

GUIDANCE FOR EMPLOYERS ON STARTING COMPENSATION

Overview of Current Law

Under California law pursuant to Labor Code 432.3(e), employers cannot:

- Seek salary history, including “compensation and benefits,” of an applicant
- Rely on salary history information in determining whether to offer employment or what salary to offer unless the applicant voluntarily and without prompting discloses their salary history
- Rely on prior salary, by itself, to justify any disparity in compensation based on sex, race, or ethnicity

The law also requires employers to provide the pay scale for a position to an applicant who makes a reasonable request for that information.

In this tool, we provide suggested practices for employers for setting starting salaries based on factors other than prior salary. Each organization is different, and there is no one-size-fits-all strategy. However, we aim to provide high level tips, examples, and factors for employers to consider. Ultimately, each employer must determine how best to develop, implement and maintain a non-discriminatory compensation system. Nothing expressed here mandates or requires employers to follow any of the suggested guidance. Nor will a failure by an employer to follow this guidance be construed as a violation of the law.

[[LINK TO OVERVIEW OF CURRENT CA LAW](#)]

Suggested Practices for Employers in Setting Starting Salaries

Compensation Philosophy. Before determining what any given employee should be paid, you should consider developing and documenting the organization’s compensation philosophy. In other words, how does your organization think about compensation? What do you value in your employees? What factors are important in recruiting new hires? What different forms of compensation do you offer? Documenting this information and communicating it to those involved in hiring and setting compensation—whether through training, written policies, or otherwise—is important so that you can (1) be consistent in setting pay; and (2) later demonstrate legitimate reasons for any pay differences if necessary.

All organizations use and state their compensation philosophy differently. Generally, any compensation philosophy should be based on the premise that employees will be paid in a fair and non-discriminatory manner. Employers should consider performing a gender and race/ethnicity based analysis of pay for current employees in substantially similar jobs. Key considerations for setting compensation for both current and prospective employees might include, but not be limited to, some combination of those listed below:

- Rewarding employees for job performance that is evaluated based on gender-neutral factors.
- Rewarding employees for their impact or contribution to the organization, e.g., have they contributed to a particularly meaningful project that advanced the organization's competitive goals or increased revenue?
- Employee retention: Is any component of the compensation package designed to encourage employees to stay? For example, some employers offer deferred compensation that is paid out over a period of years so long as the employee stays with the organization for a certain period of time.
- Market competitiveness: Is it important to your organization to offer a compensation package that is competitive with the market in which you are competing for talent as reflected, for example, in market surveys or other external market data?
- Employee motivation: Are certain forms of compensation designed to motivate employees to achieve certain goals or performance metrics? For instance, some employers pay commissions to sales employees based on sales revenue achieved.
- Budget: How much money is available for employee compensation considering other organization expenses?
- Profitability: Are certain components of compensation based on your organization's financial performance?
- What is the scope, breadth, and/or depth of the role and its impact on your organization?

New Hires. In addition, consider what factors are important to you in recruiting new hires. Some examples are provided below, though various other factors could be considered as well.

- Relevant experience

- Relevant education
- Relevant training
- Relevant skills or knowledge
- Market conditions
- Geography/location
- Competing offer

If you rely on any of the considerations above, either upon hire or during employment, you must still show that each is a bona fide factor other than sex, is reasonably applied, is job related, is consistent with business necessity, and accounts for the entire wage differential.

[\[LINK TO STEP BY STEP DOCUMENT\]](#)

Imagine, for example, that your company sells widgets and you are looking to compete in the marketplace by making a new state-of-the-art widget. You conduct market research and find that there are few in the industry who have the experience necessary to make that type of widget. Due to high demand, those employees tend to be paid more than other widget makers. Your company makes a strategic decision to pay above market to recruit and retain those who have the specialized experience. This market consideration may justify pay disparities between widget makers. However, it would not justify a disparity if your company does not consistently consider this specialized experience when setting pay for employees with this specialized experience.

What if one of the widget makers with the specialized experience says they have a competing offer for higher pay? This may reflect growing competition in the market and may justify making a higher counteroffer. However, you should consider asking the applicant what it would take for them to accept the job with your company. Would they expect to make the same amount? Have they considered the total compensation package you are offering? Is the competing offer for a role that is substantially similar to the position for which the applicant applied? Do the applicant's qualifications support their increased compensation expectations? Would the counteroffer otherwise be consistent with your compensation philosophy? The answers to these questions may later help you justify this employee's higher rate of pay. It may also be helpful to consider whether the incumbent salaries should be adjusted as well (see Internal Equity).

Finally, an employer's compensation philosophy should also account for what forms of compensation are offered. Examples include:

- Base pay
- Bonus
- Stock or stock option awards
- Commission or other incentive compensation
- Benefits like medical insurance and retirement
- Other non-financial benefits such as:
 - Time away from work,
 - Flexible starting times,
 - Commute allowances,
 - The ability to work from home X number of days a week or month,
 - Special training opportunities,
 - Tuition reimbursement
 - 1025 benefit coverage, FLSA advantages
 - Childcare assistance/provision

Internal Equity. When setting pay for new employees, consider what current employees are making in jobs that are substantially similar [[LINK TO STEP BY STEP DOCUMENT](#)]. If there is a disparity between what you are hoping to pay the new employee as compared to current employees, evaluate whether the entire disparity can be justified based on a bona fide factor other than sex that is reasonably applied, job related, and consistent with business necessity.

Setting Salary Ranges. Consider setting salary ranges for each job position prior to interviewing applicants. To do this, you can look at external market data and the salaries of your existing employees in jobs that are substantially similar when viewed as a composite of skill, effort, and responsibility. This will help you evaluate the reasonable value to your organization of each job position. Employers generally aim to place new hires in the salary range based on the applicant's readiness for the position. A fully qualified applicant is likely to be placed in the

mid-point of the range, absent appropriate differentiating factors that may support placement at the higher or lower end of the range.

Communicating with the Prospective Employee about Starting Salary. Strategies exist for evaluating what to pay new employees without asking their prior salary or other prior forms of compensation or benefits. Ultimately, you want to know if there is a possible “match” between the applicant’s expectations and the realities of the total compensation for the position you are discussing.

To accomplish this, you can:

- Ask the applicant, "What are your salary expectations?" and ask why they believe their qualifications are in line with their expectations.
- If the applicant mentions that he or she would be forfeiting deferred equity by leaving their current job, focus back on the applicant’s expectations: “What does that mean in terms of your compensation expectations? What will it take for you to take a job at this organization?”
- Be ready to discuss your pay scale (i.e. salary range) for the specific position for which you are considering the applicant and for which the applicant is qualified, whether that be an internal or external applicant. Remember that the law requires employers to provide the pay scale for a position to an applicant applying for employment who makes a reasonable request for that information. If you do not already have a pay scale for the job, be prepared to provide the range of what you are prepared to pay for the position. If there is only one static rate as opposed to a range, provide the rate.
- Be prepared to discuss your compensation philosophy, which may help guide the applicant in setting their salary expectations and explain their basis for them.
- Be able to clearly define the “total” compensation being offered, especially if there are performance-based bonuses or rewards. This should also include a discussion of what other non-financial incentives the organization offers.

Document What You Considered in Setting the Employee’s Compensation. Take the time to appropriately document the factors you consider in setting each employee’s pay upon hire to ensure that you are making decisions that are consistent with your compensation philosophy and to enable the organization to better defend these decisions if later challenged.

If you conduct individualized reference checks, take notes about responses, including what the references said and on what date they said it. This information can be key in making a more accurate assessment about the applicant. Below are examples of questions that you can ask an applicant's references to further solidify the responses gathered from the applicant:

- What the applicant did in the previous position
- Confirm the applicant's title and the scope of their responsibilities
- What were their major strengths? (ask for example)
- Was there any area that needed more development? If so, what?
- What did you value and appreciate most about this applicant?
- What were the applicant's major accomplishments? Impact on the workplace?
- Were they a team player? How do you define that?
- Were they reliable and dependable? Define?
- Did you respect and trust/not respect and trust them? Why?
- Would you hire/rehire this person? Into what types of job?
- Any other question you feel is key to the job.
- If they show reluctance, explain a little bit about the position and ask if they feel the prospective applicant could do that work: Do you see any difficulty in the match between the job and the employee? What?