Compensation Analyses: A Practical Understanding and Real-World Strategies

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biddle consulting group

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Agenda

- Compensation Analyses: A Historical Perspective and Why the OFCCP has to Get it Right this Time

- Money is Tight: Compensation Analyses on a Budget

- Understanding Multiple Regression (for the Stat-Phobic)
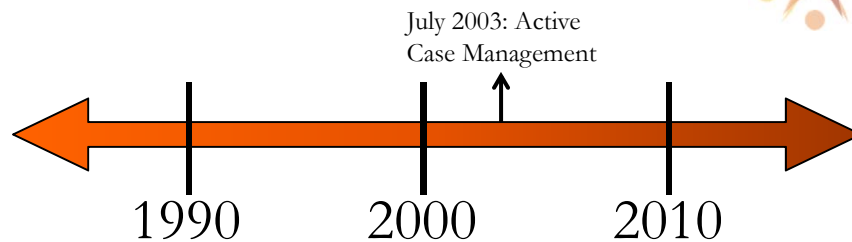
- Practical Strategies and Recommendations

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Compensation Analyses: A Historical Perspective and Why the OFCCP has to Get it Right this Time.

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The Rise of the Compensation Standards and Guidelines

July 2003: Active
Case Management

1990   2000   2010

- Dramatic reduction of Agency resources under Charles James (788 FTEs – 585 FTEs)
- Designed to focus Agency resources on issues of systemic discrimination
- Statistics drove investigations
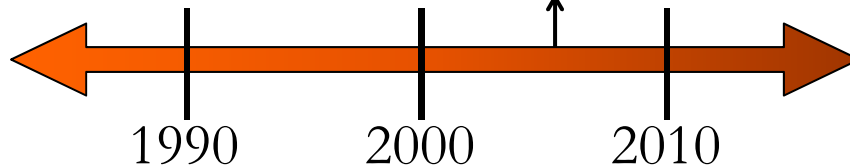- Resulted in 6+ consecutive years of record enforcement

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The Rise of the Compensation Standards and Guidelines

June 2006: Comp Standards and Guidelines - SSEGs, Regression, Anecdotal Evidence Codified

1990   2000   2010

- OFCCP realized that "litigation-worthy" analyses were necessary to successfully investigate compensation.
- Comp Standards (i.e., what the Agency will do) and Guidelines (i.e., what contractors should do) were released in 2006
- Included guidance regarding regression, SSEGs, and the need for anecdotal evidence to support statistical findings (**most** of the time)

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The Rise of the Compensation Standards and Guidelines

2006   dards   **Splat!**   Enfor

1990   2000   2010
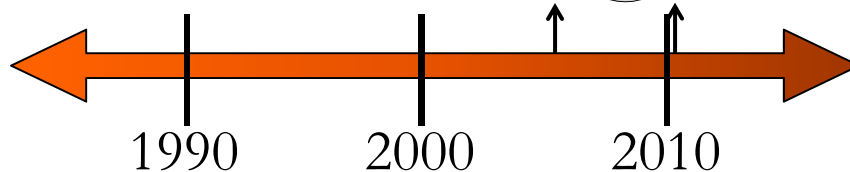
- The bar set high for compensation enforcement (is that such a bad thing?)
- Comp investigations are inherently quirky, can be very time consuming, and typically involve several stages: 1) SSEG argument, 2) Regression argument, 3) Anecdotal evidence
- On the contrary, systemic hiring investigations are relatively straightforward by comparison (and the OFCCP has a successful history of enforcement)
- **No systemic compensation-based conciliation agreements in 4+ years**

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The Fall of the Compensation Standards and Guidelines

2009/2010: Change of Administration and Significant Increase in OFCCP Budget

1990   2000   2010
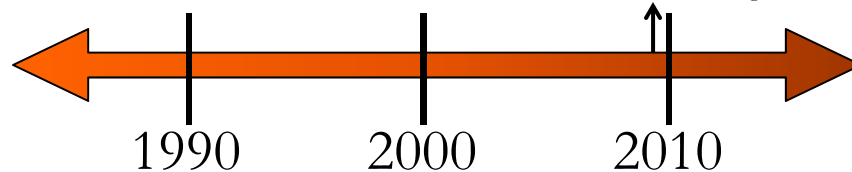
- President Obama inaugurated January 20, 2009
- January 29, 2009 – Ledbetter signed into law (Paycheck Fairness Act fails)
- January 2010: Establishment of the Equal Pay Enforcement Task Force
- Patricia Shiu becomes director of OFCCP – Former EEO litigation attorney (OFCCP is an "enforcement agency")
- OFCCP receives $20M+ budget increase and approval for 200+ more FTEs
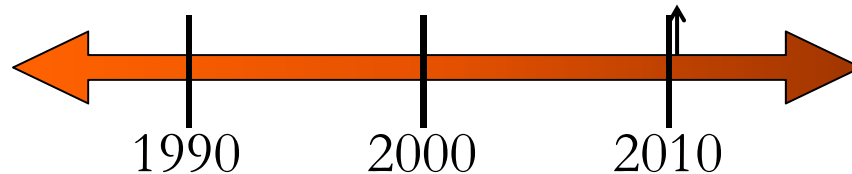- Tremendous amount of pressure to perform

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The Fall of the Compensation Standards and Guidelines

Jan 2011: Notice to Rescind Comp Standards and Guidelines

1990   2000   2010

- "Standards have limited OFCCP's ability to effectively investigate, analyze, and identify compensation discrimination"
- OFCCP wants to dramatically change enforcement by eliminating the requirement for SSEGs, regression, and anecdotal evidence . . . (which, by the way, are firmly codified in legal precedent)
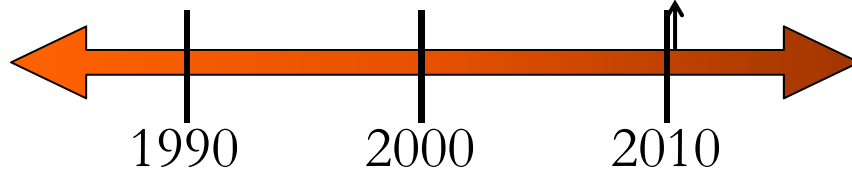
It's a Big Deal for the OFCCP . . . And They Have to Get it Right This Time!

Feb 2011: Release of OFCCP 2012 Budget Justification

1990   2000   2010

- "OFCCP is making the issue of pay equity a top priority"
- "OFCCP plans to develop and implement a web-based compensation data collection tool that would enable the agency to identify indicators of pay disparity among federal contractors"
- "The scope of the data is yet to be fully determined. Current possibilities include salary, gender, race and ethnicity data **for each employee** OR average compensation and **variances** for each group by gender, race and ethnicity"

It's a Big Deal for the OFCCP . . . And They Have to Get it Right This Time!

August 5, 2011: OFCCP submits NPRM for compensation data collection tool

1990   2000   2010

- OFCCP proposes changes to the audit scheduling letter to allow for collection of individual employee-level compensation data (still not yet codified as of today)

It's a Big Deal for the OFCCP . . . And They Have to Get it Right This Time!

February 2012: Release of OFCCP 2013 Budget Justification

1990　　　2000　　　2010

- OFCCP Outlines the Federal Contract Compliance System (FCCS), a cloud-based tool that will include:
  - Basic case and content management functionality
  - Dashboard reporting
  - **Automated data analysis**
  - **Electronic submission of AAP data and other HR reports**
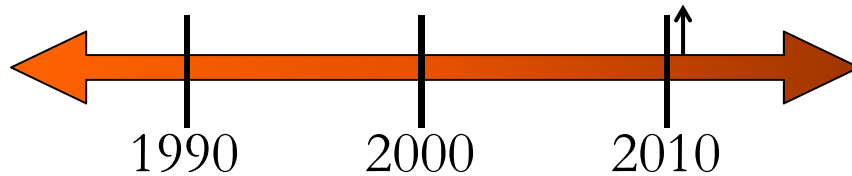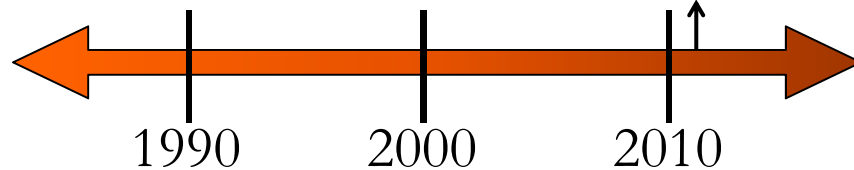 - **Integration of a compensation data collection tool**

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It's a Big Deal for the OFCCP . . . And They Have to Get it Right This Time!

February 2013: OFCCP Formally Rescinds Comp Standards and Guidelines and Releases Directive 307

1990　　　2000　　　2010

- Standards and Guidelines are no longer in effect
- Directive 307 formally replaces all previous directives on the subject of comp enforcement and broadens (dramatically) the ability of the OFCCP to investigate compensation
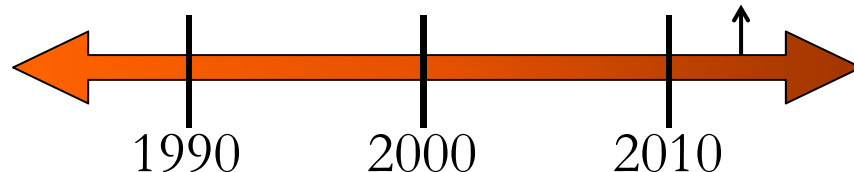- OFCCP now bringing a wide variety of enforcement and analytical strategies to bear

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It's a Big Deal for the OFCCP . . . And They Have to Get it Right This Time!

Is this EO Survey 2.0?

April 2014: President Obama signs "*Advancing Pay Equity Through Compensation Data Collection*"

1990   2000   2010
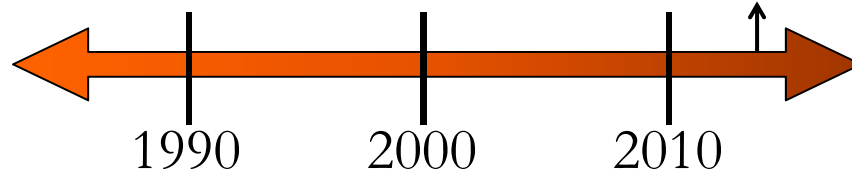
- Part of the Obama Administration's strategy to use Executive Orders to further the Whitehouse agenda
- Applies only to federal contractors and sub-contractors
- Equal Pay Task Force identified a "lack of sufficiently robust and reliable compensation data" as a key impediment to shrinking the pay gap
- Calls for proposal of a new rule, by August 8, 2014, that would require contractors/subcontractors to *submit summary-level compensation data on the pay of their employees*

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Money is Tight: Compensation Analyses on a Budget

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By Being Proactive, You Can Dramatically Reduce the Damages

- OFCCP generally begins with a "make-whole" relief calculation which typically includes:
  - Current adjustments
  - Back-pay (for two years)
  - Interest (from the beginning of the enforcement period through the signing of the conciliation agreement)
  - Benefits
- When you proactively identify problems, you have the option to just make current adjustments
- The difference in financial impact (cost) between the OFCCP finding issues v proactively finding them yourself can sometimes be 10X+

It's Nowhere Near as Expensive as You Think… And You Can Set the Budget

- Because of technological advancements, the cost for performing analyses has dropped dramatically . . . analyses can oftentimes be conducted for a fraction of what they cost just a few years ago

- Of course . . . running the analyses is just one portion of the cost, what about the cost of fixing the identified issues?

- The cost for **completely** fixing the identified issues can often dwarf the cost for running the analyses . . . but there is another option . . . allocate a **fixed amount** of available funds then address the issues in priority of legal exposure.

It's Nowhere Near as Expensive as You Think… And You Can Set the Budget

- Creating a fixed-pool of available funds has several advantages:
  - It avoids the need for a "blank-check"
  - It increases the likelihood of receiving approval for the project because now the total costs are known
  - The amount of available funds can be determined based on: 1) budgetary constraints, and 2) a company's level of risk aversion/tolerance
  - You can choose to focus on either: 1) the job titles with the largest exposure, or 2) the most egregiously under-paid employees (regardless of job title)

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It's Nowhere Near as Expensive as You Think… And You Can Set the Budget

Risk Tolerance/Aversion Continuum

Conduct No Analyses: It's Better We Don't Know

Identify and Completely Address All Problems

Extremely Risk Tolerant   **Extremely Risk Averse**

Conduct Analyses: Limited Budget to Fix Issues – Issues Will Take Many Years to Address . . . But Exposure Will be Reduced

Conduct Analyses: Moderate Budget to Fix Issues – Issues Will Take a Few Years to Address . . . But Exposure Will be Reduced

Moving in the right direction . . . but how long are you comfortable with the exposure?

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Understanding Multiple Regression (for the Stat-Phobic)

Multiple Linear Regression

Multiple Regression

Used to create a "model" to determine whether differences in compensation are due to "legitimate job-related factors" or (perhaps) an employee's gender or ethnicity.

Gender

Experience

Job Market Factors

Performance

Differences in Compensation

Tenure

Education
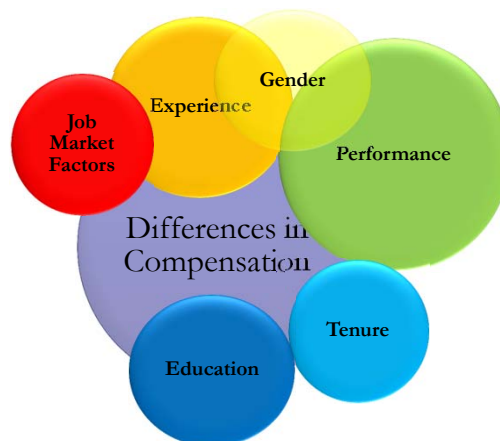
Correlation: The Precursor to Regression

Correlation Coefficient (r = .35)

Customer Service Representative

Compensation ↑

Tenure with Company →
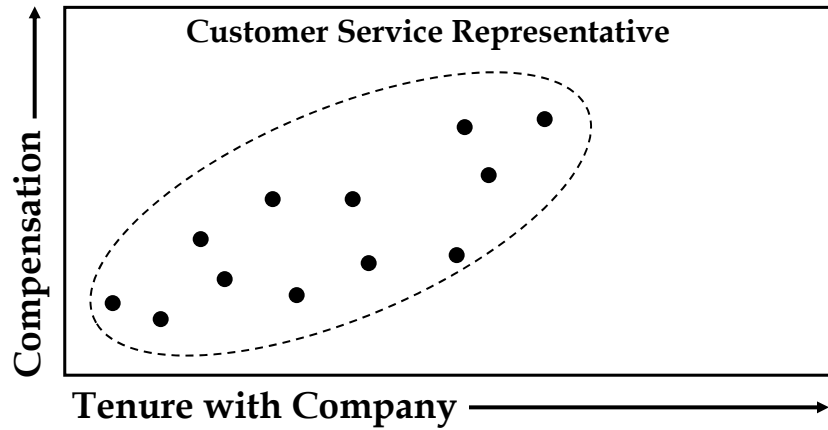
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Correlation: The Precursor to Regression

r = .35

Compensation   Tenure
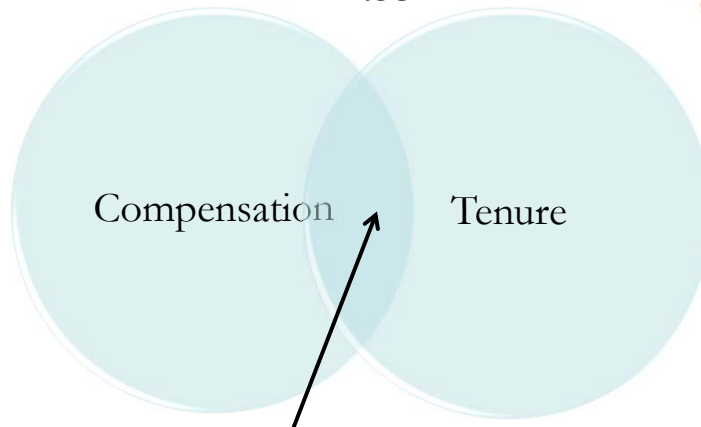
Percent of compensation explained by tenure
(r^2 = .35 x .35 = 12.3%)

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The Correlation Coefficient

Range	• Always between -1.00 and +1.00
Size	• Close to + or − 1.00: stronger the relationship • Close to 0.00: weaker the relationship • 0.00: no relationship
Direction	• Negative: variables move in the opposite direction • Positive: variables move in the same direction
Coefficient of Determination	• Square the correlation coefficient to get the percent of one variable that is accounted for by the other variable

Correlation and Multiple Regression

Customer Service Representative

$55,000

Compensation

Regression/Prediction Line

r = .35

8 years
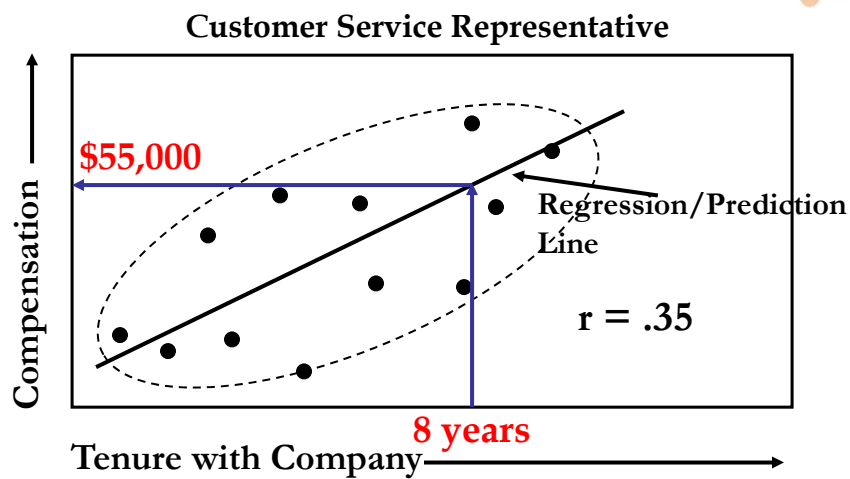
Tenure with Company

Correlation and Multiple Regression

But we have more than just the employee's tenure with the company!

Customer Service Representative

$51,000

Regression/Prediction Line

r = .28

6 years

Prior Experience

Compensation
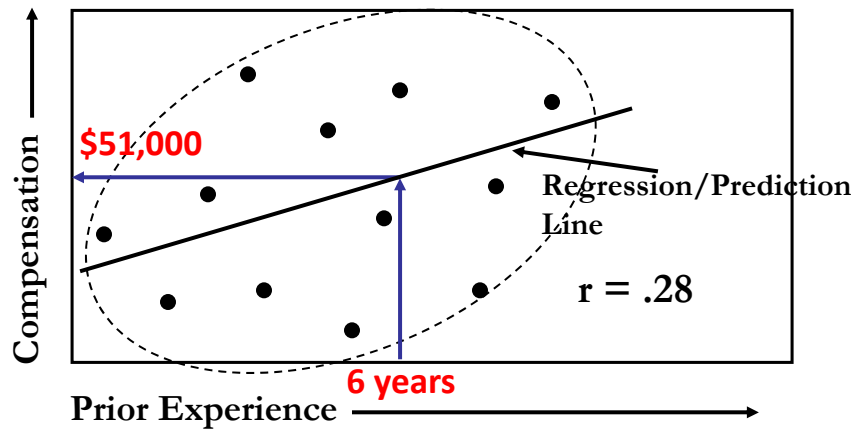
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Correlation and Multiple Regression

Don't stop there, we have more relevant data . . . What about performance appraisal score(s)!

Customer Service Representative

$47,000

Regression/Prediction Line

r = .22

Compensation

1   2   3   **3.5 Avg** 4   5

Perf. Score(s)
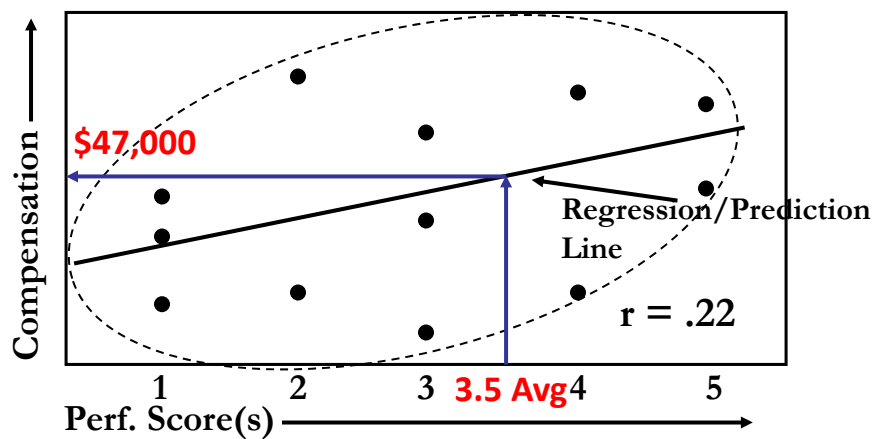
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The Regression "Model"

- All variables together become the basis for a prediction "model" known as a regression model.

- The regression model predicts a certain percentage of what makes up an employee's compensation.

$R = .67$
$R^2 = 45\%$

Prior Experience

Compensation

Tenure w Company

Perf. Score
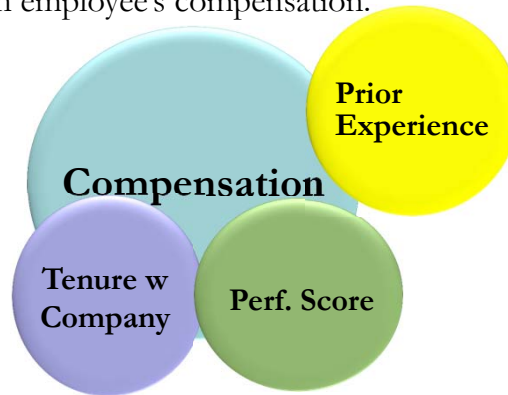
The Regression "Model"

Q: So how does regression help to identify discrimination in pay?

A: If the prediction model becomes significantly better *after* including the protected variable.

Experience
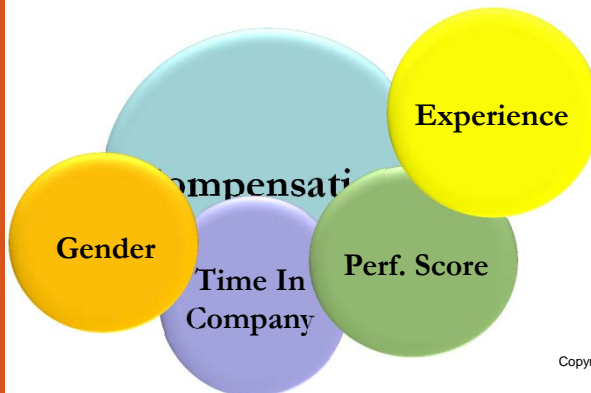
$R^2 = 45\%$
without gender

Compensation

$R^2 = 51\%$
with gender

Gender

Time In Company

Perf. Score

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Practical Strategies and Recommendations

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Strategies and Recommendations

Policy/Personnel-Based

Step 1: Audit Current Pay Documentation Practices – Verify sufficient documentation exists to clearly support compensation decisions. Focus primarily on rationale behind **starting pay** and performance-based specifics.

Step 2: Develop Specific Criteria for Compensation Decisions – Develop objective and measurable guidelines for compensation decisions and apply them consistently. For example: establish (narrow) starting salary ranges for specific positions.

Step 3: Review Compensation Decisions – Establish third-party internal review process for compensation decisions (e.g., starting salary, yearly increases, etc.) . . . review should be conducted by personnel with knowledge of identified issues.

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Strategies and Recommendations

Policy/Personnel-Based (cont.)

Step 4: Revise Document Retention Practices as Necessary – Maintain records regarding compensation decisions to ensure data/evidence is available in the event of future litigation.

Step 5: Train Supervisors and Managers – Train all supervisors and managers regarding new policies/procedures.

Step 6: Conduct Periodic Statistical Analysis of Compensation Data – Proactively determine whether pay disparities exist. Once identified, make adjustments to eliminate unexplained disparities (only make adjustments after a statistical *and* cohort-level review have been conducted)

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Strategies and Recommendations

Nothing "sells" the need for action like liability calculations!

Analytical

Step 1: Create pivot tables (as initial investigation)

JOBCODE/JOBTITLE	Data	Female	Male	Grand Total	Difference	Difference (%)	Potential Liability ($)[1]
ADMINISTRATIVE SUPPORT	Count of GENDER	12	5	17			
Priority 2	Average of Salary	$12.08	$14.52	$12.80	$2.44	16.8%	$152,256.00
	Average of Time in Company	3.0	8.9	3.9	5.9		
	Average of Performance	3.1	4.6	3.5	1.5		
	Average of Time in Job	1.1	3.6	1.8	2.5		
CUST SERV REP 1	Count of GENDER	24	126	150			
Priority 1	Average of Salary	$11.29	$13.25	$12.94	$1.96	14.8%	$244,608.00
	Average of Time in Company	4.2	3.1	3.9	-1.1		
	Average of Performance	3.4	2.9	3.3	-0.5		
	Average of Time in Job	4.2	3.1	3.9	-1.1		
CUST SERV REP 2	Count of GENDER	45	29	74			
	Average of Salary	$14.29	$14.35	$14.31	$0.06	0.4%	$14,040.00
	Average of Time in Company	5.1	4.9	5.0	-0.2		
	Average of Performance	3.0	3.0	3.0	0.0		
	Average of Time in Job	2.9	2.7	2.8	-0.2		
DEPARTMENT MANAGER	Count of GENDER	8	15	23			
Priority 2	Average of Salary	$15.97	$17.42	$16.92	$1.45	8.3%	$60,320.00
	Average of Time in Company	6.6	6.7	6.6	0.1		
	Average of Performance	4.2	4.2	4.2	0.0		
	Average of Time in Job	4.1	4.2	4.1	0.1		
SUPERVISOR - CUSTOMER SERVICE	Count of GENDER	15	24	39			
Priority 3	Average of Salary	$23.70	$23.70	$23.70	$0.00	0.0%	$0.00
	Average of Time in Company	8.3	2.0	6.4	-6.3		
	Average of Performance	4.8	2.9	4.2	-1.9		
	Average of Time in Job	4.9	0.8	3.7	-4.1		

Note:
1. Potential Liability = "Make-Whole Relief" = Difference ($) x 2080 (hours) x 2 (years) x # impacted x 1.25 (benefits + interest)

Strategies and Recommendations

Analytical (cont.)

Step 2: Prioritize your efforts (focus on the low-hanging fruit – i.e., a statistically significant difference with a large number of employees

Step 3: Conduct statistical regression analyses (if differences are identified in initial review)

Step 4: Conduct "cohort" review (i.e., a file-by-file review to identify why differences remain – ***starting salary***, education, prior salary, quantity or quality of previous experience)

- Starting salary is often the culprit . . . But the question is **why are the starting salaries different and do you have the information necessary to justify the difference?**

Step 5: Make changes where differences cannot be justified statistically _or_ by cohort review (must use regression analyses to identify the amount needed for each impacted individual)

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Strategies and Recommendations

Cohort Review (Example 1)

Sample Cohort Analysis Ordered by Salary (Descending)

Name	Gender	Salary ($)	Time in Co. (Years)	Avg. Perform. Scores (3 years)	Educ. (Years)
Steve Randall	M	$57,000	7.3	3.5	18
Chris Avery	M	$52,350	4.9	3.3	16
Leigh Barrows	F	$51,950	12.1	3.9	18
Danielle Yoko	F	$51,500	11.0	3.4	16
Mike Freeman	M	$51,000	13.9	2.9	16
Frank Viola	M	$50,500	8.7	3.2	16
John Smith	M	$50,000	8.5	3.5	16
Frank Robison	M	$49,560	12.1	2.7	16
John Cameron	M	$49,250	9.5	3.0	16
Mike Stevens	M	$48,995	10.9	4.0	16
Shelli Jackson	F	$48,000	8.5	2.9	16
Desiree Laub	F	$47,580	8.9	3.8	16
Dan Bostick	M	$43,675	9.2	2.9	16
Nina Ling	F	$42,850	3.6	3.9	18
Heather Monte	F	$42,678	4.9	3.8	16
Shana Larris	F	$40,750	13.8	3.9	18
Nancy Tramel	F	$40,500	5.6	3.3	16

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Strategies and Recommendations

Cohort Review (Example 2)

Sample Cohort Analysis Ordered by Time in Company (Descending)

Name	Gender	Salary ($)	Time in Co. (Years)	Avg. Perform. Scores (3 years)	Educ. (Years)
Mike Freeman	M	$51,000	13.9	2.9	16
Shana Larris	F	$40,750	13.8	3.9	18
Leigh Barrows	F	$51,950	12.1	3.9	18
Frank Robison	M	$49,560	12.1	2.7	16
Danielle Yoko	F	$51,500	11.0	3.4	16
Mike Stevens	M	$48,995	10.9	4.0	16
John Cameron	M	$49,250	9.5	3.0	16
Sarah Norris	F	$47,560	9.2	2.9	16
Dan Bostick	M	$43,675	9.2	2.9	16
Desiree Laub	F	$47,580	8.9	3.8	16
Frank Viola	M	$50,500	8.7	3.2	16
John Smith	M	$50,000	8.5	3.5	16
Nancy Tramel	F	$40,500	5.6	3.3	16
Heather Monte	F	$42,678	4.9	3.8	16
Chris Avery	M	$52,350	4.9	3.3	16
Nina Ling	F	$42,850	3.6	3.9	18

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Strategies and Recommendations

Impact of Starting Salary (Example 1)

Longitudinal Impact of $4,000 Difference in Starting Salaries (Assuming a Constant 4% Yearly Increase)

Year	Salary ($)		Pay Disparity ($)
	Mike	**Stephanie**	
Starting	$40,000.00	$36,000.00	$4,000.00
5	$46,794.34	$42,114.91	$4,679.43
10	$56,932.47	$51,239.23	$5,693.25
15	$69,267.06	$62,340.35	$6,926.71
20	$84,273.97	$75,846.57	$8,427.40
25	$102,532.17	$92,278.95	$10,253.22
30	$124,746.06	$112,271.45	$12,474.61

Accumulated difference over 30 years: $224,339.75
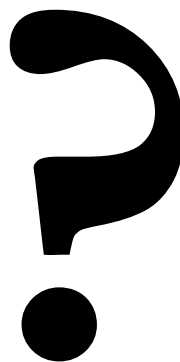
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Strategies and Recommendations

Impact of Starting Salary (Example 2)

Longitudinal Impact of $4,000 Difference in Starting Salaries (Assuming: 4% Yearly Increase for Mike / 5% Yearly Increase for Stephanie)

Year	Salary ($)		Pay Disparity ($)
	Mike	**Stephanie**	
Starting	$40,000.00	$36,000.00	$4,000.00
1	$41,600.00	$37,800.00	$3,800.00
2	$43,264.00	$39,690.00	$3,574.00
3	$44,994.56	$41,674.50	$3,320.06
4	$46,794.34	$43,758.23	$3,036.12
5	$48,666.12	$45,946.14	$2,719.98
6	$50,612.76	$48,243.44	$2,369.32
7	$52,637.27	$50,655.62	$1,981.66
8	$54,742.76	$53,188.40	$1,554.37
9	$56,932.47	$55,847.82	$1,084.66
10	$59,209.77	$58,640.21	$569.56
11	$61,578.16	$61,572.22	$5.95
12	$64,041.29	$64,650.83	