

## **Salary Management for Nonprofits: The Fine Art of Distributing Dissatisfaction Equitably**

*By Jerry Jensen*

Who gets what? Determining appropriate compensation is one of the most difficult tasks facing any manager, but it is especially difficult for those who run nonprofits. The problem is as fundamental as it is familiar--too many needs and too few resources.

Salary decisions involve much more than dollars and cents. They force management to ask basic questions about an individual's real worth to an organization. Those in turn can have profound implications for the employee's sense of self-worth. Inevitably, compensation is a highly-charged issue for everyone concerned.

Among the many factors that must be weighed are the difficulty, importance, and responsibility of a position; the employee's skills, seniority, and salary history; the demands and needs of other employees; market conditions; and the agency's financial situation.

Balancing these sometimes conflicting considerations is not a pleasant job. Many nonprofit managers, who feel uncomfortable mediating between their social mission and material concerns, would prefer to ignore the issue altogether. As a consequence, salary matters are confronted only when absolutely necessary, and not very rigorously.

But the absence of a systematic salary policy is a major impediment to productivity. It leads to unease on the part of employees, and it robs management of necessary control over what is probably the agency's biggest expenditure.

Developing an effective salary program must be an integral part of any organization's personnel policies, and those policies must reflect the particular nature of the organization and its goals. Simply put, you need to know what your agency's primary objectives are in order to determine which positions are most critical and which employees will get paid the most.

While there may be significant differences in the salary systems of public and private agencies, many of the challenges they face are the same. In general, the public sector uses a highly structured pay system with automatic

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administrative mechanisms; the private sector tends to favor systems that emphasize merit. Both approaches work, but each requires continuous attention and periodic overhauls.

**Put your basic compensation policies in writing before making decisions about anyone's pay.**

Even if your agency employs only a handful of people, it is important to think about the role you want money to play in attracting and retaining the best workers. Put your ideas down in writing as a starting point for discussion. Subsequent documents may evolve into formal policy statements, or they may simply remain in the executive director's desk for reference when specific decisions have to be checked for compliance with the intended policy.

Many smaller agencies are reluctant to formalize their policies because they fear becoming too "bureaucratic." But without well-conceived pay policies, the likely results are low morale, high turnover, and disapproval on the part of funding sources. Submitting to the discipline of formal policy writing can help you avoid these pitfalls.

The best place to start is with a general statement about how you intend your agency's pay scales to relate to those of comparable organizations. For example, "The Youngstown YMCA will pay salaries that are, on average, comparable to those paid by other YMCAs in the Midwest." Or, "The Mental Health Foundation will pay salaries to its professional staff that are competitive with the national market for their disciplines. Support staff will be paid salaries comparable to those paid by other, similar nonprofit agencies in Toledo."

In the course of developing a general salary policy, many nonprofit groups discover tacit assumptions that are hindering the agency's work. The most common such assumption is the "sacrifice syndrome," which is built into many organizations' value systems. This is the assumption that teachers, preachers, and kindred welfare workers should work for less money because their cause is noble.

There may be nothing inherently right or wrong about that premise, but it is fast becoming outmoded. Organizations that insist on offering below-average wages can expect to hire below-average workers. Most private and public sector jobs pay substantially above subsistence levels, and good people, even those with altruistic motives, usually have many employment options.

If economic conditions require your agency to offer modest wages, every effort should be made to pay competitive wages for the most critical employees. All organizations have certain key jobs without which they are doomed. If well-qualified, motivated people are not retained in those jobs, the organization will go bankrupt in spirit and purpose, if not financially. You must identify and adequately compensate at least those few critical positions.

This kind of selective wage policy accounts for the relatively high salaries paid to nurses and doctors at community clinics. It also explains why development officers at private universities, whose special skills make them highly mobile in the job market, are often much better paid than other administrative officers or faculty members.

In developing a written compensation plan, it is important to prioritize the following factors:

1. Attraction and retention of desired employees.
2. Employee confidence in and acceptance of the pay plan.
3. Client or funding source confidence in and acceptance of the pay plan.
4. Control of costs.
5. Facilitation of equitable salary adjustments.

The order of your objectives may change with circumstances. If your agency is expanding, attracting and retaining good employees may head the list. On the other hand, if a period of budget uncertainty is looming, cost control may be the top priority.

It is always important that your employees and your funding sources have confidence in the plan. If the funding source is a federal agency, acceptance may depend on a formal audit that includes an assessment of the reasonableness of your pay policies. Such audits invariably require that your approach to compensation be systematic and in keeping with accepted practices. Intuitive decision-making about salaries simply will not pass muster with most government auditors, and it may lead to contractual limitations or even withdrawal of support.

It is equally important that your employees have confidence in the plan. If they perceive that their pay is determined by whim, personality preferences, or negotiating ability, morale will suffer.

"System" is a key word in developing confidence in any salary program, but that does not mean there is no room for flexibility. You should acknowledge that you may have to deal with thorny situations. For example, a valued employee may receive another job offer, forcing you to decide whether to give more pay to keep the person. Here's one example of a policy statement dealing with this problem:

"It is recognized that some people may consider leaving for more pay, and the agency is willing to consider a salary adjustment that is equitable for other employees and commensurate with general market conditions. However, it is unlikely that the agency will be able to meet all salary offers received by its employees. They should not expect to negotiate their salaries upward by regularly soliciting better-paying jobs elsewhere."

### **Decide how salaries will be increased.**

How will salaries advance? By merit or by automatic progression? Most people prefer that their pay reflect the quality and quantity of their work. A good employee who works beside a poor employee receiving the same pay is likely to become demoralized. If this condition is prevalent, the whole organization suffers.

Government employers have been notorious for failing to deal with this problem effectively. They use automatic progression pay systems that advance individuals on a predetermined schedule, regardless of work quality or quantity. Moreover, they provide the marginal performer with job security through cumbersome procedures that all but eliminate the possibility of being fired for inadequate performance.

Does this mean that the only good pay systems are based on merit? No, because merit pay systems also have major flaws; unless they are well run, they can be just as ineffective in stimulating good performance. In deciding which of these two basic kinds of pay systems your agency should use, consider the following:

1. Not all jobs lend themselves to the recognition of good or poor performance. Trying to identify the most meritorious performance from

among a large group of people doing routine tasks is very difficult. It may also be a waste of time if differences in performance are inconsequential.

2. Merit pay requires that supervisors are well-trained, willing to make tough judgments, and capable of communicating those judgments to their subordinates. Those skills are hard to develop, but a merit system will fail without them.
3. Merit pay demands that standards be clearly established and that those standards be clearly understood by employees. Setting standards and getting them applied consistently throughout an organization is a time-consuming task that takes patience and persistence.
4. No merit system can be totally objective because human judgment is always fallible. That's why automatic pay progression, which appears to be free of management bias, has strong appeal for certain organizations, such as labor unions.
5. There is no such thing as a pure merit pay system. If there were, pay would go down as well as up with changes in performance. Even in systems that purport to be based on merit, wages are almost always affected by length of service, the organization's ability to pay, other salary levels inside and outside the organization, and cost-of-living factors.

If your agency is relatively new--less than four years old--your best salary management system is likely to be one that is based on automatic pay progression. This is because management resources in the early stages of organizational development must be applied to where the needs are most critical. Establishing a merit pay plan probably requires too much time to develop performance criteria and to make individual pay decisions. Later, when the agency has operating momentum, a transition to merit pay may enhance organizational performance. It often takes at least two or three years to develop an effective merit system that everyone in the agency understands and accepts.

The fundamental question is whether a merit system will sufficiently improve performance to justify the extra effort necessary to administer it. In most agencies it will, but there are other options. Some positions in the agency can be under a merit pay plan while others are under an automatic

plan, particularly in situations where the agency's success is determined by a few key personnel.

Other modifications are also possible, such as having an automatic-salary system that provides exceptions for the poor performer. With this method, everyone gets an increase according to a predetermined schedule, but if John or Mary Marginal doesn't deserve it, he or she is told so ahead of time and given the reasons why. This approach offers some of the administrative simplicities of automatic pay raises, but it also deals with the demoralizing effect that poor workers have on good ones when there is no difference in their pay.

Whichever method of pay progression you choose, it should be put in writing so that all employees have an opportunity to review and understand it.

### **Determine the value of each job in your agency.**

When setting up your system, it is important to separate the job from the employee. A job evaluation, which nearly always begins with a one- or two-page job description, can help define the job as separate from the particular person who currently performs the job. Remember that job evaluation and performance evaluation are not the same thing. The former focuses on the job itself; the latter on how well a particular employee does the job.

Presumably, no one knows the job better than the person doing it, so the initial drafts of job descriptions can be prepared by incumbents, if they are accustomed to expressing themselves on paper. But incumbents cannot be expected to evaluate their own jobs relative to those of others. They may make a routine clerical job sound as if it is the most important position in the organization. To avoid this bias, it is necessary for a supervisor and, if possible, a third party to edit job descriptions so that are not overblown, and so that they have consistency in form and terminology.

Typically, job descriptions cover the following areas:

1. Purpose of the job.
2. Work performed (specific tasks, responsibilities, examples of work).
3. Importance of the job relative to organizational objectives.

4. Approximate amount of time spent on each principal duty.
5. Authority of incumbent.
6. Working relationships (supervision given or received).
7. Methods or equipment used.
8. Conditions of work (physical effort, deadlines, travel, pressure).

This information may be gathered through questionnaires, interviews, or written narratives from each incumbent. Then descriptions can be combined so that superfluous distinctions are eliminated. For example, there may be 10 or more secretaries in an agency, each doing work that is slightly different; their job descriptions should be edited into two or three basic positions, such as secretary, senior secretary, and executive secretary.

Final job descriptions are the source documents for a job evaluation exercise, which is the next step in setting up a pay system. The objective of this exercise is to arrange the value of every job in the agency hierarchically, from most important to least important. Factors to be considered include working conditions, contacts with others inside and outside the organization, responsibility, amount of supervision required, consequences if mistakes are made, handling of money or confidential information, length of training required to do the job, creativity required, etc.

If your organization has no more than 25 different positions, the process of job evaluation should be relatively simple. A few people can sit down and do a very credible job of ranking all the positions, based on the written job descriptions. Identifying the top and bottom jobs should be easy enough, but in order to distinguish the 16th most important positions from the 17th most important position, you will have to study the job descriptions. For a small community development agency, the end product of the job evaluation committee's work might look something like this:

<b>Job Hierarchy</b>	<b>Job Grades</b>
1. Executive Director	Grade 5
2. Management Services Officer	
3. Government Liaison Officer	Grade 4
4. Business Liaison Officer	
5. Field Services Assistant	Grade 3

6. Community Liaison Assistant	
7. Interviewer	Grade 2
8. Secretary	
9. Clerk Typist	Grade 1
10. Receptionist	

If your agency is large--with, say, 50 or more different jobs--a more structured approach to job evaluation will be necessary. No one person will be knowledgeable enough about all the jobs to rank them accurately. Under these circumstances, the most common method of job evaluation is to break down each job into basic components that are compared to standards which have designated point values. For example, degree of responsibility might be one component, and the responsibility associated with each job might be rated on a scale of 1 to 10. The numbers for each component are tallied to give an overall point score for the job. Jobs can then be ranked in order, depending on their point scores. Objectivity in this process is achieved by having different people independently evaluate jobs according to the same point score standards and then comparing evaluations. Significant differences between evaluators are negotiated until a hierarchy is agreed upon.

**Devise a permanent structure for your pay system, including dollar values for each job.**

To come up with a salary range for each job, develop a hierarchy of jobs grouped by job grade. Job grades are not determined by grouping jobs of like function (e.g., file clerks and other clerks). Instead, jobs of similar difficulty and value are grouped into the same grade regardless of how dissimilar the functions may be. For example, executive secretaries would be in the same job grade as field interviewers if job evaluations determine that these positions are of comparable value to the organization.

Sample Salary Structure				
Grade 1		Grade 2		Grade 3
(+15%)	\$1,610	(+15%)	\$2,070	(+15%) \$2,760
Clerk Typist	\$1,400*	Interviewer	\$1,800*	Field Services Worker \$2,400*
Receptionist	\$1,400	Secretary	\$1,800	Community Liaison \$2,400
(-15%)	\$1,190	(-15%)	\$1,530	(-15%) \$2,040

\*Average salary for key job in the grade (determined by survey.)

As new jobs develop, they can be evaluated and assigned to the appropriate grade. There is no magic number of pay grades, but five to seven are usual, except in very large, diverse organizations. The purpose of grades is to facilitate the development of salary ranges for jobs of similar difficulty. Setting a salary range for each and every job in an organization could become extremely burdensome. Setting ranges for five to seven grades is a far more manageable undertaking.

The next step is to figure out the monetary value of these jobs. The basic tool for doing this is the salary survey, which is used to establish the market value of key jobs in each salary grade. (For more, see page 12.)

You don't have to conduct a salary survey for every job in your agency. If you have already grouped jobs into grades, you may only need to survey one job in each grade to come up with monetary values for all the jobs in that grade. Try to select one benchmark job in each grade, a job that can be found in many organizations and thus can be surveyed easily. Since most agencies also have at least a few unique jobs for which market data is hard to track down, their values will have to be established by comparing the difficulty of these jobs to jobs for which market data is available.

You don't have to start from scratch every time you conduct a survey. Many associations gather and publish salary data that are useful to their members. Government agencies are another good source of data that, when combined with more specific information, can be very useful. Classified ads in local newspapers and specialized publications can tell you something about the market for specific jobs. Chambers of commerce may also be a source of local wage rate information.

For health care workers, hospital councils in major metropolitan areas are worth contacting. Local college placement offices compile data on new graduates, and the College Placement Council does the same at the national level. Usually, it is best to use several sources of information to determine the monetary value of any job.

Whatever you determine the monetary value is for each key job, it should only be used as the basis for constructing a salary range for the grade in which that job is found. The average salary becomes the midpoint of the salary range for that grade. That range usually extends 15 percent above and below the midpoint, but your own spread may be somewhat wider. A sample structure is shown in the chart to the right.

With this kind of flexible structure, individual salary levels can be set. Without such a framework, it would be hard to convince your employees or an outside auditor that you administer salaries in a businesslike way.

### **Anticipate the problems you will have in everyday administration of salaries.**

Here are some of the main questions that must be answered in administering any salary program:

#### *How often should salaries be reviewed?*

Annual reviews are the norm, but reviews may be as frequent as every six months or as infrequent as every two years for executive level positions. Whatever duration you decide upon, it is important that everyone in the agency knows that a schedule exists and what that schedule is. No one should have to ask for a raise because they believe they have been forgotten.

If all salary reviews coincide with the beginning of the calendar year or your agency's fiscal year, two problems can result. First, when everyone is reviewed at the same time, the salary administrator's workload may be excessive. Second, when everyone becomes salary-conscious at the same time, they tend to make invidious comparisons. If you wish to avoid these two problems, you can stagger review dates alphabetically or according to an individual's employment anniversary date.

#### *How large and how frequent should raises be?*

Raises tend to depend on an organization's ability to pay, its relationship to the market, and its need to comply with any governmental wage guidelines. If you have decided to use a merit pay system, a simple salary planning table can be developed to assist in making equitable decisions. Such a table tells you what percentage increase to offer and when to offer it.

Merit System Salary Planning Table								
			Performance Rating					
		Salary Range	A Outstanding	B Exceeds Requirements	C Meets all Requirements	D Needs Improvement	E Marginal	
Level of Present Salary within Salary Range	4th quartile	Max.	8% after 12 months	8% after 13 months	7% after 14 months	6% after 15 months	5% after 16 months	
	3rd quartile	Mid Point	9% after 11 months	9% after 12 months	8% after 13 months	7% after 14 months	6% after 15 months	
	2nd quartile		10% after 10 months	10% after 11 months	9% after 12 months	8% after 13 months	6% after 15 months	
	1st quartile	Min.	12% after 10 months	11% after 11 months	10% after 11 months	9% after 13 months	6% after 15 months	

Here's how it works: Assume that you are considering increasing the salary of an employee who meets all the requirements of his or her job and that the person's present salary is just below the midpoint of the range. Read down column C to the second quartile row. That box tells you that the person should get a 9 percent increase 12 months after the last increase.

If the same person had been judged a marginal worker, he or she would be given only a 6 percent increase after 15 months. If that person met all the job requirements but was near the top of the salary range, he or she would receive a 7 percent raise after 14 months.

The precise figures can be changed to allow for budgetary constraints or to meet other objectives. Note, however, that the table takes into account both the time elapsed since the last increase and the actual percentage of that increase. In other words, it recognizes that time is money. A smaller increase given sooner than a larger one may mean more money in an employee's pocket.

This salary planning table also takes into account another important factor in determining the size and timing of a salary increase--how near the employee is to the top of the salary range for that particular job. It presumes

that as the person nears the top of the range, raises should be smaller and less frequent. After all, no matter how well an employee performs, the job itself is only worth so much to the agency.

Many good employees will want to continue to advance even after they have hit the top of their range. If that's the case, they should be encouraged to move up to a position with a higher salary potential.

*What should be done about the employee who "needs" a raise?*

Nearly all bosses have been approached by someone who "needs" a raise for one reason or another. When the request comes from a hard-working, conscientious employee, it is hard to say no. If the request is based on adverse personal circumstances, it is even harder. But the fact is that once need dictates pay decisions, you have lost control of the process.

Denying an increase to the newly divorced mother of three young children who finds herself faced with a big rent increase is very tough, especially when she also happens to be a good employee. But if you want an organized, equitable salary system, you must be willing to bite the bullet.

This does not mean that you have to turn into Scrooge. You may certainly help employees with their problems; just don't use your salary program to do it. Counseling, referral to another appropriate agency, personal loans (not from agency funds) are all ways to help a deserving employee who needs your assistance.

Remember that if you agree to an unscheduled salary increase for one employee, all employees have a right to expect the same consideration. And acting as arbiter of who "really" needs an increase--and when--is a very dangerous game for any manager to be playing.

*How can new employees be hired if it is necessary to pay them more than present employees?*

This is a universal dilemma. Large, mature organizations handle it with preferential promotion-from-within policies, doing most of their outside hiring only at the entry level. They can do this because they have many staff members in the pipeline ready for promotion when new opportunities come up. Young, rapidly growing organizations can't do this. Nor can they afford to adjust their entire salary structure upward every time an essential new employee comes on board.

There is no simple solution to this problem. One approach is to formalize a policy of promotion from within, but to add that outside recruitment will be necessary on occasion.

When those occasions do arise, the new person who receives premium pay must have qualifications that are obviously unavailable internally and are superior to those of others within the organization. It must also be clear that the higher salary reflects the market value of the new employee's background and skills.

Veteran employees are more likely to accept this disparity when they understand the organizational need and if they respect the special qualifications of the new employee. They will be understandably demoralized, however, if the newcomer is perceived to be no better qualified than someone already with the organization.

*What should be done about increases in the cost of living?*

Although many agencies make regular cost of living adjustments (COLAs), these increases create problems:

1. Once begun, they are expected, and come to be seen as an entitlement. Employees feel cheated if they miss a year.
2. When given across the board, they are indiscriminate, rewarding excellent workers exactly the same as poor workers.
3. All employees are not affected by the cost of living to the same degree. Factors such as age, marital status, and salary level all have an impact.
4. COLAs can skew the value of particular jobs, damaging your salary structure by overpaying some positions and underpaying others.

To avoid these problems but still deal with the realities of inflation, some organizations budget extra money for cost of living increases, but administer them selectively rather than as a blanket raise for all.. Different percentages are given different groups: perhaps 3 percent for employees earning over \$30,000 and 5 percent for those earning less. Or a flat dollar amount may be given regardless of base pay. Another option is to give a one-time, lump-sum payment, which does not increase the basic salary schedule.

### *Who should make decisions about pay?*

Committees certainly have a role in making sure that all dimensions of a particular pay decision are considered, but committees do not make the best salary decisions. After all the discussion and debate, someone has to get off the fence, and committees tend to straddle it awkwardly with compromises. Therefore, the agency's board should give an executive director broad responsibility in setting salaries, with prudent checks and balances to be sure that all board-approved policies are followed.

A small salary committee may also be appointed to advise the director and to review policies. This committee may also have authority to recommend individual merit increases. It should be comprised of people who have significant responsibility in the agency and who can make balanced judgments about organizational and employee needs. In any case, individual members must respect the absolute privacy of committee deliberations.

Involvement of supervisors in salary matters is complicated. They must be able to make rational, fair judgments and not play the role of "good cop" to the boss's "bad cop." It is not constructive to tell the people they supervise, "I tried to get you a raise, but the director vetoed it."

Of course, if your agency has a merit pay system, supervisors inevitably have input. This may be in the form of recommendations based on their evaluation of an individual employee's performance. But the best pay decisions require perspective from the top, which is something that supervisors cannot be expected to have.

### *How confidential should salary matters be?*

Employees must have confidence in your salary system, which means it must be confidential. They should know the salary ranges for their own grades and perhaps for the grades above them, and they should know who makes the decisions about their pay and how often those decisions are made.

They do not need to know what other employees earn, but you should expect that they will. If individuals choose to disclose their salaries to others, there is nothing to stop them from doing so. Management should not be in the business of revealing this sort of information unless it is required to.

*What laws must be considered in administering salaries?*

When it comes to matters of pay, it is prudent to assume that all the standard labor laws apply, rather than to look for nonprofit loopholes. Nonprofit organizations are not immune from employee lawsuits merely because they have noble missions. Such litigation is very unpleasant and very expensive.

The Fair Labor Standards Act is the most basic law with which you must be concerned. It is commonly called the Wage and Hour Law because it establishes minimum, overtime pay and child-labor standards. Establishing employee rights to overtime pay is a particularly important aspect of the law. Some employees--such as executive, administrative and professional personnel--are exempt from this overtime pay requirement. You can determine who qualifies for these exemptions by studying the act. If you deny overtime pay to an employee who has a right to it and the employee files a complaint, the Department of Labor can impose administrative or legal sanctions.

You don't have to be an attorney to understand and comply with the Wage and Hour Law. Guide to the Fair Labor Standards provides straightforward criteria for deciding which jobs in your agency are exempt from the law. You can get a copy free from your nearest Department of Labor office.

The Equal Pay Act requires that under similar working conditions, men and women be paid equally for jobs requiring equal skill, effort and responsibility. If jobs vary, be sure you know how they vary in order to justify any pay differences that exist. If your pay system is based on merit, salary differences are acceptable if you can document differences in job performances.

In addition to these two basic federal laws, there are many state and city regulations regarding salaries. Legal counsel should help you sort out those that pertain to your organization.

*How can funds be generated for regular salary increases?*

A sound compensation program includes provisions for salary increases. It is reasonable to provide for such increases in contracts or grant proposals, especially if there is evidence that salaries are systematically managed in your organization. Written policy statements regarding wages or a written job evaluation system and a resulting salary structure covering every job in your agency provide such evidence. Generally, funding agencies are

interested in the reasonableness of your salaries. They don't expect you to pay low salaries; they do expect you to have a system that recognizes and responds to the realities of the job market.

If a funder is unwilling to consider salary increases as a part of a grant, you can assume it isn't interested in your organization's financial health or longevity. That's not a good sign. If possible, look for a funding source that acknowledges the realities of running an effective organization.

Budgeting for salary increases does not require expertise in accounting or finance; calculating a simple percentage of payroll is usually all that is required. The figure may be quite modest--3 or 4 percent--and may include providing for individual increases higher than that percentage. Some employees will leave before they are eligible for a raise and their replacements may not be eligible to receive one in the current budget period. Hence, the money budgeted for former employees' raises can be used for other employees who have been with the organization for the entire budget period.

It is relatively easy to forecast individual salary increases at least a year in advance, add up the extra money required for each increase, and then compare that total with what you have budgeted. But don't budget salary increases too rigidly. Without the flexibility to meet unanticipated needs, you could lose that valued employee who is offered more money elsewhere.

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