up about 40-60% of the typical top executive's annual compensation total. A provision of a 1993 tax act prohibits a publicly traded company from deducting pay of more than $1 million for each of its top five officers unless that pay is based on performance criteria approved by outside directors and shareholders.

b) Executive bonus plans

Bonus plays an important role in today's competitive executive payment programmes. This type of incentive is usually short-term (annual) and is based on performance. There are almost as many bonus systems as there are companies using this form of executive remuneration. Because executive performance may be difficult to determine, bonus compensation must reflect some kind of performance measure if it is to be meaningful. As an example, a retail chain with over 250 stores ties annual bonuses for managers to store profitability. The bonuses have amounted to as much as 35% of a store manager's base salary.

Bonuses for executives can be determined in several ways. A discretionary system whereby bonuses are awarded based on the judgments of the chief executive officer and the board of directors is one way. However, the absence of formal, measurable targets is a major drawback of this approach. Also, as noted, bonuses can be tied to specific measures, such as return on investment, earnings per share, or net profits before taxes. More complex systems create bonus pools and thresholds above which bonuses are computed. Whatever method is used, it is important to describe it so that executives trying to earn bonuses understand the plan; otherwise, the incentive effect will be diminished.

c) Performance incentives-long term vs. short term

Performance-based incentives attempt to tie executive compensation to the long-term growth and success of the organization. However, whether the emphasis is really on the long term or merely represents a series of short-term rewards is controversial. Short-term rewards based on quarterly or annual performance may not result in the kind of long-run-oriented decisions necessary for the company to continue to do well.

A stock option gives an individual the right to buy stock in a company, usually at an advantageous price. Different types of stock options have been used depending on the tax laws in effect. Stock options have increased in use as a component of executive compensation during the past 10 years, and employers may use a variety of very specialized and technical approaches to them, which are beyond the scope of this discussion. However, the overall trend is toward using stock options as performance-based long-term incentives.

Where stock is closely held, firms may grant "stock equivalencies" in the form of phantom stock or share appreciation rights. These plans pay recipients the increased value of the stock in the future, determined by a base valuation made at the time the phantom stock or share appreciation rights are given. Depending on how these plans are established, the executives may be able to defer taxes or be taxed at lower capital-gains tax rates.

d) Benefits for executives

As with benefits for non-executive employees, executive benefits may take several forms, including traditional retirement, health insurance, vacations, and others. However, executive benefits may include some items that other employees do not receive. For example, executive health plans with no co-payments and with no limitations on deductibles or physician choice are popular among small and middle-sized businesses. Corporate-owned life insurance on the life of the executive is popular and pays both the executive's estate and the company in the event of death. Trusts of various kinds may be designed by the company to help the executive deal with estate issues. Deferred compensation is another possible means used to help executives with tax liabilities caused by incentive compensation plans.

e) Executive perquisites

In addition to the regular benefits received by all employees, executives often receive benefits called perquisites. Perquisites (perks) are special executive benefits—usually noncash items. Perks are useful in tying executives to organizations and in demonstrating their importance to the companies. It is the status enhancement value of perks that is important to many executives. Visible symbols of status allow executives to be seen as "very important people (VIPs)" both inside and outside their organizations. In addition, perks can offer substantial tax savings because many perks are not taxed as income.

Perks constitute a major source of income for executives. In addition to the normally allowed perks like provident fund, gratuity and the like, executives enjoy special parking, plush office, vacation travel, membership in clubs and well-furnished houses. Perks take care of all possible needs.. Their holidays, servants, telephone bills and even electricity and gas bills are taken care of by their companies.

17.8 SPECIAL FEATURES OF EXECUTIVE REMUNERATION :

Executive remuneration has certain unique features

First, remuneration cannot be compared to the wage and salary schemes meant for other employees in organisations. Factors and variables are more numerous in management jobs, and simple comparisons and ratings may not be possible.

Second, executives are denied the privilege of having unionised strength. They cannot demand for higher salaries and perks, hoist red flags on factory gates, shout slogans, pelt stones, and burn buses. It is the workers who resort to all these and if they succeed in their efforts, executives too benefit. Put in another way, executives often prompt workers to go on a strike.

Third, secrecy is maintained in respect of executive remuneration. What A receives is not made known to B and what B gets, C cannot know. Secrecy is maintained because no two executives in the private sector, in the same grade, receive the same pay. Remuneration depends upon such factors as competence, length of service and loyalty to the founders.

Fourth, executive pay is not supposed to be based on individual performance measure but rather on unit or organisational performance. This is because an executive's own performance is assumed to be rather directly reflected in measures of unit or corporate performance. However, in practice, an executive pay may not be linked to the organisation's performance.

Finally, executive remuneration, as was stated earlier, is subject to statutory ceilings. As per the latest guidelines, the monthly salary various from Rs.40,000 to 87,000 subject to an overall limit of Rs.10,50,000 per annum including perquisites.

Remuneration is restricted to five per cent of its net profit if the company has one executive, but the total remuneration is not to exceed 10 per cent of its net profit the number of managerial personnel is more than one.

These ceilings, however, do not apply to private limited companies.

Extent of pay :

Theoretically, remuneration of managerial personnel is supposed to be guided by job descriptions, job evaluations, salary grades with ranges of pay in each grade, and salary surveys. But in practice, the norms seem to have been thrown to winds and exorbitant amounts are paid to decision makers in organisations.

Average compensation for CEOs at some Indian firms

Company	Name	Remuneration Rs. in crore (March 2013)
Hindalco Inds	D. Bhattacharya-MD	Rs. 20.61 crore
L&T	**K. Venkataramanan**-MD & CEO	Rs. 14.28 crore
Welspun Corp	**Braja K Mishra**-MD	**Rs 13.72 crore**
Tata Motors	**Karl Slym**-MD	**Rs 10.97 crore**
Indian Hotels	**Raymond N Bickson**-MD	**Rs 10.33 crore**
Hind. Unilever	**Nitin Paranjpe**-MD & CEO	**Rs 10.12 crore**
Ranbaxy Labs	**Arun Sawhney**-MD & CEO	**Rs 9.72 crore** (Dec 2012)
Nestle Ind	**Antonio Helio Waszyk**-Chairman & MD	**Rs 9.47 crore**
Idea Cellular	**Himanshu Kapania**-MD	**Rs 8.75 crore**

Bosses take home up to 70% of pat (profit after tax)

CEO salaries have been a hot topic in the West, back home it has not caught the attention of shareholders for public limited companies. It's high time it did. The study finds out that there are a large number of corporate whose top executives draw remunerations that vary anywhere between 10% & 70% of the companies' reported Profit After Tax (PAT).

Take the case of optical storage media manufacturer Moser Baer. The promoter-cum-managing director, Deepak Puri, grossed an annual package of Rs. 2.08 crore which is 44% of the net profit of the company. Add the pay packet of executive director Ratul Puri Rs. 1.25 crore and the due took home an amount which was 71% of the net profit of their company last year.

Other individual examples where the executives' annual package is disproportionate to the net profit of their company include-iGate Global's CEO Phaneesh Nurthy, Ashok Chaturvedi of Flex Industries, Ashok Geol of Essel Oropack, S. Narayanan and H. Nandi of NRO-TEK, Kalyan Ganguly of United Breweries, Hemendra Kothari of DSP, Merril Lynch, Kalanithi Maran and Kavery Maran of Sun TV, and Prathap Reddy of Apollo Hospitals to name just a few.

The study looked at 400 corporate directors belonging to 245 companies who have a declared annual packages of Rs. 1 crore and above as per the annual reports, and calculated their compensation figures as a percentage of net profit.

Vivek Paul as Vice-Chairman of Wipro rakes in an annual salary of Rs. 4.5 crore a year. For the record, he is also the highest paid non-promoter executive in a listed Indian firm. In fact, Paul's boss Azim Premji, Chairman and Managing Director of Wipro, takes home two crore less.

The top Indian executive working for a listed MNC was M.S. Banga, Managing Director of Hindustan Lever. The company paid Banga Rs. 1.58 crore last fiscal. The top woman on the list of highest paid executives in India was Lalita D. Gupte, joint Managing Director, CICI, who took home Rs. 1.29 crore last year.

17.9 METHODOLOGIES-CUM-STRATEGIES FOR MANAGERIAL COMPENSATION

- Salary/Basic salary/Consolidated salary continues to remain a major component, though salary scales are often discarded these days or used only as guides. It is performance contribution that determines the pay and future revisions, which vary widely from individual manager to individual manager. Salary broad binding is also getting recognition and acceptance.

- Grade-wise flat allowance are being consolidated, except where tax exemption benefits are available. Allowances may be linked to the salary as a percentage or by slabs, but preference is for flat amounts, which do not increase automatically and increases at the discretion, and therefore, controllable.

- Reimbursement of expenses incurred on company's work has become limited, and in line to conform to the tax laws.

- Annual payments- Bonus or commission, and leave travel are common features. Some tax relief applies for the latter.

- Benefits generally comprises of unfurnished/furnished company owned or leased accommodation, use of company owned or leased vehicle, medical coverage, retiral benefit, covering provident fund, pension, or superannuation and gratuity, post retiral medical assistance, easy loan scheme at low or zero interest rates for house building, car or vehicle, furniture or utility items, etc., renting employee's owned housing, club entrance fee reimbursement, tec. Minor benefits could be provision of security, driver, gardening assistant, sale of products or assets at a concessional rate, the relocation and transfer expenses, including admission etc., fees for children, credit card fees, phones etc.

- Employees Stock Option Plans, which have been popular in IT industry is not extensively used yet, for not being tax advantageous to other industries, nor seen as being very attractive which lesser growth trends for their share values, especially in the well-established older companies.

- Most of the companies are moving away from traditional compensation packages (Basic, DA, HRA, etc.) to cost to the company basis. Companies are talking in terms of gross salary and asking managers to do their own tax planning.

- Companies, special the multinationals, are observing transparency in pay package keeping in view the total cost. It means giving managers the flexibility to choose lifestyle of their own living within the certain parameters. But such a cafeteria/menu/in-basket benefits are on the wane.

- Performance linked payments-bonus + generous increment + merit awards, are increasing. The trend is to move away from seniority and hierarchy system and attach value to performers. The concepts of star performers are giving ground.

- Lifestyle perks (good accommodation, club membership, liberal furnishing, holiday abroad with family, etc,) continues to be the practice even if these are taxed.

Ten highest paid CEOs of India

Company	**Name**	**Remuneration in $**
Jindal Steel and Power Limited	Naveen Jindal	$14.68 million
Sun Group	Kalanithi Maran-	$11.4 million
Aditya Birla Group	Kumar Mangalam Birla	$9.42 million
Hero MotoCorp Limited	PawanMunjal	$6.89 million
Hero Honda motors	BrijmohanLAllMunjal	$6.88 million
Madras Cement Ltd	P. R. Subrahmaneya Rajha	$5.86 million
BGR Energy	B G Raghupathy	$5.19 million
JSW Steel	Sajjan Jindal	$5.06 million
Divis Laboratories	Dr. Divi	$4.63 million
Bharti Airtel	Sunil Bharti Mittal	$4.25 million

Determining "reasonableness" of executive compensation

Measurement of executive compensation is often justified by comparison to compensation market surveys, but these surveys usually provide a range of compensation data that requires interpretation. Various aspects have been suggested for determining if executive pay is "reasonable" in a specific instance, including the following:

- Would another company hire this person as an executive?
- How does the executive's compensation compare with that of executives in similar companies in the industry?
- Is the executive's pay consistent with the pay of other employees in the company?
- What would an investor pay for the level of performance of the executive?

Undoubtedly, the criticism of executive compensation will continue as huge payouts occur, particularly if organizational performance has been weak. Hopefully, boards of directors of more corporations will address the need to better link organizational performance with variable pay rewards for executives and other employees.

17.10 RELEVANT ISSUES IN EXECUTIVE REMUNERATION :

Several issues crop up in the context of remuneration provided to the highest decision-makers in organisations. Surely, there are many number of employees in an organisation whose competency is no less significant but their remuneration is in no way near to that of a managing director or a general manager.

Assuming that an executive is worth that much, the success of an organisation does not depend only on one individual (thought failure douse). The healthy bottom line of an organisation is the result of combined efforts of technicians, scientists, financial wizards, marketing experts, HR specialists, canteen staff, sweepers, drivers and a host of others. If it were not so, TISCO should not have survived after the exits of Russi Mody, SAIL after V. Krishnamurthy and HLL after T. Thomas. Obviously, the CEOs alone should not be given all the credit for healthy bottom lines.

If there is one individual who really deserves applause and handsome rewards, it is the founder of the organisation. In the initial stages, this gentleman sheds his blood for the organisation. When banks refuse to sanction additional loans, he pledges family assets to raise money for buying raw materials and paying salaries to employees. He spends sleepless nights devising strategies to market his products, to tackle labour militancy and to satisfy government agencies. It is a struggle and a challenge all the way till the unit starts doing well. He then needs a deputy to assist in managing the business. The executive demands 100 times more than what the founder had been drawing all along. Such demands naturally defy logic.

Yet another issue relates to the gap between the pay drawn by an executive and the wages paid to a worker. Huge disparities in incomes are often dysfunctional. Disparities in pay increase the probability of top executives getting alienated from front-line employees. It creates a psychological distance and also a life-style disparity. That is why executives at various levels sometimes tend to feel out of touch and uncomfortable while dealing with front-line employees.

One of the popular arguments in favour of hefty pay scales to executives is their motivation. They should be paid more to put in better performance. Looking at the flip side, money ceases to be the motivator beyond a certain point. One must have a house, vehicle, bank deposits, insurance policies and good education for children. And money induces an individual to acquire and enjoy these. Beyond this, money becomes irrelevant and often makes people extravagant and wasteful. Children are the worst affected by this kind of affluence. Then there is the constant fear of raids by tax authorities. Surplus money therefore results in needless tension.

Assuming that money motivates, these high-flying executives hardly stick to one organisation. A few thousands more offered by a rival organisation will induce them to put in their papers. Majority of managerial personnel are known for organisational rootlessness; gratitude and loyalty are words of the past.

Finally, there is the question of equity. When hundreds of people are languishing in the unorganised sector, it may be unethical to pay huge salaries and perks to select elites in the society. The hapless employees work hard for eight to ten hours a day but get paid a paltry sum of Rs. 500 to Rs. 600 per month each. Added to this is the endless uncertainty of tenure. A lecturer with a doctoral degree slogs in a college for a mere Rs.1200 per month and stays eternally 'temporary' on his or her job. An MBA demands an entry level pay of Rs.60 lakh per annum whereas the professor who trains the MBAs takes 25 years of continuous service to earn a monthly salary of Rs.20,000.

Hike-Spike: Indian firms pay better than MNCs

The Indian firms are paying better than the much-coveted multinationals. As India takes on the world, there's an increased willingness to pay top rupee for the best talent. There is almost across the board acceptance of variable pay - salary being linked to meeting targets. But the ration of fixed to variable pay varies. For investment bankers, this pay is almost 33% of total package, whereas it is less than 10% in the case of pharma executives. A long-established trend is thus likely to be bucked with the IT sector, reigning champ for the last five years, relinquishing its title as the most generous when it comes to pay increases.

From 1991-92, when we entered the age of liberalilzed and globalized economy, the managerial compensation packages have zoomed. The reasons for this are the same as has been explained before i.e. the quest for attraction, retention and motivation of talented manager, such managers being in short supply, the competitors inside the country and throughout the globe are paying higher compensation packages.

MNCs are finding high caliber managers for their Indian as well as global organisations from India Itself. In fact, India is proving to be a global managerial pool. The pay packages of MNCs in India are comparable to their counterparts in the parent country and other locations across the globe. With this on sloughts from MNCs, the Indian family owned companies could not remain complacent. They are turning to professionals, even going to the campuses for talent hunting. The result is senior managers in family owned companies are getting higher pay than others. MNCs pay attractive remuneration to their executives, be they home-country or host-country nationals. The Indian chiefs of Pepsi and Coke, for example, are paid identical scales like their counterparts in the US or elsewhere. If executives of Pepsi and Coke in India get paid so well, why not their equivalents in Indian businesses? We talk of globalising trade, technology, and managerial practices, why not executive salaries ? Why not salaries of all employees?

17.11 REMEDIES :

Action on the following lines may partly answer the issue raised with regard to high managerial remuneration :

1. Income beyond a certain limit must be subject to higher taxation. Statutory guidelines governing executive remuneration are now liberal. Payment beyond specified limits needs the prior approval of the government. And the government does not generally deny approval.

2. Executive, on their own, must take up more and more socially responsive actions such as adopting and uplifting villages, sustaining ecology, caring for the hungry and the homeless, supporting a cause, sponsoring cultural programmes, contributing to education, and the like. Such actions will make the business and its executives more acceptable to the society.

3. Conscious efforts must be made to increase the supply of managers and technicians. There is, therefore, greater need for starting more colleges and institutes to train young MBAs, BEs and other technicians.

4. Participative management needs to be encouraged. Employees must be offered stock option schemes and be encouraged to become owners of the undertakings for which they serve as workers, clerks, and supervisors.

The concept of corporate governance is highly helpful in resolving the issues. The Kumaramangalam Birla Committee on Corporate Governance recommends the formation of a 'remuneration committee' which will determine, on behalf of shareholders, the remuneration to be provided to executives. With this, a sense of equity will prevail in executive remuneration.

Following the recommendation of the Kumaramangalam Birla Committee, only some companies have constituted remuneration committees. Such companies are Asian Paints, Lupin, Bajaj and Rico Auto. As pointed out by the N R Narayana Murthy panel on corporate governance, most companies had been tardy on the issue of setting up remuneration committees.

There are also other safeguards like the Board of Directors and AGMs which need to okay salary increase of chief executives.

17.12 SUMMARY :

Executive remuneration comprises salaries, bonus, commission stock option and perks. Perks generally outstrip other elements in the package of remuneration.

Executive remuneration differs from wages and salaries paid to other employees. A major chunk of the salaries of managerial personnel is take away by taxes. Executives are denied the privilege of enjoying unionised strength, though they stand to gain when workers go on strike and succeed. Secrecy is maintained in respect of salaries and perks to executive.

Certain generalisation can be made in respect of executive remuneration in our country. First, norms of wage and salary administration are observed only in part; salaries and perks are subject to annual reviews; 'composite' salaries are gaining acceptability; salaries are sought to be linked to performance; rat race exists among rival firms to attract talented individuals; and there is large-scale migration of senior managers from public sector units to those in the private sector.

There are several reason why executives are paid more. They are worth lakhs of rupees in terms of talent and brain power. They need to be attracted, retained and motivated, and their greed must be satisfied so that they can adopt honest business practices.

Certain social and ethical issues are relevant in this context. First, high remuneration seems to be merely a hype disregarding individual intrinsic worth. Second, executives alone are not responsible for an organisation's healthy bottom line. Third, there must be some parity between salaries of an executive and wages of a worker. Finally, higher salaries and perks do not guarantee motivation.

More and more socially responsive actions, stiffer income taxation, increasing supply of managers and technicians and encouraging employees to become owners of enterprises are the answers to the issues raised.

17.13 KEYWORDS :

Executive Remuneration

Perquisites

Performance incentives-long term vs. short term

Stock Option

17.14 SELF ASSESSMENT QUESTIONS :

1. Justify the high remuneration paid to executives.
2. Write about managerial/executive compensation.
3. Describe the elements of executive remuneration.
4. What are the characteristic features of executive compensation?
5. Discuss the present trend in the executive remuneration

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LESSON - 18

RECENT TRENDS IN MANAGERIAL COMPENSATION

18.0 OBJECTIVE :

After reading this lesson, you should be able to :

- Study the various guidelines issued by Government on Managerial Compensation.
- Understand the Managerial Compensation in Private Sector.
- Know the Managerial Compensation in Central Public Sector undertakings.
- Review the Recent Trends and Developments of Managerial Compensation.

STRUCTURE :

18.1 Introduction

18.2 Government Guidelines

18.3 Arguments in Support of Government Regulation of Managerial Compensation

18.4 Critical Comments

18.5 Managerial Compensation in Private Sector

18.6 Managerial Compensation in Public Sector Undertakings

18.7 Constitution of Justice Mohan Committee

18.8 Recommendations of the Committee

18.9 Financial Implications

1810 Issues considered but not Reckoned

18.11 Criticism.

18.12 Elements of Wage Revision in PSUs

18.13 Managerial Compensation in Private Sector Vs Public Sector

18.14 Summary

18.15 Keywords

18.16 Self Assessment Questions

18.17 Further Readings

18.1 INTRODUCTION :

Compensation refers to a salary component, various fringe benefits performances - linked bonuses stock options etc. The term compensation is used in the sense of total cost of employment. It includes all tangible items incurred by an organisation on the employees. In recent years India includes, has witnessed a major revamp - both qualitatively and qualitatively of compensation packages offered to professional managers and executives.

The executive group is the king pin in an organisation, making as it does the difference between success and failure. Their motivation and performance are, therefore of particular significance to an organisation. The executive compensation thus has become an integral part of management. Due to the growth of the service sector in India many companies have witnessed a significant upward revision of remuneration packages, making the traditional salary structure uncompetitive and antiquated.

For instance there is a great demand for competent professionals in the financial service sector. These financial instructions have to complete in the make to attract and retain capable employees. Therefore in addition to healthy emoluments, these companies have started giving incentives to their employees in terms of performance- linked benefits which include bonus, profit sharing and stock options. Companies have started looking at executive compensation more systematically and more proactively so that they can expect better performance from the executives.

With the technological developments taking place at a higher rate, the salary packages are too increasing at a much higher rate. Pay packages in India have witnessed an increase of more than 14% in 2006 over last year's salary packages. The compensation package comprises of monetary and non-monetary benefits that includes salary, special allowances, house rent allowance, travel allowance, mobile allowance, employee stock options, club memberships, accommodations, retirement benefits and other benefits. Globalization is being considered as the cause for such salary hikes. The establishment of multinational companies and privatization has led the Indian industry to witness higher salary package. With the immense competition of attracting and retaining talented human resource, compensation package is the only motivation factor available with the organizations be it Indian origin organizations or foreign-owned multinationals. With the high attrition rate organizations are increasing their salary packages to attract and retain talented human resource. In the race, India has begged first position followed by Lithuania and China.

Compensation Trends

Most executive managerial compensation comes from stock options, and defenders of this system argue that you should compare the executive pay system to the returns executives earn for their companies. The government set pay levels for executive compensation at companies that received federal assistance during the 2008 financial crisis. However, after paying off these obligations, most companies returned to a system that uses bonuses and stock options to compensate managers

The CEOs paid more in the world, often bringing in annual compensation packages worth millions of dollars. In the last three decades, CEO pay grew at a faster rate than any other top executive. In fact, CEOs were paid 273 times more than their average employee in 2012, according to a study by the

Economic Policy Institute. Oftentimes, these highly paid CEOs can count on their hefty paychecks whether their companies are doing well or poorly.

Interestingly, Yahoo's Marissa Mayer is the only woman who made it on our list, with $36.6 million in total compensation in 2012 - a figure that, while impressive, pales in comparison to Oracle CEO Larry Ellison's $96.2 million.

Compensation strategy for special groups

The major challenge in compensating supervisors centers on equity. Previously, the supervisor's compensation was just like that of lower level managers. Due to which they make less money and little incentive. A typical board of directors comprises 10 outside the company and 3 inside directors, each having a term average of three years. But modern boards have changed considerably, approximately two thirds and boards now include more outside directors than in side directors (e.g., CEO, corporate officers) and this move to more outside directors comes with a price-higher compensation. The companies are planning to increase board pay because of competition been found that total director's compensation ranges from $ 40,000 to the low $ 50,000. In addition to cash compensation, there is an increasing emphasis on directors rewards that attempt to link to corporate performance. Our survey sample of more than 75 proxies from fortune 500 companies gives us rich insight into the efforts boards are pursuing to secure and improve the appropriateness, fairness and effectiveness of compensation pay, for performance has been embraced by 100 percent of our sample group as the guiding philosophy for executive compensation.

Four to five years ago, the figure was roughly half and two years ago it was 30 per cent less. In contrast, multinational corporations (MNCs) s pay about 50-70 per cent less to their top CEOs in the same sector for a similar-sized company. The hefty packages, however, are available only to an elite club, offered by big Indian corporate groups with turnovers between $3 billion and $10 billion. And, they are concentrated in resources industries, including energy, petroleum and metals, to name a few. In sectors such as fast-moving consumer goods, telecom, information technology or consumer goods, CEOs do not command such large salaries.

Unique features of managerial remuneration

- Managerial remuneration cannot be compared to wage and salary schemes meant for non-managerial employees in organization. Factors and variables are more numerous in managerial jobs and simple comparisons and ratings are not possible.

- Managers are denied the privilege of having unions and collective bargaining. Their competence and contribution are their strength for determining their pay package.

- Secrecy is maintained in respect of managerial remuneration. This is done because no tow managers in the private sectors, in the same grade receive the same pay. Compensation and reward depends upon such factors as competence, length of service, contributions and loyalty to the company.

- Managerial pay is not supposed to be individual performance measure but rather on the unit or organisational performance. This is because a manager's own performance is assumed to be rather directly reflected in measure of unit or corporate performance.

- Manager's compensation is subject to statutory sealing. As per the latest guidelines, monthly salary varies from Rs. 40, 000 to 87,500, subject to an overall limit of Rs. 10,500,000 per annum including perquisites.

- Remuneration is restricted to 5 per cent of net profit if the company has one executive, but the total remuneration is not to exceed 10 per cent of net profit if the number of managerial personnel is more than one. These sealing, however do not apply to private limited companies.

- Finally, theoretically, remuneration of managerial personnel is supposed to be guided by job description, job evaluations, salary grades with ranges of pay in each grade and salary surveys. But in practice, the norms seem to have been thrown to winds and exorbitant amounts are paid to decision-makers in organisations. The annual salaries of CEO's range from Rs. 50 lakhs to few crores.

THE 3-PCOMPENSATION CONCEPT

The concept of paying for the 3 P's consists of three parameters that are considered by the management of any organization while deciding the salary as well as the incentives of employees. It is to pay for the Position, the Person and the Performance.

Pay for Position

The focus of the compensation policy translated into the width of the grade, in relation to Pay for Position. The width of the grade is the degree to which jobs of different size are included in the same grade. Therefore, a wide grade, in effect, reduces the emphasis on Position since many jobs of varying job sizes are encompassed in the same grade. In such instances, other factors, such as person's capabilities or competency (i.e. Pay for Person) or an individual's achievement of objectives (i.e. Pay for Performance) will have a much greater impact on the total pay level than the grade level. Broad-banding is an example of this type of approach. By contrast, narrow grades emphasis positions since a small increase in responsibility would lead to a promotion and an increase in grade. A grade width not only determines the overall importance of Position to pay but also can be used to vary the emphasis of the three pay elements-position, person, and performance at different levels of the organization.

Creating a grading structure: The ranking of positions as a result of position evaluation can be converted into grades based on the unique requirements of each organization. This process is called the Internal Position Evaluation (IPE). These grades are created from IPE by answering three questions: One, how many employee groups are there in the organization? Two, how many levels are there within each employee group? Three, how many levels are there within each employee group? The entire organization is first divided into broad classifications depending on designations or levels. Consistent policies are then designed for each of the groups.

Pay for Person

The second P in this model is the "Person"- considered one of the hardest and most subjective part of compensation management. Pay for Person takes into account, a person's capabilities and experience in setting a pay level that is both equitable and competitive. It also considers the market demand of a person's unique skills and experience. Pay for Person is most commonly associated with "competency-based pay". However, it also incorporates a market-based pay approach.

The starting point for this approach is the position. An individual's assessment looks at the person's capabilities and experience relative to the position requirements. Thus, the first step in Person for Pay is to determine the position requirements for competencies and experience. This "position competency profile" lays out the experience and competencies (aptitudes, attitudes, skills, and knowledge) that the organization ideally wants in a person for a given position.

Organizations should be looking for a process that assesses position and people against the same competency criteria within the framework of the organisation's philosophy, image, value, and identity. The 3-P competency profiling forms and process are designed to ensure that competencies are carefully identified, defined and weighted for the specific culture and need of the organization. Each position and person has their own profile, which enables the organization to match positions and persons against each other.

The linchpin between Pay for Positions and pay for person is the Reference salary which is a set based on the market-competitive pay for someone who fulfils the position's requirements for competency and experience. In the 3-P system, the actual salary varies relative to the Reference Salary based on the Position/Person ratio and the number of years that the individual has been in the position. Each grade has its own range of Person for Pay. The minimum pay for each grade is based on the minimum competency acceptable for the position and the corresponding market pay level required to attract a person with that level of competency. On the other hand, the maximum pay for the range of each grade is close to the Reference Salary the logic being that an organization should pay for only those competencies required to fulfill a position's responsibility.

The Position/Person profile and ratio provides a basis not just to evaluate the Pay for Person (i.e the actual salary) but also provides guidance in titling, training, and development. An organization can set the titles within a grade based on the person's competencies relative to the position requirements. Companies can arrange training for the person based on the areas where the person's competencies have fallen short of the position requirement and determine the person's development plans and potential for promotion based on a simulation of profile.

Pay for Person may also include a market premium in case the competencies related to the position are rare and under market pressure. Usually market pressure is temporary since over time, supply and demand equalizes pay levels for jobs of the same size. Thus, market premiums should be paid separately from salary and adjusted up or down based on changes in market conditions. In the present day market scenario, it is the skills and the talents that matters the most. Companies are paying the least attention towards the skyrocketing remunerations of the deserving employees. IIM graduated drawing astronomical packages and breaking their own records year after year are perhaps the biggest example of this.

There are two exceptions that may warrant a permanent premium incorporated into the Pay for Person. These include permanent shortages of skills, capabilities competencies and experience linked to a specific individual. Permanent shortages of skills and capabilities are usually due to controlled and limited supply. This may be the case when a qualification is required to assume a position and the qualifications are limited regardless of demand. This can happen for positions such as doctors, lawyers, actuaries and certified public accountants. In these cases, an organization may pay position holders a salary that incorporates a permanent premium over other jobs in the same grade.

At senior levels within an organization, an individual may possess specific experience and capabilities that uniquely qualify that person for the position. In such cases, an organization may be willing to pay for above the market to secure and retain the individual.

Pay for Performance

The third prefers to Pay for Performance. In 3-P compensation management, the performance of the individual is not the only consideration in setting the salary or granting a salary increase. The logic is that since performance is variable and fluctuates from year to year, so should performance pay be variable and fluctuates from year to year. Granting a salary increase based on one year's performance is equivalent to repeatedly paying a bonus year after year for performance delivered in a single year.

In this new form, an individual's performance is managed through a "performance contract" which comprises the clarification of the role, the setting of objectives, and the review of performance. As an outcome of the performance contract process, a measure of performance at the corporate, unit and individual level becomes the basis for setting the performance pay.

The purpose of Pay for Performance is to define all incentive schemes- short –term or long-term and efficiently reward the employee's contribution to its immediate and long-term results. An efficient scheme implies that it includes agreed-upon, challenging, and realistic targets, that it motivates the employee by linking targets to sizeable rewards, and that it openly and clearly recognize the employee's contribution.

The management chooses from all possibilities one or several types of plans that are in line with the organization's activities, the types of objectives assigned to the employees, and the corporate culture. Rules of eligibility should then be established for each plan. It is very important to remember that for whatever plan each category of employee is eligible, the total amount of possible rewards should be equitable from one person to another. In other words, a similar performance evaluation should bear similar amounts or value of rewards, even if the nature of the incentive plan is different. Finally, in assessing who should be eligible for what plan, it is useful to remember how each plan is funded.

Background

Traditionally, the following have been the characteristics of the compensation structure of a white-collar, non-unionized Indian: high "basic" pay, variable pay restricted to senior management in a few private sector companies, government pay scales often used as the benchmark, an almost guaranteed annual increase irrespective of the organization's performance, and promotion in the hierarchy based on number of years of service completed in the organization.

During the last two decades, the compensation philosophy and, indeed, the compensation structure of Indian organizations, have undergone radical change. It is not surprising that the reason for this change is the growth in information technology-enabled services (ITES) and, more recently, in the business process outsourcing (BPO) industry. The talent war in both of these areas, and the consequent globalization of the workforce across organizations in India, is compelling the finance, human resource (HR), and tax experts to constantly study, benchmark, and redefine the compensation imperatives.

Such jobs involve a more thought-driven solution from the employee. These jobs, termed collectively as "knowledge process outsourcing" (KPO), emphasize the fact that the Indian outsourcing industry has matured and the world has begun to acknowledge the country's specialized capabilities, the high quality of work, and the importance the country places on intellectual property rights. Given the hunt for high-quality jobs, it is not surprising that today the approach to Indian compensation is changing and compensation packages are, in fact, the fattest at senior management levels. While one would expect that this would be true of managers in the United States or any other Western country, surprisingly it is India that has the highest paid senior managers in the world. According to a global study conducted by the Hay Group, Philadelphia, PA, and the synopsis published in the *Daily News and Analysis,* a regional daily published in Mumbai, India is in the pole position in terms of global average real salary of senior managers, followed by Germany and Switzerland. For perspective, India's per capita income stands at 12,416 rupees (Rs) per year.

18.2 GOVERNMENT GUIDELINES :

While for public sector enterprises managerial remuneration is fixed in terms of the recommendation of the pay commissions and parity with the remuneration of the civil servants is maintained, for the private sector enterprises which are companies, Government has certain power to regulate the emolument of the top level managers (Directors, Managing Directors, and Functional Chairman etc.)

- According to sec 198 of Companies Act. 1956, the total managerial remuneration payable by a public company to its Directors, Secretaries and Treasurers or Managers in respect of any financial year shall not exceed 11% of the net of the company for that financial year.

- See 309 (3) prescribes that the managing director and/or whole time directors may be paid up to 5% of the companies not profits for one such director and where there is more than one such director up to 10% for all of them put together.

- Under the Act, the Government is competent to lay down from time to time guidelines for the fixation of managerial emoluments and perquisites.

1) In 1961 the fixed ceiling of salary + perks was Rs.1,20,000 p.a.

2) In 1967 it was Rs.1,80,000 p.a. + perks.

3) In 1969 the guidelines visualised the maximum remuneration of the top level management in the private sector as Rs.2,23,000 p.a.

4) The Sachar Committee made two recommendations in regard to managerial remuneration.

(i) It would be regulated by the company itself or the share holders without consulting the Government subject to overall administrative guidelines of November 11, 1969, issued by Government under the Companies Act, or as per the recommendations of the Boothalingam Study Group i.e. salary maximum Rs.6,000 p.m. and perks 25% of the pay.

(ii) Companies should be classified as A, B, C and D on the basis of effective capitals employed by them. A category companies would be those with an effective capital of Rs. 10 crores & above. "B" those with Rs.5 to 10 crores, "C" with Rs.1 to 5 crores and "D" below Rs. 1 crores.

The Government should indicate the maximum and the minimum salary that could be paid to managerial persons under such category of the companies.

5) In 1978 'K.K. Ray', Member Secretary of the Sachar committee submitted a dissenting note comparing the rates as per 1969 guidelines for private sectors with central government's rates and recommended rational ceilings for the four categories of the private companies keeping in mind the 'Janata Party's' manifesto of 1:10 ratio on the highest paid and lowest paid categories or employees in the private sector.

According to 1978 guidelines the monthly salary for private sector top managerial personnel worked out to be Rs.18,500 p.m. or Rs.2,23,000 p.a.

Whereas top most executives of public sector were paid :

Central Government	Rs. 67,421.00 p.a.
Services Chiefs	Rs. 1,33,844.00 p.a.
Comptroller and auditor general	Rs. 67,412.00 pa.
Public Sector	Rs. 83,740.00 p.a.
Banks	Rs. 83,934.00 p.a.

Salary ceilings for the four categories of private companies are :

Category 'A' Company In scale a fixed salary up to Rs.6,000/- p.m. or

Rs. 72,000/- p.a.

Category 'B' Company- In scale a fixed salary up to Rs.5,000/- or

Rs.60,000/- p.a.

Category 'C' Company- In scale a fixed salary up to Rs.4,000/- or

Rs.48,000/- p.a.

Category 'D' Company- In scale a fixed salary up to Rs.3,000/- or

Rs.36,000/- p.a.

6) The Government of India announced new guidelines on the ceiling of remuneration and perquisites on November 9, 1978.

Under the new guidelines the perquisites would be restricted to amount equivalent to annual salary subject to a maximum of Rs.60,000 a year with separate non interchangeable medical treatments and housing within the limits and a commission of net profit up to 1%. This should be only up to 20% of the salary subject to an overall ceiling on the salary plus commission which would not exceed Rs.72,000 p.a.

But these guidelines caused widespread reactions. The employer organisations and associations of executives were extremely critical of those guidelines. They were of the view that these would encourage the growth of malpractices of all kinds because the existing guidelines do not prescribe the remunerations of the executives below the top level.

Secondly to restrain conspicuous consumption Government has only thought of one category of persons i.e. managers in the private sectors. It has also been argued that in the public sector certain superior perquisites are available e.g. heavily subsidised; medical care etc. and these are being ignored in case of private sector manager's.

7) On October 5, 1979, some liberalisations on the guidelines were issued. The used guidelines on management remuneration give only a marginal concession on house rent, over all ceiling on the perquisite remains at 60,000. The revised ceiling will have retrospective effect from Nov. 9, 1978.

8) As per 1983 guidelines the ceilings on salary, commission and perks were as follows :

Salary	:	Rs. 90,000 pa.
Commission	:	Rs. 45,000 p.a.
Perks	:	Rs. 88,000 p.a.
Total	:	Rs. 2,23,000 p.a.

9) As per 1987 guidelines it was Rs.4,05,000 p.a. The Companies Act was amended in 1974 and hence further called as the Companies Amended Act 1974 to lift/easy to control on managers pay in the private sector.

The entry of multinationals, the return of expatriates and the scouting of talent for the globalising economy resulted in sky rocketing rise in executive remuneration in several sector, occasionally influenced by the logic of dollar parity remuneration.

18.3 ARGUMENTS IN SUPPORT OF GOVERNMENT REGULATION OF MANAGERIAL COMPENSATION :

1. The per capita income is low and a large portion of India's population has remained poor over time.

2. High salaries encourage conspicuous consumption which will have undesirable socio-economic effects.

3. The public policy seeks to reduce income disparities. Some committees noted that the differences in chief executive remuneration's public sector (including nationalised banks) and private sector is 1:3 and between civil servants and private sector chiefs it is 1:4.

4. To safeguard the interest of consumer and public including minority share holders.

5. Avoid unfair competition in managerial remuneration to attract talent which may have undesirable impact on the social welfare sectors of the economy.

18.4 CRITICAL COMMENTS :

Whatever be the rationale and extent of regulation in actual practice ironically, it appears that there is no statutory limit for managerial remuneration (in private sector). If the companies willing to bear the tax on the disallowed portion of the pay, it is not necessary to have any Government approval, unless the executive desire a seat, on the board of director. A change in designation from director to vice-president is enough to come out of statutory restrains on compensation. In the process however company board may be deprived of professionals. The fact that the remuneration of the chief executive in the public sector continues to be only 1/3rd that of their counterparts in private sector has implications for flow of talent from one sector to another, though at that level compensation alone may not be the driving force.

The Gujarat High Court struck down in May 1980, the guidelines of November 1978 modified in 1929 in a case filed by Cibatul Ltd., Dr A.R. Naik.

Section 309 (3) of the Companies Act provide that within the overall limit of 11% of net profit of the company as stipulated in Section 198, remuneration to a managing director or a whole time director shall not exceed 5% of a company's net profit for only one such director and 10% where there is more than one.

In 1961, an administrative ceiling was Rs.1,20,000 p.a.

In 1967, an administrative ceiling was Rs.1,80,000 p.a.

In 1969, an administrative ceiling was Rs.1,35,000 p.a.

In 1978, an administrative ceiling was Rs.1,32,000 p.a.

On 25th August 1978, Delhi High Court struck down 1978 guidelines modified in 1979 as violative of Section 637 AA of the Companies Act, on the appeal filed by the Government, the Supreme Court granted to operate these guidelines only in respective of these companies, which consent to the fixation of remuneration as per those guidelines to keep in obeyance proposals of those who object to such fixation. The same ruling holds good for 1983 and 1987 guidelines also.

18.5 MANAGERIAL COMPENSATION IN PRIVATE SECTOR :

As we found that previously, the Government guidelines were somewhat strict with respect to managerial compensation in private sectors. But soon after liberalisation and globalisation, the guidelines of the Government have become somewhat liberal.

The findings of the Business Today's survey for 1997-98 conducted by Delhi based HRD and Consultancy Firm, Oman Consultants covering 100 corporate across 19 industries reveal that middle managers has more reason to cheer than both their bases and their juniors.

In a year of indifferent growth and dropping profits, the middle manager out jumped the senior manager whose average monthly compensation rose by 14.90% in 1977 and the entry level MBA, who was offered just 9.60% more on campus the same year.

Moreover at the entry or junior level the emoluments are higher in public sector than their counterpart in private sector. However at the middle and top levels it is the private sector where compensation is more attractive in comparison to PSU's.

Unfortunately very little research has been conducted about the higher level executives and junior managers to probe deeply into the relationship between various forms of compensation and motivation, so concentration has been given to middle level managers.

Realistically however, middle managerial pay has entered the real of posts-rightsizing compensation. There can be no doubt that there are fewer middle managers today in most companies that they were in 1995. Having shed the deadwoods of corporates are now lavishing then largest on those in its middle ranges whom they have chosen to retain. Crucially, the specialised skills now required at this level no longer allow managers to be substituted easily. And with targeted staffing replacing the nation of filling up the number, specific abilities are not only in demand but also carry higher pay tags. Post-rightsizing the middle manager who is left is quality resources for any company. Retaining them is obviously a top priority.

The Middle Mangers are classified into 2 categories :

1. Middle Manager I - Companies all those who head of department e.g. Deputy General Manager, Senior Manager and Manager.

2. Middle Manager II - Consists of those who either head a section with in a department as second in command e.g. Senior Manager, Deputy Manager, Asst. Manager.

The Oman Consultants, survey (conducted in 1998) compared the compensation packages offered to the middle managements I and II during the year 1996 & 1997. The average monthly pay for the upper level middle manager at Rs.61,039 rose by only 22% over its 1996 levels. In the case of the lower range the average monthly compensation at Rs.41,176 increased by 22.09% well below the 38% jump in 1996. But then shorter hops were the warm up and down organisations in a year when corporate India's rules rose by only 18.60% and profits actually fell by 8.40%.

Besides the increase appear larger in real terms when compared to low rate of inflation of 6% that prevailed. It is a basic rationalisation of compensation that is taking place in respective of levels. Therefore packages at the top have constricted raises even more. And the bad of opportunities at the entry level were reflected in the class handsome salaries that were offered.

Clearly the middle managers has fought obsolescence and become competent and the most of the transformation has come from his ability to adapt to the changing environment. After being cut to the bone once bloated middle management is developing new muscle now.

18.6 MANAGERIAL COMPENSATION IN PUBLIC SECTOR UNDERTAKINGS (PSU) :

The central PSUs in India, comprising 242 enterprises with a total employed capital at Rs.202,022 crores classified into 4 schedules and 22 cognate groups, plays a significant role in the Indian Economy. Employing 19.78 lakhs personnel of which 6.4 lakhs in managerial and supervisory cadres, compensation in public sector is a complex issue given the diverse nature of business activities, talent may be attached, corruption reduced and discipline ensured by appropriate pay scales and perks. At the same time, the pay bill should not be allowed to strike economy. It is import to compare the pay of Govt. employees with per capita income which may be obtained by dividing the gross national income by population.

Historical perspective of compensation in PSUs :

Compensation in PSUs evolved from ad-hoc fixation by Govt. in 1960's to developing compensation structures on a rational and uniform basis over a period of 4 decades. This evolution passes through many important stages.

Classification of PSEs and fixation of CEOs pay in 1960's:

The pay scales of executives at as well as below the Board level were fixed on an ad-hoc basis by the Govt. by maintaining some parity with comparable positions on the Govt. This practice changed when PSUs were classified into four schedules and pay scales of chief executives fixed bases on the schedules as per the recommendation made by the committee in the case of executives below the Board level, the respective administrative ministers fixed with the Bureau of Public Enterprises and Ministry of Finance, which led to some homogeneity in the pay scales.

Restoration of relativity and party - 1980's :

In 1982 a need was felt for revision of emoluments for executives at the below Board level in order to restore the relativities between the emoluments of officers in the scheduled post and other officers. It was then decided that such revision would have effective for five years from 1st August 1982. This was the beginning of serious efforts to rationalise the managerial compensation in PSUs.

Uniformity and flexibility - 1990's :

The guidelines issued by the Govt. in 1990, based on the recommendation of high power pay committee headed by Justice R.B. Mishra made a significant effort to streamline the pay structure in PSUs and also attempted to bring in uniformity by rationalising the pay scale. The pay revision that took effect from January 1st 1992 was based on the guidelines issued by the department of Public Enterprise. These guidelines include 14 scales of pay for the executives below the Board level and non-unionised supervisors.

18.7 CONSTITUTION OF JUSTICE MOHAN COMMITTEE :

A pay revision committee consisting of five members was constituted under the chairmanship of 'Justice Mohan' in 1997. The four other members of the committee are

1. Former R.B.I. Governor - Mr. S. Venkataraman
2. Chairman of the Housing Development Finance Corporation - Dr. Deepak Parek.
3. The JNU Professor - Dr. Deepak Nayyar.
4. The Secretary, Department of Public Enterprises - Mr. P.G. Mankad.

The term of reference for the committee were, to examine the present structure of pay, allowance perquisites and benefits for the executives (both at as well as below the Board level) and non-unionised supervisory categories in central PSEs, taking into account the total package of benefits available to them including non-monetary ones, and suggest changes that are both desirable and feasible. It was also suggested that the committee take into account the report of the 5th Pay Commission. The Committee submitted its report on October 30, 1998. The committee directly interacted with senior officers of Govt. of India CEOs Executive of PSEs Representatives of Officer Associations, SCOPE and Central Trade Union Representatives.

Mohan Committee considered issues such as :

1. Capacity to pay

2. The relativity issue
3. The need for Autonomy
4. Performance and emoluments
5. Uniformity and differentiation.

18.8 RECOMMENDATIONS OF THE COMMITTEE :

1. A relativity of 1.12 : 1 between the pay of CEO of schedule A, PSEs and that of a Secretary level officer of the Govt. of India and a near 1 : 1 parity at the entry level.

2. The relativity between the pay of highest paid executive and lowest paid employee should be about 10 : 1 and between the CEO at the highest level and the executive at the point of entry should be about 4 : 1.

3. Fitment benefits of 20% of Basic pay, including personal pay and excluding all other components.

4. To adopt 100% neutralisation of cost of living the capacity of adjustment of D.A. to be six months.

5. The pay revision to be after ten years or co-terminus with the next pay revision for central Govt. employees.

6. To adopt the recent re-classification of cities for HRA and to pay HRA at the following rates.

Classification of cities	**Rates of HRA as percentage of Basic Pay**
A - 1	30
A	25
B_1 and B_2	15
C and below	10

7. Perquisite and allowances may go up to 50% of basic pay in few enterprises, where the level of perquisites and allowances today exceeds 50% payment over and above the ceiling should be entirely in the nature of performance related payments, which should not exceed 50% of the basic pay. It is desirable to consider whether such performance rated payments do in fact lead to improvement in performance, productivity and profitability at the end of a reasonable time.

8. Those sick PSU that have been provided budgetary support for various reasons may have to be provided additional funds to meet the requirements of the revision unless it is found that the provision provided is not justified.

9. In order to rationalise the manner in which sick undertakings are treated a core group of secretaries assisted by finance expect be formed to look in to the problems and prospects of sick PSUs within a

period of 6 months. This core group can identify by the such undertakings can be nursed back to health provided with new strategic business plans and adequate funds including emoluments on revised scales, for undertakings that cannot be so restructured, the group should take early steps to close down by VRS or any other measure.

10. P.F. and gratuity to continue as they are and the provisions of the employee pension scheme 1995 be so amended to allow PSEs to chose the Govt. pension scheme or to work out their own individual pension schemes.

11. PSEs could as far as possible, look in to obtaining mediclaim cover through insurance companies for their retired employees. Fund for this purpose should be contributed by both employees and organisation.

18.9 FINANCIAL IMPLICATIONS :

Overall financial implication of the recommendations of the committee is estimated to be in the range of Rs.207 - Rs.2300 crores as compared to the present level of local emoluments for executives and non-unionised supervisions at around Rs.6000 crores.

18.10 ISSUES CONSIDERED BUT NOT RECKONED :

Mohan committee considered issues such as capacity to pay, relativity issues etc. None if these issues seen to have been taken us to account while finalising the recommendations. Govt. was asked to provide funds for revision, relativity with private sector was avoided, autonomy was totally controlled with standards and ceilings no framework was given for linking pay to performance and no clear demarcation was made between uniformity and differentiation.

18.11 CRITICISM :

The final recommendations made by the committee were considered by factors such as financial impact on the economy, equity, principle, divergence of PSUs and the need to contain the wage level. The report as stated in their own words, was an exercise in constrained optimization. The committee seems to have been influenced by the recommendations of past committees and revisions rather than evolving with its own frame work for dealing with current issues.

18.12 ELEMENTS OF WAGE REVISION IN PSUs :

1) The Government today decided to rise wages of public sector executives based on recommendations of S. Mohan Committee. The total revenue out go will be Rs.2,070 crores annually but the burden will have to be borne largely by the public enterprises themselves as no budgetary support will be provided for the purpose. The provision will benefit 3.6 lakh executives and non-supervisory staff in the public sector.

2) Under the new wages, the lowest salary scale payable to the unionised supervisions will rise from Rs. 3,375 - Rs.5,875 to Rs. 6,400 - Rs. 10,000. At the 1st level of board appointees in ‘A’ the scale will increase from the existing level of Rs.13,000 - Rs.15,000 to Rs.27,750 - Rs.31,500.

18.12.1REVISED PAY SCALES :

Revised pay scales for public sector executives as announced by the Govt. of India on May 24, 2000.

Schedule	Existing scales affective from 1-1-92 (Rs.)	Scales to be effective from 1-1-97
A	13000-15000	27750-31500
B	12000-14000	25750-30950
C	10000-12000	22500-27300
D	9000-10500	20500-25000
Below Board level scales		
E_0	3500-6200	6550-11350
E_1	4000-7150	8600-14600
E_2	4800-8275	11500-16750
E_3	5400-9050	1300-18250
E_4	6500-9425	14500-18700
E_5	7000-9600	16000-20800
E_6	7500-9900	17500-22300
$E_{7\text{-}a}$	8250-10050	18500-23900
$E_{7\text{-}c}$	8500-10300	18500-23900
$E_{7\text{-}c}$	9500-11500	20500-26500
E_8	9500-11500	20500-26500
E_9	11500-13500	23750-28550
Non Unionised supervisors scales :		
S_1	2800-4850	5200-8000
S_2	3000-5055	5600-8600
S_3	3200-5290	6000-9200
S_4	3375-5875	6400-11000

3) In case of sick companies including these referred to the BIFR, the revised pay scales will apply offer a strategic plan of restructuring for revival has been approved. Though there is no budgetary support will be made available to the enterprise, there will be no impact on the budget and funds from the revised pay scales will have to mobilised from internal resources of public sector companies.

4) 100% neutralisation will be adopted for employees drawing Industrial Dearness Allowance rates and adjustment will continue to be made every three months as at present.

5) House rent allowances to Public Sector Employees will be at rates applicable to central Govt. employees.

6) Payment of allowances and perks will be allowed up to maximum of 50% of basic pay.

7) Payments in the nature of performance related payments can be made by PSUs up to maximum of 5% of the distributable profits of the enterprise.

8) Mediclaim covers through insurance companies for their retired employees.

9) Besides above these benefits or compensation there are some other superannuation benefits are now given like pension and gratuity. The pension doesn't exceed 50% of pay. Gratuity is a welcome addition to pension. But there is a ceiling on gratuity which is unjustified and unwarranted.

Changing trends in compensation

It is interesting to track the changes—some quite radical—in the Indian compensation scene. The following are true of most organizations today:

- Compensation is now viewed as the total "cost to company," (CTC) rather than an employee's net pay alone. As the environment gets competitive, such an approach helps organizations take a holistic view of what could be the costs and the operating margins.

- Variable pay based on individual performance is the norm, and a larger percentage of the Indian salary is based on performance.

- Organization performance also is factored in while structuring salary increases.

- Some organizations also have implemented highly evolved systems, such as the "economic value added" (EVA) framework, ensuring a performance-oriented culture throughout the organization applicable to all employees.

- Basic, guaranteed pay has seen a gradual reduction.

· Benchmarking against organizations, both nationally and internationally, has become common.

· Employee stock options (ESOPs) that were, a few years back, considered as valuable compensation components have ceased to be so given the erratic nature of the stock market and the lock-in periods.

· Non-taxable benefits, which increased the net "take-home" of an employee, are now subject to the Fringe Benefits Tax (FBT), and so organizations are forced to take second looks at these components.

· Retirement benefits are left to what is mandated by the government. Organizations that were contributing to a superannuation fund for the employee now have to pay the FBT.

· Pension benefits and other similar social security benefits are not on the radar screen of compensation experts in India today, but this component could be under significant discussion and speculation in the coming years.

18.13 MANAGERIAL COMPENSATION IN PRIVATE SECTOR Vs. PUBLIC SECTOR :

I. In 1978 guidelines salary for private sector managerial personal worked out to be Rs.18,500 p.m. or 2,23,000 p.a. whereas PSUs top executives were paid 83,740,000 p.a.

II. In PSEs some superior perks are available, e.g. heavily subsidised house, medical care etc. and these are being ignored in case of private sector managers.

III. Some committees noted that the differences in CEOs remuneration between PSUs and private sector is 1:3.

IV. More over at the entry or junior level the emoluments are higher ion PSUs than their counterparts in private sector. However at the middle and top levels it is the private sector, where compensation is more attractive in compensation to PSUs.

V. For private sector undertakings the salaries or compensations are fixed by the entrepreneurs and some Govt. guidelines are there for the compensation rate of top executives. In case of PSUs the remuneration or compensation are fixed by pay commission recommendations.

18.14 SUMMARY :

Despite a major up-trend, India Includes salary structure is still significantly lower than that of developed country. It is quite apparent that salaries are increasingly driven by performance rather than years of experience. The downside of performance linked incentives and higher salaries go insecurity. Competitive pressures facing the corporate world are permitting down to the individual employee level. This is a term makes the employee aware and alert of the fact that efficiency is followed by success, and failure by job loss. Executives thus face perform or perish situation.

If the Government employees want a substantial increase in their pay, they have to accept reduction in the strength of staff and increase in productivity as in the private sector; it is however, the state's duty to create conditions congenial for the continuous increase of minimum wages. Balance can be achieved by linking the salary of the Government servants to the per capita income.

Capacity to pay of the Public sector enterprises, relatively between emoluments in PSU's vis-a-vis the Governments need for autonomy in determination of compensation and requirement of uniformity of pay scales across PSEs.

The management of PSEs must be provided with some structural flexibility in the implementation of pay scales such that outstanding managers can be attracted and rewarded through special measures. System must be evolved to link performance related payments to performances and to increase the proportion of such payments to gross emoluments of overtime.

It should be born in mind that these packages are offered to only a select few in the organisation, primarily those who are responsible and accountable for the company's performance in the face of increased global competition.

With international competition there is now a greater need for retaining the best talent within the country and reversing brash dream. Therefore the price paid by today's company's for seminar managers is justifiable. Fears about unbridled growth in remuneration leading to decreased competitiveness re unjustified because these incentives are directly linked to results. Therefore, executive compensation demands careful though and attention to maintain the kind of leadership i.e. essential for an organisation's continued growth and vitality.

18.15 KEYWORDS:

Private sector: The private sector is that part of the economy, sometimes referred to as the citizen sector, which is run by private individuals or groups, usually as a means of enterprise for profit, and is not controlled by the state (areas of the economy controlled by the state being referred to as the public sector)

Public sector: The public sector is the part of the economy concerned with providing various government services.

18.16 SELF ASSESSMENT QUESTIONS :

1. Do you think that Indian executives are overpaid? Discuss.

2. Discuss the recent trends and developments in Managerial Compensation.

3. What action can the government take when companies violate statutory guidelines relating to executive remuneration?

4. Briefly enunciate the role and important provisions of the Companies Act, 1956 on Executive Remuneration.

5. What type of compensation systems normally motivate the executives?

6. Analyse the recommendations of various committees and commissions to Managerial Compensation.

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LESSON - 19

ROLE OF HUMAN RESOURCE DEPARTMENT IN EMPLOYEE COMPENSATION

19.0 OBJECTIVE :

After reading this lesson, you should be able to :

- Know the Role of Human Resource Management Department in Compensation.
- Study the Several HR Practices in Relevance to Compensation Management.
- Visualise the Compensation Plans / Policies and HRM Strategy.
- Review the Challenges of Remuneration / Compensation Practices.

STRUCTURE :

19.1 Introduction

19.2 Employee compensation benefits

19.3 Compensation Issues to Organisation

19.4 HRM Department Role in Compensation Administration

19.5 HR Department Role in Pay Determination

19.6 HR Department Role of Conducting Pay Surveys

19.7 HR Department Role in Preparation of Pay Structure

19.8 Compensation Plans / Policies and HRM Strategy

19.9 Devising Compensation Plan / Policies

19.10 Challenges of Remuneration / Compensation

19.11 Elitism versus Egalitarianism

19.12 Monetary Versus Non-monetary Rewards

19.13 Wages and Salaries

19.14 Summary

19.15 Keywords

19.16 Self Assessment Questions

19.17 Further Readings

19.1 INTRODUCTION :

Employee Compensation decisions are crucial for the success of an organisation. From as cost perspective alone, effective management of employee compensation is critical because of the total operating costs. It is all the more in some labour intensive organisations. Of course, cost is only one part of the picture. It is also necessary to evaluate an employee's contribution to the organisation, in exchange. Another reason for studying compensation from the organization's perspective is to assess its impact on a wide range of employee attitudes and its units.

Compensation may directly influence key outcomes like job satisfaction, attraction, retention, performance, skill acquisition, cooperation, flexibility, and so on. Compensation includes any direct or indirect payments to employees, such as wages, bonuses, stock options, and benefits. Ehrenberg and Milkovich (1987) have defined pay level as the "average

19.2 EMPLOYEE COMPENSATION BENEFITS:

The **compensation and benefits processes** belong to most important HR Processes, which are critical for the organization and modern HR organization. The compensation and benefits is about managing the personnel expenses budget, setting the performance standards, setting the transparent compensation policies and introducing the competitive benefits for employees. The organization with effective compensation and benefits drives its personnel costs, manages the performance of employees and rewards the extraordinary performance.

The compensation and benefits functions of HR often can be handled by one HR specialist with dual expertise. On the compensation side, the HR functions include setting compensation structures and evaluating competitive pay practices. A compensation and benefits specialist also may negotiate group health coverage rates with insurers and coordinate activities with the retirement savings fund administrator. Payroll can be a component of the compensation and benefits section of HR; however, in many cases, employers outsource such administrative functions as payroll.

This covers salaries, bonuses, vacation pay, sick leave pay, Workers' Compensation, and insurance policies such as medical, dental, life, and 401k. The Human Resources Department is responsible for developing and administering a benefits compensation system that serves as an incentive to ensure the recruitment and retainment of top talent that will stay on with the company. When an employee is hired, the company's Benefits Coordinator is required to meet with employees one-on-one or in small group settings to explain their benefits package. This often requires an employee to make an informed decision and to provide their signature for processing purposes

19.2.1 Compensation and Benefits Role

The compensation and benefits processes **introduce the transparency into Human Resources** and rewarding employees for the achieved performance. The compensation and benefits provides the managers with the **compensation tools** to build a difference among employees as the high performance corporate culture can be built in the organization. The compensation and benefits department monitors the external job market and optimizes the personnel expenses budget of the organization. The compensation and benefits defines the compensation strategy, sets the transparent and simple compensation policy and defines the general rules for the extraordinary payments, bonus schemes applied in the organization and introduces general other compensation policies like the Relocation Policy, Short-Term Assignment Policies, Benefit Car Policies and other.

19.2.2 Compensation and Benefits Responsibilities

The compensation and benefits department is usually responsible for the **transparency in the compensation practices** in the organization and keeping the internal fairness of the total cash. The compensation and benefits has to supervise the development of new compensation components and keeping the general rules for the design of the compensation component.

The compensation and benefits department is responsible for the personnel expenses budget of the organization. The compensation and benefits department sets the standards for the individual salary increase, the mass salary review and the rules for the bonus payout as the organization keeps the financial stability and the planned personnel expenses budget is kept.

The compensation and benefits department has special processes to monitor the external job market as it can set the **right compensation policy**, which is compliant with the approved compensation strategy. The compensation and benefits department is responsible for the extensive monitoring of the market and designing the new compensation components inspired by the HR Best Practices in the compensation area.

The compensation and benefits department is always closely attached to the development of the **new compensation components**, which support the performance and effectivity of the organization. It co-operates with the different business units and it aligns their requests into the general rules for the compensation components, which are transparent and fair. The compensation and benefits designs new adjustments to the **compensation strategy** and the **compensation policy** as the organization does not lose its competitive advantage on the job market.

19.2.3 Compensation and Benefits Content

It is responsible for organisation of people in the entire Company and plans for future ventures and objectives involving people in the Company. *These roles come with certain positive and negative aspects in compensation packages.*

Improvement of Compensation Packages (positive aspect)

One of the major functions of the HR department is to **motivate employees**. This can be done through **rewards** especially for those who have done well. The HR department needs to evaluate performance of employees and those who have exceeded expectations should be compensated for their actions. Research has shown that rewarding employees for good performance is the number one incentive for keeping up this trend. These compensation packages can come in the following ways;

- Holiday offers
- End of the year bonuses
- Equities
- Awards

- Salary increments
- Provision of flexible working hours
- Straight forward promotion schemes and career developments

If the HR department includes these incentives, then it will ensure that employees are satisfied with the company. It will also contribute towards good staff retention rates. This is especially crucial in increasing stability within the organisation. It also makes employees identify with the firm and instills a sense of loyalty.

Problems in Remuneration (negative aspect)

In the process of trying to motivate members of staff to perform better, the Human Resource may make deals that eventually cause problems. A case in point is the **Home Depot**. This company has an employee compensation policy that requires that one should be rewarded for the time they have served the company.

The Home Depot Company offers an end of year bonus, basic salary and grant on stock shares as an incentive for some of its employees. The CEO of the Company **Robert Nardelli** lost his job in the year **2007**. This was because the company has experienced a lot of losses under his leadership; its shares fell by eight percent in the stock exchange and he deserved to leave the Company. However, because the **Human Resource Department** had put in place a policy that requires all members of staff to be given the incentive mentioned above, he left with a lot of money. It was reported that he had with him about two hundred and ten million dollars. The Company had no way out of this payment because HR had already passed that policy and they were bound by the law. This goes to show that sometimes policies made by the HR department do not benefit the Company especially if the parties involved are considered as losses to the Company.

19.3 COMPENSATION ISSUES TO ORGANISATION :

The domain problem facing any organisation is the laying down a fair and equitable compensation system. While the objective is simple, the process is complex. For instance, the employer will be concerned primarily with productivity. The employee's emphasis may be on higher compensation to offset their increased cost of living and perhaps the price his skill will fetch in a competitive job market. The compensation issues commanding most interest today and likely to continue in future will centre around questions of compensation levels and compensation structure. Obviously, this will raise questions concerning the level of compensation in the plant or firm, industry, region, or nation. Closely related to this is the broad question of the determinants of various influences controlling compensation, the nature of decision making bodies and the different traditions and customary attitudes that have developed in individual firms or industries. In some cases, the controlling influences may be standards in a particular locality or region, sudden change in technology, source of labour supply, firm's competitive standing, general sales-and-profits prospects of the industry, and so on.

The managerial decision about compensation rates in a given situation has to be reconciled with a variety of considerations such as when pay rates should be changed and by how much, how they should be distributed among the different employees, and what firms should be covered. Disputes between employers and unions over wages and salaries are often a part and parcel of conflicts over such diversified matters.

One of the important considerations the HR Department involving in formulating a pay package is the quantum of take-home pay that is the net packet, after an employee has paid for his deduction. Some of these dedications are saving for old age, like the provident fund and pension schemes. The balance something that is variable in each case. In an employee's earlier years, normally, children's education, medical treatment, recreation will necessitate a larger income. In his later years an employee will need to provide for his old age, in terms of a house and a steady income to maintain his habituated life style. Another HR related issue is salary and tax planning. In this context, organisation has taken recourse to fringe benefits, some of which are taxable. The incidence of tax, either on money incomes or on the total taxable income including perquisites, has to be worked out.

19.4 HR DEPARTMENT ROLE IN COMPENSATION ADMINISTRATION :

Compensation administration deals with techniques and procedures for designing and maintaining salary structure regarding staff, executives and exercising pay controls. The basic aim of compensation administration is to attract, retain and motivate employees by developing and maintaining competitive and equitable salary structure. It is formulated and maintained by HRM Department and concerned with :

1. HR Department involving in the design and maintenance of pay structure;
2. HR Department participated at the operation of salary progression systems;
3. Implementing the provisions of employee benefits and other allowances; and
4. Prepare, maintain and the development of a total remuneration policy.
5. The tasks of HRM People / Compensation Administrator is a broad and complex one.

HRM Department shall consider the following guidelines for Compensation Administration.

1. Compensation should be competitive with what other employers are paying for similar skills or similar jobs.
2. Compensation paid to various individuals in an organisastion should reflect the comparative value of their respective contributions to that organisation.
3. Compensation decision should be made and communicated in a way that is perceived as rational and fair.

The following aspects of compensation planning and administration shall be implemented by HRM Department for executives / managerial levels : (i) position level, (ii) the salary structure, (iii) performance appraisal, (vi) incentive bonus plans, and (v) supplementary forms of compensation.

A basic approach to pay problems involves identifying needs, objectives, developing programmes, and planning and executing the programmes.

19.4.1 IDENTIFYING NEEDS :

The first approach to wage and salary administration is a realistic appraisal of needs. Needs can be determined in various ways. Personnel specialists should have sufficient knowledge and experience to predict pay problems. Also the line managers must possess knowledge of the company's pay problems from their operating experience.

19.4.2 DETERMINING OBJECTIVES :

It may not be practical to attempt to solve all the pay problems which can be identified. Solution of one problem may create more serious ones. Hence, it is important to make a qualitative analysis of needs and then to translate these needs into realistic, specific, and attainable objectives.

19.4.3 DEVELOPING PROGRAMMES :

After objectives have been established, it is possible to consider various techniques and procedures for receiving them. Pay programmes are easier to design and apply when the preliminary steps of determining needs and objectives are done well.

19.4.4 PLANNING AND EXECUTING THE PROGRAMMES :

Once a programme is determined, there must be some planning of the manner in which it will be carried out. Planning should provide for follow-up at various stages to determine both progress and results. It is important to specify who is responsible for accomplishing the various aspects of the programme that has been established.

19.4.5 RESPONSIBILITY FOR COMPENSATION ADMINISTRATION :

Responsibilities should be fixed carefully so that each HR specialist associated with the programme knows exactly what is expected of him. The question is basically one of determining which assignments will be given to the individual supervisor, which will be retained by higher-level line management, and which will be assigned to staff personnel.

In actual practice, the HR Manager seldom has complete authority and responsibility for wage and salary administration. His authority is limited because of the need for consistency in administering the wage and salary programme among the different sections of the company. Thus, policy formulation is generally retained by top management. Higher-level management may also limit the authority of individual managers by establishing techniques and procedures to ensure conformity with company policies. Furthermore, salary administration encompasses a considerable body of knowledge and skill.

It would be both unreasonable and impractical to expect all line managers to become expert in this specialised field.

Line managers have the basic responsibility for making pay decisions within the framework of policies, practices and techniques which have been established by the company. The quality of their day-to-day decisions is really the heart of any wage and salary programme. Line managers also have a role to play in policy formulations. Even where they do not participate in it on a formal basis, they offer constructive ideas for improved wage and salary administration.

Compensation Management specialists also have certain areas of responsibility in carrying out the programme. Research in wage and salary administration is a basic staff function. It generally includes such assignments as compensation surveys; preparation of reports administration of company controls; investigation of programmes, practices and techniques used by other companies. Because of the specialised knowledge obtained through research, the staff specialist can play a significant role in such areas as developing and recommending wage and salary policies, plans, programmes, and procedures; assisting line managers at all levels in interpreting and applying wage and salary programmes; advising and counseling line managers on the various ways and salary problems which may arise. Staff personnel also carry out the work of job descriptions. A final function of the staff lies in the area of audit and control. Top management must establish some means of auditing and controlling the wage and salary actions of managers.

19.5 HR DEPARTMENT ROLE IN PAY DETERMINANTS :

At the outset, it is important to distinguish between two related but different questions. First, one can ask what factors account for individuals differences in pay within organisation. An extensive literature suggests that education, experience, performance, and other individual differences play some role in pay determination.

19.5.1 PRODUCT MARKET :

Labour market and product market competitors play an important role in determining the pay level. Mohoney (1979) and Dunlop (1957) argues that product market competitions places an upper boundary on pay level because organisations in a particular industry "encounter similar constraints of technology, raw materials, product demand, and pricing". Thus, an organisation will find itself at a competitive advantage in the product market if its labour costs exceed those of its competitors. The reason being such costs will ordinarily reflect to some extent in higher prices for its products. For example, if Hindustan Motors will have difficulty in providing the same quality of automobile as a competitive price. Consequently, product market pressures may act as an upper boundary on employee compensation.

19.5.2 LABOUR MARKET :

Organisations not only compete solely in the product market but also in the labour market. Maruti Udyog, for example, compete for engineers, lawyers, and human resource managers. A pay level that is too low relative to these competitors could lead to difficulties in attracting and retaining sufficient numbers of quality employees. As such, labour market competition can be seen as placing a lower boundary on pay level.

19.5.3 LEGAL ENACTMENTS :

The HR Managers shall follow and implement the wage/compensation legislations i.e. The Minimum Wages Act, 1948, The Payment of Wages Act, 1936, The Equal Remuneration Act, 1976 and The Payment of Bonus Act, 1965.

The main purpose of the Payment of Wages Act is to ensure regular and prompt payment of wages and to prevent the exploitation of the wage earner by prohibiting arbitrary fines and deductions from wages. Periodical fixation and revision of wages under Minimum Wages Act and their effective implementation is very much desirable. The Payment of Bonus Act provides for the Payment of Bonus to persons employed in certain establishment and for matters connected therewith. The Equal Remuneration Act provides for the payment of equal remuneration to men and women for the same work, or work of a similar nature, and for prevention of discrimination against women.

19.6 HR DEPARTMENT ROLE OF CONDUCTING PAY SURVEYS:

HRM Department attempt to gather information about pay practices of competitors through the use of pay surveys. However, finding the "going rate" of pay may be easier in theory than in practice. Administrative decisions on pay involves a range of questions including the following :

(a) Which employees are included?

(b) Which jobs are included?

(c) Which jobs are considered similar enough to use in benchmarking?

(d) How are the multiple rates of pay weighted and combined in a multiple survey?

The choice of organisations in probably one of the most important decisions in conducting pay surveys. The HR Department must decide:

(a) which employers are its key competitors in both its labour and product markets; and (b) whether to give more weight to either the product or labour market.

In considering the latter decision, there are probably several factors that argue in favour of emphasising one or the other. For example, product market comparisons are likely to deserve greater weight when (a) labour costs represent a large share of total costs, (b) product demand is elastic, (c) the supply of labour is inelastic and (d) employee skills are specific to the product market, and will remain so. In contrast, labour market comparisons may be more important to the extent that (a) attracting and retaining qualified employees is difficult, and (b) the costs of recruiting replacements are high.

Another phase of comparisons of levels of wages is concerned with wage differentials among the various regions of the country. Geographic wage differential implies different rates for the same job in a company and differences in the average wage among regions because of the type of industries located. Under the slogan, "equal pay for equal work", the demand is frequently made to eliminate such differentials within a company. Where a union represents workers in a company with plants in different regions of the country, one of the pronounced objectives usually is to eliminate geographic wage differentials.

Apart from establishing desired relationship with the external market, it is also vital that the internal pay relationship be maintained. The HRM Department shall periodically review of job evaluation and salary structure is to be carried out to assure the company's ability to pay on a competitive basis.

19.7 HR DEPARTMENT ROLE IN PREPARATION OF PAY STRUCTURE:

Pay structures are essentially hierarchies. 'Milkovich and Newman' (1990) define them as the array of rates paid for different work within a single organisation, focusing attention on the levels; differentials, and criteria used to determine those pay rates. Also, there are certain additional features of pay structure such as:

(i) Number of distinct hierarchies (e.g., separate ones for executives, office staff, managers and engineers, or dual ladders that combine the latter two)

(ii) Number of levels in each (i.e., salary grades and classes)

(iii) Pay differentials between adjacent levels.

(iv) Differentials between the maximum and minimum paid within a grade

(v) Time duration for an employee to progress through the hierarchy.

19.7.1 CONDUCTING JOB EVALUATION :

Most pay schemes are founded on the idea of paying individuals based on the job they hold, leading to the system of job evaluation. Job evaluation is a formal procedure for ordering a set of jobs or positions in an organisation with respect to their inherent value or work in achieving the organisation's objectives. This procedure is usually linked to a rate of pay prescribed for that job.

Regardless of the specific type of job evaluation procedure used, almost all share a similar methodology. First, jobs to be evaluated are carefully prescribed using a thorough job analysis. Second, based on the description of the job, each job is evaluated with respect to its value or work to the organisation, and the jobs are then arranged hierarchically with respect to this evaluation. Finally, these results are used to set wage rates within the organisation.

There are four major methods of job evaluation which can be selected by the top executives of HRM Department for Job Evaluation : (1) Job ranking systems (2) Job classification systems (3) Factor comparison systems, and (4) Profit systems.

While job evaluation approaches are probably the most prevalent methods of establishing base pay, their usefulness like the usefulness of any management system depends on how well they achieve their objectives. Nevertheless, they have a role to play in the administration of compensation. It can provide, at least an internally justifiable wage structure for organisations.

Although job evaluation is a common practice used by HRM Departments to help design and rationalise an acceptable pay structure, other administrative procedures are used to help design and manage acceptable pay structures. In fact, skill-based plans are widely regarded as a superior alternative to job evaluation (Gupta, Jenkins and Curington, 1986; Lawler, 1989). Skill-based structures pay employees for the skills they possess, demonstrate, and/or apply, in contrast to job-based structures, in which employees are paid for the jobs they perform. These plans are grouped into two types; (a) Knowledge plans, which link pay differentials to the depth of knowledge related to one occupation (e.g., scientists, teachers) and (b) multi-skill plans, which link pay differentials to the number of different sets of tasks an employee is supposed to perform.

The single biggest advantage of skill-based pay systems in a production setting is increased flexibility. Because workers know more than one job, they can move with ease from one task to another as the need arises. As the market and product demands change, workers can move from one set of jobs to another. Absenteeism and turnover tend to be lower in organisations using skill-based pay.

From the perspective of employees, a number of advantages may be gained from skill-based pay systems. Perhaps the most noticeable is an increase in satisfaction. The increased flexibility may also create increased job security for employees. The organisation will be able to maintain a more stable workforce, redeploying people in times of low shifting demand. By rewarding skill acquisition these systems encourage employees to become more valuable to the organisation by mastering new skills.

19.7.2 ANALYSE OR FORECAST THE FUTURE TRENDS :

Introduction of performance related payment systems in various industrial organisations is a much debated topic today. Although performance related pay appears to be an attractive proposition, it is very difficult to implement effectively. The HRM Department has to be confident that it can measure performance accurately and introduce a scheme that is objective and perceived to be fair. The HR people follow the latest developments, recent changes and practices for the performance appraised for pay structures.

There are some organisations that see pay as the clearest method of delivering a message to an employee to reinforce the value of teamwork. As interest in individual schemes declines, the interest in team-based schemes grows. There have been a set of recent research findings in the U.S. reporting the success of team-based schemes. These have concentrated on gain-sharing and profit-sharing schemes. Team-based pay appears to be growing at a rapid rate in the U.K. and Japan.

Incentive schemes play a major part in remuneration system. For instance, in our country different types of productivity and profit linked bonus schemes are operating in different enterprises over a period of years. The recent innovation in the compensation system is stock option. This incentive is used to recognise improved performance and rich contribution of the employees and provides them with an opportunity to build ownership. Its major purpose is to reward performance over a longer period of time and to encourage employees to stay with the organisation. In future, stock option schemes are likely to gain momentum and popularity as a fringe benefit in many industrial organisations in our country.

19.8 HRM STRATEGY AND COMPENSATION PLANS / POLICIES :

Remuneration plans/policies like any other HR activity must become an input to formulating a business strategy. But in most companies, this integration rarely occurs. The general practice is to pay what competitors pay or to adhere to the "corporate policy". The actual remuneration plan should not be strictly a matter of what is being paid in the market place. Instead, wage and salary plans must derive from an assessment of what must be paid to attract and retain the right people, what the organisation can afford, and what will be paid to attract and retain the right people, what the organisation can afford, and what will be required to meet the organisation's strategic goals. Table 19.8.1 illustrates how different compensation strategies can be applied to firms that differ in (i) their business strategies, and (ii) their market position and maturity.

In companies that are growing rapidly, business strategy tends to be focused on investing to grow. To be consistent with this business strategy, HR strategy, the remuneration strategy should stimulate an enterprising and entrepreneurial style of HR management. For this purpose, the company should emphasise high cash payments with above-average incentives. In 'mature' companies, its business strategy is oriented primarily towards managing earnings and protecting markets. A remuneration strategy must have a blend of average cash payments moderate incentives and standard benefits and should aim at rewarding management skills. In an 'aging' company, the most appropriate strategy is to harness earnings and reinvest them elsewhere. Remuneration strategy should therefore aim at control of costs. To improve such a modest incentives are tied directly to control costs. Thus, HR specialists do the following, viewing remuneration from a strategic perspective :

1. HR Department recognise remuneration as a pivotal control and incentive mechanism that can be used flexibly by the management to attain business objectives.

2. HR Manager make the pay system an integral part of strategy formulation.

3. HR Department integrates pay considerations into strategic decision-making processes, such as those that involve planning and control.

4. HR Executives view the company's performance as the ultimate criterion of the success of the strategic pay decisions and operational remuneration programmes.

Table 19.8.1 Linkage of Compensation Strategy to Business & HR Strategy

Business Strategy	Market Position	HR Dept.	Compensation
Invest to grow	Merging or growth rapidly	Stimulate entrepreneurialism	High cash with above average incentive for individual performance. Modest benefits.
Manage Earnings -	Normal growth to maturity	Reward management skills	Average cash with moderate incentives on individual, unit, or corporate performance. Standard benefits.
Harvest earnings – reinvest elsewhere	No real growth or decline	Stress on control	Below-average cash with small incentive tied to cost control, Standard benefits.

Source : Wayne F. Cascio, Managing Human Resources, McGraw-Hill, 1995.

19.9 DEVISING COMPENSATION PLAN :

Any remuneration plan must be understandable, workable and acceptable. The remuneration scheme must have two components - a base rate and the scope for increasing the base rate. The remuneration plan must have two components - a base rate and the scope for increasing the base rate. The remuneration plan must be determined keeping in mind the requisites and the components.

The HR Department is responsible for determining compensation plan, a model of plan of sequential steps as described below.

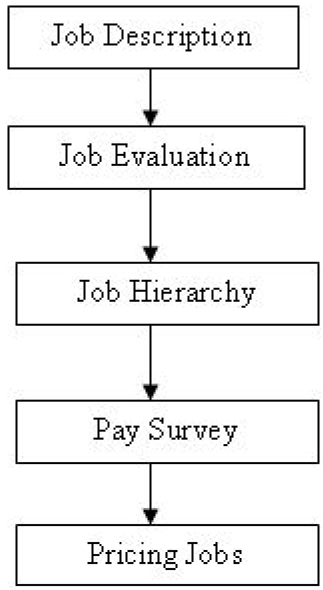

Fig. 19.9.1 Compensation Model

19.9.1 JOB DESCRIPTIONS :

Job descriptions are crucial in designing compensation systems, for, they help to identify important job characteristics. They also help determine, define and weigh compensable factors (factors for which an organisation is willing to pay - skill, experience, effort and working environment).

19.9.2 JOB EVALUATION :

The next step in pay fixation is to establish relative worth of jobs by employing job evaluating. A number of techniques are available to evaluate jobs. For example, in the point-ranking method job evaluation, each job is analysed and defined in terms of the compensable factors an organisation has agreed to adopt. Points are assigned to each degree of a compensable factor, such a responsibility.

19.9.3 JOB HIERARCHY :

The points assigned to all compensable factors are aggregated. The total points scored will help establish the hierarchy of job worth, starting from the highest point total to the lowest point total.

19.9.4 PAY SURVEYS :

Job hierarchy being established, the next step is to establish pay differentials. Before fixing wage and salary differentials, prevailing wage and salary rates in the labour market need to be ascertained. Hence the relevance of pay surveys.

One way of collecting pay details is to conduct a survey. This requires that a sample of key jobs and a sample of companies need to be selected. Questionnaires could be mailed to select companies, requesting them to furnish pay details relating to key jobs. Information can also be collected over the telephone.

There are also other sources of collecting pay details. Labour departments of the government, trade unions, and professional bodies, and consulting firms (See Exhibit 19.9.2) provide copious amount of information about the prevailing wage and salary rates.

Business magazines also carry data on salaries prevailing in different industries. Business Today, dated September 12, 2004, for example, carried a story on salary raises from 2003 to 2004 in different industries, as shown in Table 19.9.2. The magazine reported that in high-growth and high-attrition industries such as IT, IT enabled services, telecom, and banking and financial services have registered highest increase in salaries. An increase in salaries translates into a corresponding increase in discretionary spending.

Table 19.9.2 - RAISING SALARIES

	2003	*(Increase in per cent) 2004*
IT	15	17
ITES	23	26
Telecom (Services)	10	12
Insurance	23	25
Banking (Retail)	12	15
Manufacturing	6	7
Pharma	20	22

Source : Business Today 2, 2004, p.46.

Job evaluation helps establish job hierarchy. Through surveys, the rate for key jobs in the labour market is also known. The next logical step is to determine pay structures.

19.9.5 PRICING JOBS :

In pricing jobs, the job evaluation worth is matched with the labour-market worth. Two activities need to be performed : (i) establishing the appropriate pay level for each job, and (ii) grouping the different pay levels into pay grades.

19.10 CHALLENGES OF REMUNERATION / COMPENSATION :

People who administer wage and salary face challenges which often necessitate adjustments to a remuneration plan. The more important of the challenges are skill-based pay, salary reviews, pay secrecy, comparable worth, employee participation, eliticism or egalitarianism, below market or above market rates, and marketing versus non-marketing rewards (See Fig. 19.9.2)

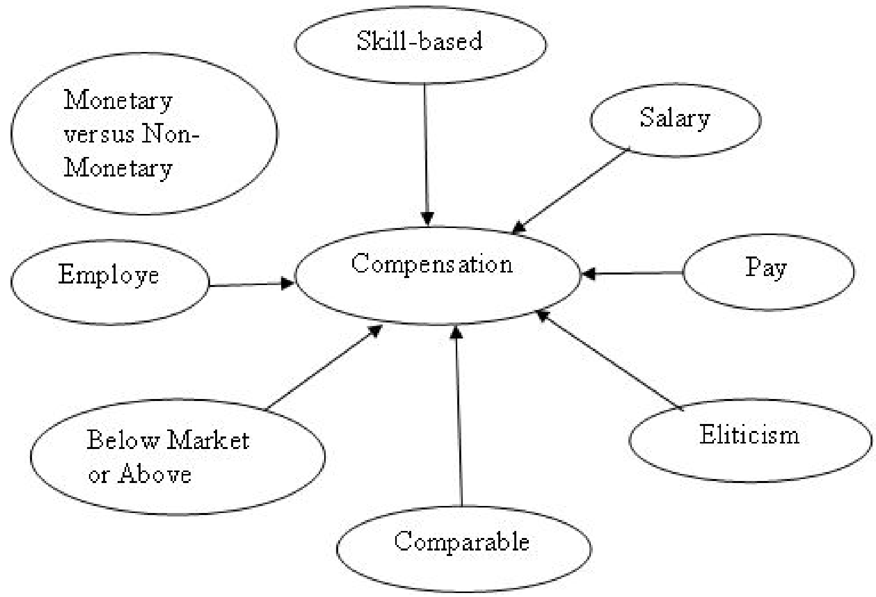

Fig. 19.9.2 Challenges of Remuneration/Compensation

19.10.1SKILL-BASED PAY :

In the traditional job-based pay, employees are paid on the bases of job they do. In the skill-based system, workers are paid on the basis of number of jobs they are capable of doing, or on the depth of their knowledge. The purpose of this system is to motivate employees to acquire additional skills so that they become more useful to the organisation. Table 19.10.3 compares skill-based pay with job-based remuneration.

Table 19.10.3 - Skill-based Pay and Job-based Pay Compared

Factors	Job-based	Skill-based
Pay structure	Based on job performance	Based on ability to perform
Employer's focus	Job carriers wage; Employee linked	Employee carries wage; Employee linked to skills.
Employee focus	Job promotion to earn greater pay	Skill acquisition to earn greater pay
Procedures required	Assess job content; Value jobs	Assess skills, Value skills
Advantages	Pay based on value of work performed	Flexibility, Reduced workforce
Disadvantages	Potential personnel bureaucracy; Inflexibility.	Potential personnel bureau-cracies; Cost controls.

Source : Raymond A. Stone, Human Resource Management, John Wiley & Sons, 1995.

Skill-based pay systems work well when the following conditions exist :

1. A supportive HRM philosophy underpins all employment activities. Such a philosophy is characterised by mutual trust and the conviction that employees have the ability and motivation to perform well.
2. Other programmes such as profit sharing, participative management, empowerment, and job enrichment complement the skill-based pay system.
3. Technology and organisational structure change frequently.
4. There are opportunities to learn new skills.
5. Employee turnover is relatively high.
6. Workers value teamwork and opportunity to participate.

19.10.2 PAY REVIEWS :

Pay, once determined, should not remain constant. It must be reviewed and changed often, but how often becomes a relevant question. Pay reviews may be made on predetermined dates, anniversary dates or there could be flexible reviews. In the fixed-date reviews, wages and salaries of all employees are reviewed and raised on a specified date each year. In the anniversary-date review, salaries may be reviewed at twelve-month intervals from the date of the employee's anniversary date of hire. Using variable timing ensures flexibility. In addition, high-performing employees, who are low on their salary ranges, can be rewarded more frequently.

In organised industrial establishments, pay review take place once in three years. Managements enter into wage and salary agreements with labour unions and the agreements will be valid for three years. Pay negotiations will take place on the expiry of the three-year period and new records are signed after conclusion of the talks.

In government department, pay revisions take place once in ten or fifteen years. Revisions will depend on the recommendations of the Pay Commission.

19.10.3 PAY SECRECY :

The process by which a remuneration plan is designed and administered is critical for any organisation. One challenge facing HRM department executives the availability of information about remuneration to employees. The tendency among most firms is to maintain pay secrecy as this would help avoid pay comparisons likely to be made by employees.

'Just how much and what types of information about pay should be provided to employees' is a question that troubles HR managers. This is a difficult question to answer. Much has been written about the effects of pay secrecy on employee behaviours and attitudes.

Firms in the organised sector and public sector enterprises disclose full information about wages and salaries. Similarly, most union contracts spell out wages and grades of pay. As stated earlier, most firms, particularly family-controlled organisations till towards maintaining pay secrecy.

The goals of achieving equity and employee satisfaction would seem to call for telling employees about pay policies and levels. For merit pay systems to have a motivating effect, an employee needs to know how efforts translate into rewards. Information about maximum and the average raises should be made available each year. Each employee should be told 'what the midpoint is' for his or her job, as well as the pay range. In addition, the organisation should explain how it arrived at the pay structure. Allowing employees to see 'where their jobs are located in the wage structure' should not create significant problems for an employer that has a well-designed job evaluation plan.

19.10.4 COMPARABLE WORTH :

One of the popular principles in employee remuneration is equal pay for equal work. In fact this principle has been the inspiration behind the enactment of the Equal Remuneration Act. Under the Act, male and female nurses are to be paid the same if their merit and seniority match, but a female nurse and a male electrician could be paid different rates.

Beyond the concept of equal wages for equal work, is the idea of comparable worth which implies that if both a nurse and an electrician receive the same number of points under a point-ranking method of job evaluation, they have to be paid the same, subject, of course, to seniority and merit differences.

Any bias in the job-evaluation process is sure to render comparable worth unworkable. Bias is bound to occur in job evaluations because of the tendency to assign higher number of points for jobs traditionally held by women.

19.10.5 EMPLOYEE PARTICIPATION :

When employees are involved in designing a remuneration plan, they exhibit little resistance in accepting it. Such a plan is much more likely to be a successful motivator than the one imposed by the management.

It is appropriate to involve employees in many phases of a reward system. For example, a wide variety of employees should serve in job evaluation committees. If a point-ranking method is adopted, it is reasonable to involve employees in identifying the compensable factors to be used and the weight to be assigned to each factor. Employees are also likely to have a good insight in identifying competitor firms that should be included in a wage survey.

There are several mechanisms for employee involvement. At the broadest level the employees can be surveyed to learn about their preferences. Employee task forces can help integrate these preferences into a system. Such groups are usually an excellent way to involve employees in any decision associated with a reward system.

These decisions to involve employees in designing or administrating a remuneration plan should not be made in haste. Employee participation is unlikely to work well unless the organisation has already established an overall philosophy of participative management, as well as a reasonable climate of organisational trust. Participation takes considerable time - if time and trust are limited, a more traditional, a top-down approach might be more appropriate.

19.11 ELITICISM VERSUS EGALITARIANISM :

Firms become egalitarian when they place most of their employees under the same remuneration plan. The plan becomes elitist when the organisations establish different remuneration schemes. In some firms only the CEO is eligible for stock options. In others, even the lowest paid workers are offered stock options. In some other companies only one category of employees is offered incentive schemes but in other all employees are covered by pay-for-performance schemes.

Egalitarianism gives organisations more flexibility to deploy employees in different areas without having to change their pay levels. It can also reduce barriers between people who need to work together. Egalitarian remuneration system are found mainly in highly competitive environments where companies frequently take business risks and try to expand their market share by continually investing in new technologies, ventures ad products.

Elitist remuneration systems are prevalent among older, well-established firms with nature products, a relatively stable market share and limited competition. Elitist pay structures tend to result in a more stable work-force because employees make more money only by moving up through the company.

Below Market versus Above Market Remuneration : Remuneration involving decision relating to below market or pay structure has two implications. First, a firm's ability to attract talent from other depends on employee's pay relative to alternative employment opportunities. Second, the choice has an important cost component. Decision to above going rate obviously adds to the cost. However in general, above market pay policies are more prevalent among larger companies in less competitive industries, such as utilities and among companies that have been performing well and have the ability to pay more. In addition, companies desirous of growing fast in a tight labour market need to pay above market rates. Unionised firms also need to pay higher rates.

Firms paying below market rates tend to be small and disorganised. Garment units, beedi rolling and incense-sticks rolling firms pay wages that do not come anywhere near current rates.

19.12 MONETARY VERSUS NON-MONETARY REWARDS :

The issue relating to monetary and non-monetary rewards has primarily tax implications. Many non-monetary rewards such as medical benefits and housing are fully or partially exempted from taxes. Employees and even employees prefer non-monetary benefits than monetary rewards.

19.13 WAGES AND SALARIES

When determining what an organization will pay for wages and salaries, it is important to understand the economic conditions of the region in which an organization is function, the volume of potential employees and the legislative requirements in place. When determining what to pay, first consideration is placement of the role organizationally which can be determined through job evaluation/classification. The second consideration is the job relevant skills and experience the applicant possesses which may impact their placement in the salary range upon hire.

1. Deciding what to pay
2. Pay increases, bonus and incentive plans
3. Approaches and techniques to determining base pay
4. Communicating wage and salary information

1. DECIDING WHAT TO PAY

They are many situations in which an HR department will be faced with deciding what to pay an employee.

- A new hire
- An existing employee due for an increase
- An existing employee moving into a new role
- A valuable employee who is considering leaving because of compensation
- Market conditions
- Scarce skill

It is important to ensure that the approach taken is guided by the compensation philosophy and is applied consistently. Ensuring that established guidelines are followed will prevent offering a compensation package so tailored to a person that the organization is jeopardized by having too heavy a financial burden or that flexible arrangements actually hinder the critical work from being completed. It takes a carefully crafted balance between the organizational needs and the individual considerations to arrive at the optimal compensation structure.

2. PAY INCREASES, BONUS AND INCENTIVE PLANS

i. Pay increases

Base pay is a fixed regular payment made to an employee in exchange for performance of the duties and responsibilities of their role. When an employee receives an increase to their base pay, it is considered a pay increase. There are various reasons and methods for determining an increase, but the common factor is that the increase changes the level of ongoing base pay.

A cost of living increase

- This is an increase offered to employees, regardless of performance, with the intention of increasing base pay for each role on the salary scale by a set percentage in order to account for increases in the cost of living. When this is offered regularly, employees can begin to see it as an entitlement.
- If cost of living increases are provided, they are generally done on an annual basis, and are given to all employees at a rate recommended by the Executive Director and approved by the Board of Directors and is contingent on the overall financial stability of the agency.
- Many small organizations are moving away from the standard cost of living increase and performing market adjustments instead.

A market adjustment following a compensation review against pre-established criteria

- Market adjustments are typically made following the receipt of market survey data. This data is usually received and evaluated towards the end of either fiscal or calendar year. Organizations will evaluate their salaries against market data and, if required, adjust base salaries for roles that are below the market. Many organizations have predetermined the percent of market they want to be paying at – i.e. a decision to pay at the median or 50^{th}percentile.

- If a position in the organization is significantly overpaid compared to market or, some companies will notify employees and not provide an increase to the employee. In this situation, the employee is considered to be "red circled" (unable to qualify for any salary increases until their salary comes in line with market)

A promotional increase

- A promotion is the advancement of an employee to a position that is evaluated at a higher grade level than the position to which the employee is currently assigned.
- An employee who is being promoted can receive a promotional increase at the time of the promotion aligned to the appropriate point in the new salary range, taking into consideration performance, qualifications, and market information.
- Promotion is usually based on availability of opportunities and preparedness of employees to advance.

A merit increase

- Merit increases are awarded to recognize an employee's contribution and to compensate them for their high level of performance.
- Performance is the key factor in awarding a merit increase and can be the factor that moves a person through the salary scale towards the midpoint or higher. Merit increases can be awarded on an employee's anniversary date following a formal performance review or at the beginning of a calendar year, depending on your compensation structure and philosophy.

ii. Bonus payments

Bonus pay is compensation over and above the amount of pay specified as wages or salary and it is only distributed as the organization is able to pay or as outlined in an employment contract. Bonus pay is used by many organizations to improve employee morale, motivation, and productivity or as a thank you to employees who achieve a significant goal. As long as bonus pay is discretionary by the employer, it is not considered to be a contract. If the employer promises a bonus, they may be legally liable to pay it out.

iii. Incentive plans

Incentive plans have not typically been popular in the nonprofit sector. However, leaders are starting to see a change in perspective regarding the use of incentive plans. Providing incentive plans, especially to senior level staff, can enable organizations to compete for talent they would otherwise have not been able to pursue.

- Incentive plans are established to reward employees for improved commitment and performance and as a means of motivation
- An incentive plan is designed to supplement base pay and fringe benefits

- A financial incentive plan may offer a percentage of base salary or a cash bonus whereas a non-financial incentive plans offer benefits such as additional paid vacations or increased professional development

3. APPROACHES AND TECHNIQUES TO DETERMINING BASE PAY

Determining base pay is directly linked to organization compensation philosophy. Having a clear understanding of what role the position plays in the organization, including the complexity of the required responsibilities and tasks, is factored into the equation along with data on market and sector comparatives. Organizations that take the time to ensure they have factored in all of the following components will be more effective in managing their competitiveness externally as well as their consistency and credibility internally.

a. Creation of job descriptions

Job descriptions define the requirements and responsibilities of a job that has been created to meet an organizational need. Job descriptions are an important element of organization's overall compensation philosophy when they are used to develop a consistent salary structure based on the relative level of duties, responsibility and qualifications of each position in the organization.

b. Conduct a job analysis

Conducting an analysis of each job by group/department to determine which tasks are being done and by who will help both in determining the most effective alignment of tasks to roles and in developing the job descriptions. This is important as compensation structures are built based on the level of skill and experience required for a certain role to perform core functions. If any inconsistencies or inefficiencies, organization should conduct a review to evaluate the appropriateness of the tasks assigned to that role. From there it can be determined if the job description and associated compensation warrants changing or not.

c. Perform job evaluation

Job evaluation is the process for assessing the relative worth of jobs within an organization. Paying fairly based on internal relative worth is called Internal Equity. A comprehensive analysis of each position's tasks, responsibilities, knowledge, and skill requirements is used to assess the value to the employer of the work performed and provide an internal ranking of the jobs. Job evaluation is a measurement of the internal relativity of the position and not the incumbent in the position. Job evaluation can be used independently, although it is usually part of a compensation system designed to provide appropriate salary ranges for all positions. This process will ensure an equitable and defensible compensation structure which compensates employees fairly for job value.

d. Review pay structures

Pay structures are helpful when standardizing an organization's compensation practices as they reflect the grouping of jobs based on relative worth. Typical pay structures can have several grades or levels, career bands, or job families with each having a minimum or maximum salary associated. These could be identified by hourly wages or annual salaries.

A number of levels may exist for a role or types of roles linked together, and for each, a dollar value would be associated. Creation of pay structures are based on internal and/or external data.

- The most basic salary structure is one in which each job class is a level with a single salary for all incumbents within the level.
    - This is seen as somewhat limited as employees (or potential employees) come with a variety of experience and skills and therefore should not all be compensated at the same rate.
- An alternative to the basic salary structure is to incorporate salary ranges for each of the different job levels.
    - Placement in the range is based on established criteria outlining experience, skill, potential and fit
    - The scale is usually created by evaluating the market comparative data however, the placement of the person in the salary range is usually based on their skill and ability against other employees in the same role
- Criteria for moving through a salary grade must align with the compensation philosophy and should be described in the Compensation Policy.

Building a matrix that identifies the hierarchy of the job family through levels as well as skills and competencies can assist in determining the appropriate placement of a position.

Example: Caseworker roles against Market data (numbers have been made up for purposes of this example)

Role Evaluation for Salary against External Data

	Salary ScaleRange	Salary ScaleMidpoint	External Survey Midpoint
Intermediate	35,550 – 43,450	39,500	40,000
Senior	39,690 – 48,510	44,100	45,000
Supervisory	47,880 – 58,520	53,200	58,500

In this example, the intermediate and senior salary midpoints are consistent with the external market data. However, the supervisory midpoint is significantly below market averages. A supervisor in this organization would have to be receiving 110% of the salary scale to be consistent with the market's average salary. In this case, the first salary the organization would want to address would be that of the supervisory staff.

Role Evaluation for Salary against Internal Data

	Salary ScaleRange	Salary ScaleMidpoint	Average Salary of Current Incumbents	Percentage of Midpoint
Intermediate	35,550 – 43,450	39,500	39,000	99%
Senior	39,690 – 48,510	44,100	43,200	98%
Supervisory	48,780 – 59,620	54,200	51,500	95%

Similarly in this example, the average salaries for both the intermediate and senior staff are close to the organization's salary midpoint, whereas the supervisory salaries are only 95% of the organization's midpoint (which remember is $5,000 less than the midpoint of all the organizations who participated in the salary survey). This type of inequity, both internally and against the market, could result in increased difficultly keeping or finding the right people.

However, there could be reasonable rational for this group being 95% of the midpoint. Differences in employee pay within the same salary range can be based on seniority, performance and different starting salaries.

e. Participate in salary surveys

Salary surveys are conducted with employers in the same labour market to determine pay levels for specific job categories. Generally wage and salary surveys are conducted either by region, sector or job classification for the purposes of comparability. By participating in salary surveys, the access to information that will allow to benchmark organization's compensation practices including wages, salaries, bonuses and benefit provisions against other organizations in your region or sector.

4. COMMUNICATING WAGE AND SALARY INFORMATION

Effective communications about compensation makes employees more aware of the value they receive from their compensation plan. When employees have a good understanding of their compensation plan they are more confident that they are being paid fairly - which results in greater motivation and retention. A compensation communication strategy should be created in alignment with the organization's HR strategy as well as be supported by management. The level of transparency is highly dependent on the organization's culture and varies for each organization. Ideally; employees should be advised of their own salary, their job grade / level, the position of their salary in the salary range for their job grade / level, the basis for progress through the range over time (seniority and / or performance), and the procedures for annual salary adjustments (if any).

Communicating total compensation information through formats such as statements, booklets, newsletters and memos provides a consistent message and allows employees to refer to the material later. Presenting compensation information through meetings, workshops and ongoing support allows interaction so individual questions and concerns can be addressed immediately. Overall, it is important to ensure employees have access to information regarding the compensation plan and that it is provided in clear and concise language. A compensation plan can also be used to attract prospective employees and therefore effective external communication is also important.

19.14 SUMMARY :

Pay level is a key attribute of compensation design and strategy. Managers and union officials devote considerable resources to developing and administering pay structures. The fact that how employees are paid has important consequences for individual, group, and organisational performance. Individual incentives, merit pay and bonuses, and gain sharing can contribute to higher performance under the right situations. Benefits do indeed have effects on employee attitudes on, retention, and perhaps job choice. Individual preferences may play a particularly important role in determining employee reactions to benefits.

19.15 KEYWORDS:

Skill-based pay: Remuneration system in which employees are paid wages on the basis of number of job skills they have acquired

Product market: The marketplace in which a final good or service is bought and sold. A product market does not include trading in raw or other intermediate materials, and instead focuses on finished goods purchased by consumers, businesses, the public sector and foreign buyers.

Compensation Plans: In network marketing, the details of how the commission of independent agents will be determined on their own and their down line's sales revenue.

Paid survey: A paid survey is used to collect quantitative information about the participants' personal and economic habits set against their particular demographic. Incentivized surveys are considered to be more likely to catch a wider and more representative range of respondents compared to unincentivised surveys.

19.16 SELF ASSESSMENT QUESTIONS :

1. Describe the role of HR Department in the Compensation Management.
2. What are challenges of HR Manager for Compensation Administration ?
3. What are the HR Strategies for Compensation Issues, Policies and Plans ?
4. What is the importance of compensation survey?
5. What is the future trend of compensation?
6. In future, the compensation policies, programmes, and practices of an organisation will revolve around introduction of newer allowances, incentives and fringe benefits. Discuss.

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LESSON - 20

INTERNATIONAL COMPENSATION MANAGEMENT

20.0 OBJECTIVE :

- After studying this lesson, the student is able to:
  - Know about the global dimension of compensation
  - Study the components of global compensation
  - Gets an information about the different elements that are required to be considered while computing expatriates/repatriates compensation
  - Give information about the emerging trends of global compensation

STRUCTURE:

20.1 Introduction

20.2 Nature of the international compensation assignments

20.3 Objectives of international compensation

20.4 Components of international compensation

20.5 International remuneration benefits and holidays

20.6 Various approaches to international compensation

20.7 International compensation policies

20.8 Expatriate system

20.9 Repatriate system

20.10 Complexity of international compensation programs

20.11 Summary

20.12 Keywords

20.13 Self Assessment Questions

20.14 Further Readings

20.1 INTRODUCTION :

Meeting the challenge of recognizing and rewarding employees in the global economy will be the cornerstone of business success in the 21st century. While most organizations have not anticipated the resources required to meet this challenge, one thing is certain that globalization does not mean applying uniform human capital solutions in a diverse world. Globalization has increased the awareness of and concern for creating internationally equitable compensation systems in many companies. The complex nature of international compensation dictates that it receives special attention from organizations operating in a multinational environment. It is crucial that organizations understand the kind of employees employed by international firms, the elements that comprise an international compensation system and the special problems associated with returning citizens on overseas or employment to their home corporations for multinational firms. Successful management of compensation and benefits requires knowledge of the employment and taxation laws, customs, environment and employment practices of many foreign countries. Also needed are familiarity with currency fluctuations and the effect of inflation on compensation and an understanding of why and when special allowances must be supplied and which allowances are necessary in what countries.

Most employers remain wedded to the traditional home-based method of expatriate pay. But it is found that 'one size fits all' approach to expatriate remuneration is not necessarily the most effective. There should be a wide gap between wages paid for comparable position in different countries due to different in economic system, political, legal and cultural environment. Therefore, HR managers spend a great deal of time developing effective compensation and benefit programs for international employees and its importance gain tremendous success.

Tremendous changes are occurring in all areas of domestic and international compensation from flexible compensation programmes adapted to regional norms to creative result sharing programmes based on individual, team, and organizational performance. As companies become increasingly global in their operations, compensation strategies must be shared across borders, throughout industries and between organizations. At no time in the past had goods, money and people crossed national borders so rapidly, in such high volume with so far reaching impact as today. Training and moving people around can no longer be a matter of lavish luxury, but will be an absolute necessity and integral part of business to support competitiveness through flexibility. Pay, working hours, vacations, fringe benefits, retirement and other HR systems has to be organized so as to be transferable on an international as well as organizational basis.

20.2 NATURE OF INTERNATIONAL COMPENSATION ASSIGNMENTS:

The nature of the assignment of the employee to a large extent determines the method of compensation. These terms of assignments are:

a) **Short-term assignment**, which may be for a relatively short period, such as the case of a feasibility study, etc. This type of assignment does not usually exceed six months. Families also do not generally accompany.

b) **Long term assignment**, if the assignment is more than six months or one year. It will usually result in employee's moving along with his family.

c) **Permanent assignment** is when an employee signs a permanent employment contract with a foreign subsidiary, the contract is usually meant for a fixed period of time of longer duration.

The compensation package vary according to these three categories generally the longer the foreign assignment is, the more the principles and local environment of the host country should determine the compensation of the employee.

The percentage can vary by industry and geographic location. Pay decisions can be broken down into two categories: pay structure and individual pay. Organizations tend to address these concerns via market pay surveys (external equity) and job evaluations (internal equity). In order to ensure that external equity and internal equity issues are addressed, human resource professionals should consider the following tools when preparing an international compensation package: (1) an international compensation management grading system that is comparable to the domestic grading system; (2) a base salary delivery process that is integrated into the home country's base pay system as well as taking local country laws into consideration; (3) an incentive and reward system that motivates employees worldwide; and (4) a performance management system that rewards employees regardless of their geographic location.

Pay levels are influenced by two factors: product market competition and labor market competition.

- Product market competition creates a threshold on labor costs and compensation. The threshold can be constrictive when the labor costs are a larger share of total costs and when demand for the product is tied to the price.

- Labor market competition highlights the fact that the organizations must research and determine what is a competitive salary for positions, especially compared to what competitors are paying for similar positions.

In order to compete for talent, many organizations will benchmark against product market and labor market competitions. Job evaluations are used to measure a position's internal worth. An effective evaluation system is based on compensable factors and the weighing scheme for each factor (based on the factor's importance to the organization). These factors include working conditions, education, experience, and job complexity. Once scores have been assigned to each of these factors, a point factor system is developed. Market pay structures can differ across borders in terms of their level and relative worth for the job. Some markets may offer lower levels of pay overall and require lower payoff for skills, education, and advancement.

In most cases, expatriate pay and benefits will be closely in sync with the compensation structure of the home country. However, this practice is slowly being replaced with alternative practices as more companies begin to implement policies that have pay differentials that are based on geographic location. The pay differentials are used to address inequities that may arise if an employee wants to consider a position in another country that may have a higher cost of living than the home country. Unfortunately, there is a drawback to this practice. It may be difficult to adjust an employee's salary downward if the cost of living decreases and/or the employee relocates to a lower-cost area.

Problems in international compensation management:

MNCs face lot of difficulties in evolving compensation package in view of the following factors:

- Economic conditions of the host country.
- Employment condition of the host country.
- Taxation laws of the host country.
- Currency fluctuation in the host country.

- Inflation situation in the host country.

The result is that expatriates cost three to four times more than the employees of the host country.

20.3 OBJECTIVES OF INTERNATIONAL COMPENSATION:

Designing and developing a better compensation package for HR professionals for the international assignments requires knowledge of taxation, employment laws, and foreign currency fluctuation by the HR professionals. Moreover, the socio-economic conditions of the country have to be taken into consideration while developing a compensation package. It is easy to develop the compensation package for the parent country national but difficult to manage the host and third country nationals. When a firm develops international compensation policies, it tries to fulfill some broad objectives:

i. The compensation policy should be in line with the structure, business needs and overall strategy of the organization.

ii. The policy should aim at attracting and retaining the best talent.

iii. It should be enhanced employee satisfaction.

iv. It should be clear in terms of understanding of the employees and also convenient to administer

The employee also has a number of objectives that he/she wishes to achieve from the compensation policy of the firm:

i. The employee expects proper compensation against competency and performance level.

ii. The employee expects substantial financial gain for own comfort and for family also.

iii. The employee expects present and future needs to be taken care of including children's education, medical protection and housing facilities.

iv. The policy should be progressive in nature.

Challenges while designing an international remuneration package:

Generally, following problems come up while designing an international remuneration package:

- Discrepancies in pay between, parent, host and third country nationals
- Need to vary compensation packages depending on employee's stage of life and customize it accordingly (e.g. young children, children in college etc)
- Remuneration issues related to re entry into parent-country organization or home country.
- Remuneration issues to deal with changes in international business environment

20.4 COMPONENTS OF INTERNATIONAL COMPENSATION:

When creating a compensation system for international employees, one must take basic components into consideration: (monetary or non-monetary rewards/package) including base pay, benefits, allowances, incentives, tax reliefs and long term benefits or stock benefits that valued by employee's in accordance with their relative contributions to performance towards achieving the desired goal of an organization.

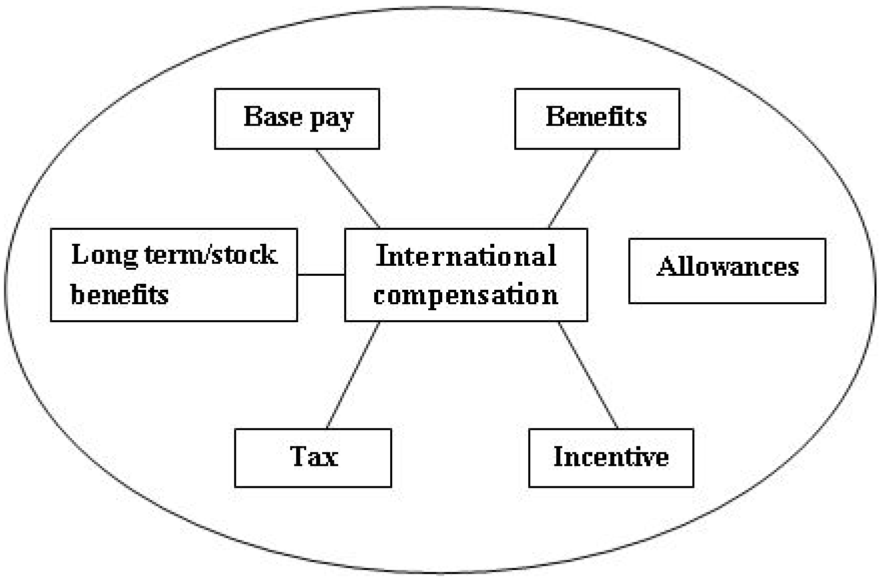


Fig. 20.4.1 Components of International Compensation

20.4.1 BASIC PAY:

Basic pay is the amount of money that an expatriate normally receives in the home country. It is finally determined after establishing consistent compensation measure between countries that builds credibility both at home and abroad. Some multinational companies conduct their own local annual compensation survey which covers all forms of compensation including cash, short and long term incentives, retirement plans, medical benefits and perquisites. The base pay also serves as the benchmark against which bonuses and benefits are calculated. Base pay may be paid in the currency or home or host country.

There are various methods for setting base the pay U.S. companies use one of the three methods to calculate expatriates, base pay.

a) Home country based method.

b) Host country based method.

c) Headquarters based method.

a) **The home country based method** is often most appropriate for expatriates. The market or going rate of pay for a comparable job in the home country is normally used for setting this rate. The assignments re short in duration and local nationals performing comparable jobs receive substantially higher pay.

b) **The host country based method** compensation is based on the host country's pay scale and is suitable when assignments are of long duration. The expatriate's base pay will be competitive with other employees base pay in the host country rather than their counterparts at home.

c) **The headquarters based method** compensates all employees according to the pay scales used at the headquarters. This method is suitable for expatriate who move from one foreign assignment to another and rarely work in their home countries.

20.4.2 BENEFITS:

These constitute a major element of remuneration of a regular employee. About one third of the compensation is benefits. In case of expatriates it can be more. Most US-based MNCs include expatriate managers in their home-office benefits programme at no additional cost to expats. If the host country requires expats to contribute to their social security programme, the MNC typically picks up the tab. Fortunately; several international agreements between countries recently have eliminated such dual coverage and expenses.

Additionally, MNCs often provide expatriates with extra vacation and with special leaves. The MNC typically will pay the airfare for expats and their families to make an annual visit-home, for emergency leave and for expenses when a relative in the home country is ill or dies.

a) **Housing**: It covers a wide range of arrangements. Some companies provide with a residence during the assignment and pay all associated expenses. Others deal a predetermined housing allowance each month and let expatriates arrange their own residence. Additionally some organizations help those going on assignments with the sale or lease of the house they are leaving behind. Costs of housing expatriates around the world can vary dramatically. Host-country housing costs are often more expensive than at home for US expatriates.

b) **Utilities**: Some companies provide air conditioners, bottled gas, bottled water, electricity, telephone and telephone call expenses.

c) **Car**-Car or Chauffeur driven car with parking facilities are provided by some organizations befitting the status or requirements of security of the employee.

d) **Helping hands** like servants, gardeners and security guards are provided by some organizations either representing affluence or power or status or all of them.

e) **Club subscriptions** are also part of benefits of expatriates. The club memberships and club fees along with entertainment power is also given by some. The club may vary from recreational/ social clubs to sports club etc.

f) **Educational** benefits are another integral part of the compensation package. These expenses cover costs such as tuition, enrolment fees, books, supplies, and transportation, room, board and school uniforms. In some cases, expenses to attend post-secondary schools are also provided.

20.4.3 ALLOWANCES:

Allowances are expensive features of expatriate compensation package. Some of the allowances are given below:

a) Cost of Living Allowance (COLA): It involves payment to compensate for difference between home country and foreign countries, especially inflation differences. It is a payment for difference between the home country and the overseas assignments. These allowances are designed to provide the expatriates with some standard of living that he or she enjoyed in the home country.

b) Relocation Allowance: It involves moving, shipping and storage charges that are associated with personal furniture, clothing, and other items that the expatriate and his or her family are (or are not) taking to the new assignment. It also includes temporary living allowance. Related expenses also may include cars and club memberships in the host country, although these perks commonly are provided only to senior-level expats.

c) Hardship Allowance: Hardship allowances are given to expatriates to work in hazardous area with poor quality of life. Some of the difficulties in the host country could be as follows:

- Excessive hot/cold climate
- Health hazard
- Poor communication
- Isolation
- Language difficulties
- Scarcities of food
- Political risks
- Force-majeure (floor, typhoons, earthquakes, tsunamis, etc)
- Regular possibility of theft, kidnapping

Those, who are posted in Africa, middle-east, are given hardship premium. That could be in shape of a lump sum pay or a percentage (15 to 50%) of base pay.

d) Separation Allowance – When family is not allowed to accompany, this allowance is given by some organizations.

e) Clothing Allowance – special in extremely cold areas.

f) Added Responsibility Allowance or Status Allowance.

g) Home Leave Allowance – Trips back to home country each year to renew family and business ties.

h) Spouse Assistance Allowance – To make up for spouse's loss of income.

20.4.4 INCENTIVES:

In recent years some MNCs have also been designing special incentive programmes for keeping expatriates motivated. Most companies giving such incentives are following the lump sum premium approach paid only at the time of acceptance of assignment. The payment retains its motivational value and cost to company is less as there is only one payment with no future financial commitment. This is also because incentive is a separate payment distinguishable from regular pay and is more readily available for spending or saving.

20.4.5 TAX RELIEF:

Taxation causes most concern to MNCs. Therefore, they adopt one of the following approaches to give relief to the expatriates.

a) Tax-equalization-Organisations withhold an amount equal to home country tax-obligation of expatriates and pay all taxes in the host country.

b) Tax protection-The employees pay up to the amount of taxes he/she would pay on the compensation package in the home country. In that event, the employer is gainer, if the taxes in foreign country are less than home country.

c) Ad hoc approach-Each expatriate is handled differently on taxation issue and tax relief is given depending on negotiation.

d) Laissez-faire-The expatriate is left on his/her own to pay the taxes because the compensation package consists of tax element also.

Tax equalization is the most commonly practiced tax relief policy of MNCs.

20.4.6 LONG TERM BENEFITS OR STOCK BENEFITS:

The most common long term benefits offered to employees of MNCs are Employee Stock Option Schemes (ESOS). Traditionally ESOS were used as means to reward top management or key people of the MNCs. Some of the commonly used stock option schemes are:

a) Employee Stock Option Schemes (ESOS) – a certain number of shares are reserved for purchase and issuance to key employees. Such shares serve as incentive for employees to build long term value for the company.

b) Restricted Stock Unit (RSU) – This is a plan established by a company, wherein units of stocks are provided with restrictions on when they can be exercised. It is usually issued as partial compensation for employees. The restrictions generally lifts in 3-5 years when the stock vests.

c) Employee Stock Option Plan (ESOP)–This is a plan wherein the company sells shares to its employees usually, at a discount. Importantly, the company deducts the purchase price of these shares every month from the employee’s salary.

Hence, the primary objective for providing stock options is to reward and improve employee’s performance and / or attract / retain critical talent in the organization.

20.5 INTERNATIONAL REMUNERATION BENEFITS:

a.	Housing:	-Housing allowance
		-Free accommodation
b.	Utilities:	-A/C, Bottled-gas, water
		-Electricity, telephone-calls etc.
c.	Car	-A common perk for either status or security reason
d.	Servant/Security-guards	-Traditional perk
	Security-guards	-Represents affluence, Power Status
		-For security reasons
e.	Club-subscription	-Club fee
		-Sports club fee
f.	Education expenses	
g.	Social security	-Pension schemes
	Arrangement	-Health insurance

For many international firms, expatriate assignments are likely to increase in distance, number and duration over an employee's career and more and more firms create cadres of permanent international assignees – called 'globals' by some firms, the inherent complexity and dynamism of culturally embedded and politically volatile national tax and pension processes promise to tax the resources, time and attention of international human resource managers for the foreseeable future. Seamless networks of global firms, their specialists consultants and local and regional public and private interest are a goal, not yet a reality.

International remuneration holidays:

1.	Annual Leave	-25-30 working days.
2.	Public Holiday	-Host country practices
		-Expatriate country holidays in addition.
3.	Home Holidays	-Company pays for expatriate and his family to fly back home, at least once a year.
		-Location affects frequencies of Home-Leave – Extreme hardship, separation from family, etc.
		-Marital status affect home trip.
4.	Rest and Recuperation Holidays	

20.6 VARIOUS APPROACHES TO INTERNATIONAL COMPENSATION:

The approaches in the area of international compensation are:-

20.6.1 The budget approach:

This system takes in all costs incurred by employees in both countries (the home country and the host country). These costs and the effect of the local tax system, form the basis on which employee's income is calculated. The system is extremely expensive to keep up there are many adjustments which need to be made, notably in high inflation countries. This method used to be popular in the colonial era, which probably explains why it is only used by a few large paternalistic British companies. An assignment from Britain to India will, for example, result in lower expenses for clothing, food and other fixed or variable private expenditure. These costs are meticulously compared and totaled. Admittedly, account is also taken of the employee's on-going expenses in the home country.

This system has been subject to criticism from expatriates. The fact that the employer determines what items will and will not be included in the budget is often seen as paternalistic. Moreover, once expatriates know what items are included in the budget they will certainly try to get other (expensive) items on the list. An added drawback is that the system may well stir up ill feeling among host-country nationals, when 'luxury' goods such as imported cheese and whisky are considered as basic essentials for the expatriate employees.

20.6.2 The going rate approach:

Under the going rate system, the expatriate is paid according to standards in the host country. This prevents the situation where junior staffs are paid substantially higher salary than the expatriate, who is compensated in conformity with the standards of income in the parent country. The approach relies on survey comparison of local nationals with expatriates. Base pay and benefits may be supplemented by additional payment for low pay countries. The going-rate system is mostly used for assignments to countries with clearly higher compensation levels. The fact that the host country could, at the same time, have lower levels of perquisites and benefits could be a reason for an expatriate to insist on maintaining the home-country package for this part of the salary. Companies are generally willing to accommodate this requirement. Again, the base salary is usually increased by various allowances to compensate for extra housing costs, international schools and family visits.

The disadvantages of going rate approach are that 1. It has variation between assignments for same level of employees, 2. It has variation between expatriate of the same nationality in different countries and it has potential re-entry problem.

But is has many advantages also 1. It ensures equality with local nationals, 2. It is simple, 3. It identifies with host countries and 4. It ensures equity amongst different nationals.

20.6.3 The balance sheet or home country approach:

The premise that underlines the balance sheet approach is that the same net sum must be available in both the countries. In this context, 'net' does not mean net survey after taxes and social security contributions. It means the freely disposable income. The idea is that spending power must be identical in both the country. Consequently, allowances will have to be made for cost of living, housing, and generally accepted spending patterns.

The balance sheet approach to international compensation is a system designed to equalize the purchasing power of employees at comparable position levels leaving abroad and in the home country and to provide incentives to offset quantitative differences between assignment locations. The key assumption of this approach is that foreign assignees should not suffer a material loss due to their transport and this is accomplished through the utilization of what is generally referred to as balance sheet approach.

The objectives of balance sheet approach are:

- To ensure mobility of people to global assignment as cost effectively as feasible.
- To ensure that expatriate neither gains nor loses financially.
- Minimize adjustments required of expatriates and their dependents.

None of these objectives link compensation with performance.

Generally, four major categories of outlays incurred by expatriates are considered in this approach. They are:

(a) Goods and services – Food, clothing, household furniture, recreation, transportation, medical care, etc.

(b) Housing – A major cost.

(c) Income tax – Whether of parent countries or host countries?

(d) Results – Contributions to savings, payments for benefits, pension contributions, investments, educational expenses, etc.

Therefore, the Balance Sheet approach has the following simple salient features:

- Basic objective is maintenance of home-country living standard, plus financial inducement

Home-country pay and benefits are the foundations of this approach

Adjustments to home package to balance additional expenditure in host country

Financial incentives (expatriate/hardship premium) added to make the package attractive

Most common system in usage by multinational firms.

Critical Assessment of the balance sheet approach

Some of the disadvantages of the Balance Sheet approach are that – 1. It can result in great disparity between expatriate of different national and between expatriates of local nationals, 2. At times, it can be quite complex to administer.

But, its advantages are many more. Some of them are as follows – 1. It ensures equity between assignments, 2. It ensures equity between expatriates of same nationality, 3. It facilitates expatriate's re-entry, 4. It is easy to communicate to the employees and 5. The expatriate is guaranteed his/her home-country spending power.

Alternatives to balance sheet approach

The balance sheet approach was refined in the 1960s and 1970s when most expatriates were technical employees of US oil companies. But the business environment and the reasons for expatriate assignments have changed since then. Consequently, many employers are exploring changes. Negotiation simply means the employer and employee find a mutually agreeable package. This approach is most common in smaller firms with many expatriates. The arrangements tend to be relatively costly, create comparability problems when other people are asked to locate overseas and need to be renegotiated with each transfer.

Another alternative localization, ties salary to the host (local) country salary scales and provides some cost of living allowances for taxes, housing and dependents. The allowances tend to be similar to those under the balance sheet, but the salary can vary. While the balance sheet approach ties salary to the home country, the modified balance sheet home country, the modified balance sheet ties salary to a region. Another common modification is to decrease allowances over time. The logic is that the longer the employee is in the host country, the closer the standard of living should come to that of a local employee. The main purpose of the modified balance sheet seems to be to reduce costs; it pays little attention to performance, ensuring fairness, or satisfying preferences of organization's expats.

20.6.4 Lump sum/Cafeteria approach:

The lump sum/cafeteria approach offers expats more choices. This approach sets salaries according to home-country system and simply offers employees lump sums of money to offset differences in standards of living. A recent survey of these different approaches shows that the balance sheet is by far the most commonly used (68%). There is little evidence that companies have developed a truly international pay strategy for their global employees.

20.6.5 Regional approach:

In this approach, expatriates are paid working in their local regions. This approach can reduce compensation costs, while providing equitable compensation to all employees. However, an assumption of small economic and cultural differences within regions may prove to be false in many cases.

20.6.6 Hybrid approach:

This approach is blending elements from both the home-country and host-country approaches. These systems are highly complex and difficult to administer. They are used with the purpose of creating a workforce where all international expatriates are paid as they were from the same nationality. Nevertheless, this type of approach does not involve local markets and therefore these systems are considered unfair for local staff.

20.7 INTERNATIONAL COMPENSATION POLICIES:

International compensation policies generally follow three alternatives:

- **A fixed value in all countries**. This means, for example, that the same net income or personal expense allowance is paid in all countries, or that the make and type of the car is the same everywhere.

- **A relative value in all countries**. This means that the benefit granted depends on other values. For example, all commitments may be defined in terms of fixed income.

- **A relative market position in all countries**. This means that the organization will take a relative position in all countries. It may, for example, opt for salary positions, which would be labeled as market average.

It is of course essential, in taking such policy decisions, that jobs are compared which are similar in terms of responsibilities. In evaluation of job size, and thus the salary, several criteria may be used.

- Complexity of markets.
- Number of product, market combinations.
- Patent of international distribution.
- Technological level.
- Branch of industry.
- Number of management areas to be administered.
- Extent to which organisations are independent.
- Size of the company in terms of turnover and workforce.

On the basis of these criteria, international companies can develop a global compensation policy.

Diversity marries consistency in global compensation:

Managing global compensation is a different ball game altogether. The laws and rules keep changing from country to country. What works wonders for employees in India may prove to be a total failure in Japan. Therefore, if you stick to a universal formula it might fall flat. Every country has a legacy to follow in compensation practices; an organization must leave space for such geographical idiosyncrasies. For example, in Scandinavian countries, there is a high level of social benefits. The UK provides company cars to a very wide population. In German company pension plans, employees require ten years in-post for vesting purposes. In Hungary, western reward practices are popular, while Poland is more conservative in its approach. Pay levels are low in India, Borneo and the Philippines, but high in Hong Kong and Singapore. In China, Like in India, housing is sometimes provided as part of the total reward package. In Malaysia, companies have a 48-hour week, but Singapore is closer to 42-44 hours per week. In Japan, promotions reflect age and service As Latin and South Africa have very high inflation zones, pay raises in accordance with these, sometimes touching 35%. In countries like Australia, on the other hand, increments vary between 12% to 15%. Depending on their cultural background, employees of different countries also perceive criteria or pay systems differently.

20.8 EXPATRIATE SYSTEMS:

Expatriate pay system affects competitive advantage, customer satisfaction, quality, or other performance concerns. It does emphasize maintaining employee purchasing power and minimizing disruptions and inequalities. But the lack of attention to improving performance or ensuring that the expatriate assignment is consistent with organization objectives is glaring. Expatriate compensation systems are forever trying to be like Goldilocks's porridge: not too high, no too low, but just right. The expatriate pay must be sufficient to encourage the employee to take the assignment yet not so attractive that local nationals will feel unfairly treated or that the expatriate will refuse any future reassignments.

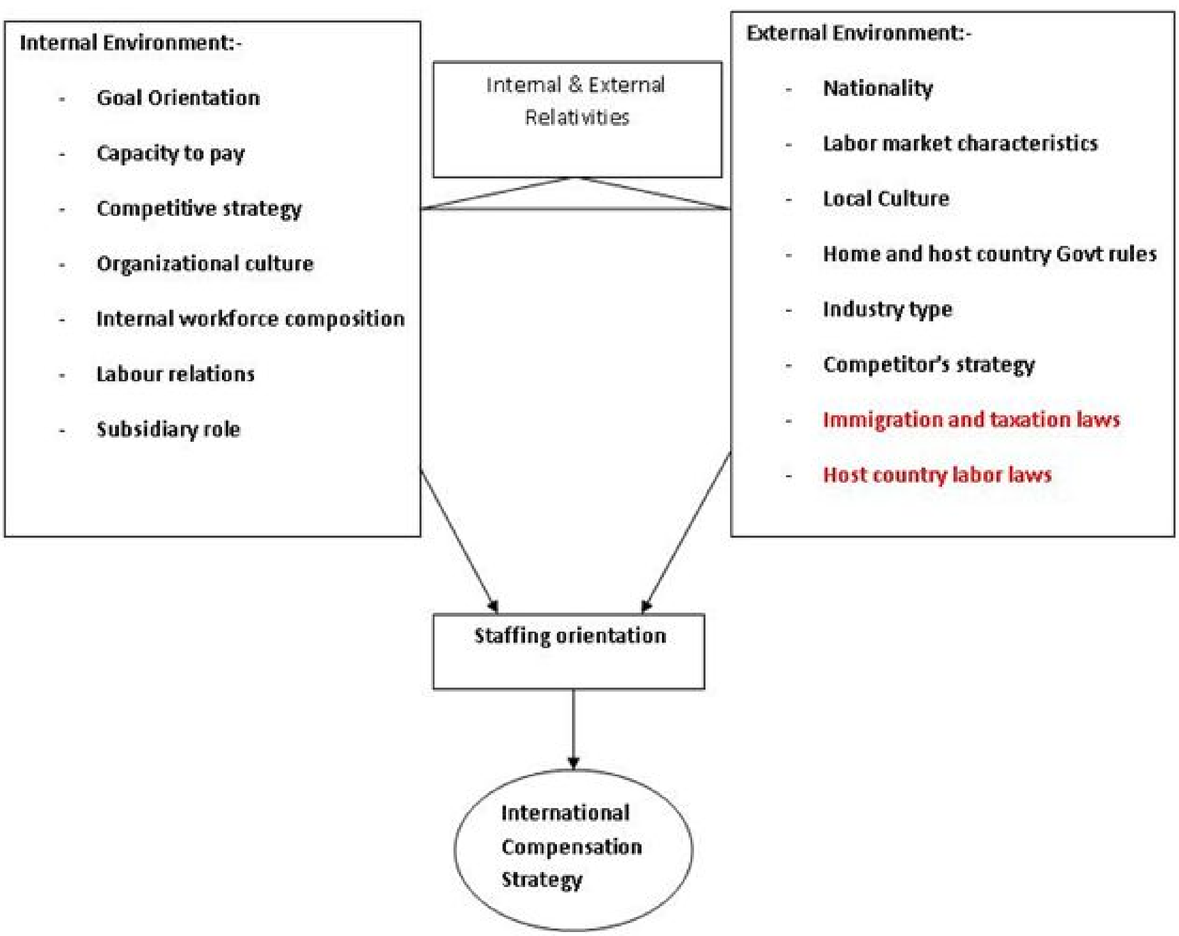
As the global guide points out one difficulty with borderless pay is that base pay levels and the other components depend too much on differences in each nation's laws and customs about managerial pay. Nevertheless, perhaps the strongest pressure to harmonize managerial pay systems is that some managers in globalizing companies are no longer expatriates from their home countries but are becoming global managers running global business.

Focusing on expatriate compensation may blind companies to the issue of adequate rewards for employees who are seeking global career opportunities. Ignoring such employees causes them to focus only on the local operations and pay less attention to the broader goals of the global firm. It is naïve to expect commitments to a longer-term global strategy in which local managers have little input and receive limited benefits. Paradoxically, attempts to localize top management in subsidiaries may reinforce the gap in focus between local and global management.

20.8.1 Factors influencing international compensation

Globalization of business has probably touched HR managers more severely than any other functional head. One activity that receives considerable attention of an International HR manager is designing attractive remuneration packages for the expatriate. Expatriate compensation depends on internal and external factors which influence the international compensation.

Fig. 20.8.1 Factors influencing international Compensation



20.8.2 Objectives while designing expat pay packages:

Any expatriate remuneration package needs to be designed to achieve the following objectives:-

- Attract employees who are qualified and interested in international assignments.
- Facilitate movement of expats from one subsidiary to another, from home country to subsidiaries and from subsidiaries back to the home country
- Provide a consistent and reasonable relationship between pay levels of employees at head quarters, domestic affiliates and foreign subsidiaries.
- Be cost effective

20.8.3 Terms and conditions for expatriate employees

Some of the terms and conditions decided by management for expatriate employees sent abroad for assignments/projects are:

❖ Period of posting.

❖ Alone/family

❖ Pay and allowances:

  - Basic salary – to be paid in India or abroad to be decided.
  - Cost of living allowance or DA is not paid as this is not applicable in India.
  - Subsistence allowance abroad varies for countries.
  - Local transportation a per local assignment management in host country.
  - Non-family station allowance to be paid in India
  - Children allowance up to 2 children either in India or abroad if accompanies.

❖ Medical facilities during posting abroad:

  - Company to contribute to social security scheme of country at site.
  - For members left in India as per existing practice.

❖ Housing :

  - Free furnished accommodation at site, etc.
  - Family in India to continue to get family house\house rent allowance.

❖ Winter clothing/outfit allowance in lump sum (half in foreign currency to be paid).

❖ Transfer grant equal to one month's salary:

  - Not if family remains in India.

❖ Travel to and fro:

- Air ticket, Visa, inoculation fees, any taxes at port of embarkation.
- Baggage allowance for 25 kg. Over and above given by airlines.

❖ Joining time before leaving.

❖ Leave:

- As per existing rules in India.
- Leave earned abroad can be availed abroad.

❖ Home leave passage:

- After certain period served abroad (one year or four months in some companies)
- Can call his family if employee desires and he does not visit home.
- Leave availed to be debited to employee leave account.

❖ Indian payments:

- HRA, children allowance to continue.
- Facilities of remittance of savings.
- Income tax to be paid in India or abroad as per rules of organization government.

Some companies require to execute agreement with the company before proceeding overseas site for not leaving service while abroad and serve a ascertain period of time on return.

20.9 REPATRIATION SYSTEMS:

Repatriation is the activity of bringing the expatriate back to the home country. It has become more widely recognized by practitioners and academies that repatriation needs careful managing, although this increased attention is somewhat belated. It becomes a traumatic experience for some, even more than what was encountered in the foreign location. From the multinational perspective, repatriation is frequently considered as the final stage in the expatriation process but the multinational ability to attract future expatriates is effected by the manner in which it handles repatriation.

Typically, on completion of the foreign assignment, the multinational brings the expatriate back to the home country, although it should be noted that not all International assignments end with a transfer home: rather, the expatriate is reassigned to another international post.

Repatriation Process

1. **Preparation**: It involves developing plans for the future and gathering information about the new position. The firm may provide a checklist of items to be considered before the returning home or a thorough preparation of employees and family for the transfer home.

2. **Physical relocation:** It refers to removing personal effects, breaking ties with colleagues and friends, and travelling to the next posting, usually the home country. Most multinational use removal firms or relocation consultants to handle the physical relocation, both for the movement out and the return home of the employee and family, and this may be formalized in their HR policies.

3. **Transition**: It means settling into temporary accommodation where necessary, making arrangements for housing and schooling, and carrying out other administrative tasks e.g., renewing drivers license, applying for medical insurance, etc. Some companies hire relocation consultants to assist in this phase also.

4. **Readjustments:** It involves coping with reverse culture shock and career demands. The reentry phase may include a number of problems that are related directly to the repatriate's attitude about the effect that an international assignments has on future employment prospects. The lack of acceptance of repatriation programs among the survey respondents tends to illustrate the absence of organized efforts by large sophisticated multinationals to assist expatriated personnel.

One reason for this oversight may be that repatriation problems are not dramatic, or visible, or readily identifiable as expensive. However, some companies assign the expatriate a mentor. The mentor is usually in a more senior position than the expatriate, from the sending work unit, and knows the expatriate personally. A mentor should ensure that the expatriate is not forgotten when important decisions are made regarding positions, promotions and so on.

The repatriation program include

1. Preparation, physical relocation, and transition information (what the company will help with)
2. Financial and tax assistance (including benefit and tax changes, loss of overseas allowance)
3. Re-entry position and career path assistance, reverse culture shock (including family disorientation)
4. School system and children's education (including adaptation) work place changes (such as corporate culture, structure and decentralization)
5. Stress management, communication related training. Establishing networking opportunities and help in forming new social contacts.

It was found that an effective mentor is likely to alert the firms of the eminent return of the repatriate and thus affect the re-entry position, or the practice is part of a managed repatriation program.

20.10 COMPLEXITY OF INTERNATIONAL COMPENSATION PROGRAMS:

The development and implementation of international compensation programs typically pose four challenges to companies. First, successful international compensation programs further corporate interests abroad and encourage employees to take foreign assignments. Second, well-designed compensation programs minimize financial risk to employees and make their and their families' experience as pleasant as possible. Third, international compensation programs promote a smooth transition back to life upon completion of the international assignment. Repatriation is the process of making the transition from an international assignment and living abroad to a domestic assignment and living in the home country. Fourth, sound international compensation programs promote businesses' lowest-cost and differentiation strategies in foreign markets.

Compensation strategy of international firms

International compensation management differs from domestic compensation in that the former has greater perspective, scope, activities and risk exposure. A host of external factors influence compensation design of international firms (or MNE), which includes:

- Industry extent and characteristics;
- Economic condition;
- Legal and political/government environments;
- Socio-cultural characteristics;
- National cultural preferences;
- Workforce characteristics such as education levels, labour cost;
- Differences in personal income taxation systems; and
- Foreign currency exchange rates.

20.11 SUMMARY:

The objective of internal compensation manager is to stimulate performance and behavior of an individual leading to organization's success. This chapter provides a discussion of international compensation and its strategic roles. The Well-designed expatriate compensation programs support strategic initiatives by attracting and maintaining the best performers. Effective expatriate compensation programs reduce risk and promote expatriate families' comfort while they are stationed at foreign posts. The balance sheet approach minimizes financial risk to expatriates, and various incentives and allowances promote facilitate returnees. All companies as well as country environments are unique, and each must determine the compensation mix that best meets its needs. However, the inclusion of some of the following basic concepts will assist in the development of a defensible, competitive, and motivational international compensation programme.

20.12 KEY WORDS:

Home country based: The country in which a person was born and usually raised, regardless of the present country of residence and citizenship.

Host country based: A nation in which representatives or organizations of another state are present because of government invitation and/or international agreement.

Headquarters based: Headquarters is the entity at the top of a corporation that takes full responsibility for the overall success of the corporation, and ensures Corporate Governance. Corporate headquarters is a key element of a corporate structure and covers different corporate functions such as strategic planning, corporate communications, tax, legal, marketing, finance, HR, IT, Procurement (CPO).

Expatriates: An expatriate is a person temporarily or permanently residing in a country other than that of the person's upbringing. In common usage, the term is often used in the context of professionals or skilled workers sent abroad by their companies

Repatriates: It is the process of returning a person to their place of origin or citizenship to return to one's own country.

Balance sheet approach: Compensation package which equates or balances an expats purchasing power in the host country with the purchasing power in the home country. For this purpose, companies provide with additional salary. The increased salary includes adjustment for difference in taxes, housing, cost of basic goods & services.

Going rate approach: Expat compensation is linked to the salary structure in the host country

Lump sum Method: Giving a predetermined pay and letting the individual decide how to spend/save the money

Cafeteria approach: Giving an expat a series of options and letting individual decide how to spend available funds

20.13 SELF ASSESSMENT QUESTIONS:

1) Discuss about the employee compensation in the global context.

2) Elaborately explain the components of international compensation?

3) What are the various approaches of the International compensation?

4) Explain about the expatriate and repatriate compensation system?

5) Discuss the strengths and weaknesses of the following methods for establishing base pay in international contexts: home-country based pay, headquarters based pay and host-country based pay.

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