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Relations industrielles / Industrial Relations, vol. 29, n° 1, 1974, p. 99-110.

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URI: <http://id.erudit.org/iderudit/028480ar>

DOI: 10.7202/028480ar

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Employee Pay and Benefit Preferences

Harish C. Jain and Edward P. Janzen

Despite a continuing growth of fringe benefits as a proportion of the total wage bill, few employees have any definite knowledge of what fringes employees really prefer. This article reports the results of a study which attempted to measure employees preferences for alternative forms of compensation in six organizations located in Ontario, Canada.

National surveys show that fringe benefits amount to nearly thirty percent of an average employer's payroll cost.¹ A recent study indicates that after adjustment for the effects of inflation, employee benefits for the years 1929-1967 increased at the rate of 9.6 percent per year as contrasted with a wage and salary average annual increase of 3.9 percent.² Thus, there has been a continuing enlargement of benefits in the total wage bill.

Despite such dramatic increase in employee fringes, few employers

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¹ *Employment Benefits 1967*, Washington, D.C., Chamber of Commerce of the United States, 1968, p. 5. Also see, *Labour Costs in Manufacturing 1968*, Ottawa, Queen's Printer, December 1969. The estimates in this survey are representative of selected employer labour costs in 13,500 Canadian establishments in manufacturing. *Fringe Benefit Costs in Canada, 1967*, Toronto, Ontario, The Throne Group Ltd., 1968. E. Robert LIVERNASH, «Wages and Benefits», in W. L. GINSBURG, *et al.*, (editors), *A Review of Industrial Relations Research*, Madison, Wisconsin, Industrial Relations Research Association, Vol. 1, 1970, pp. 79-144.

² T. J. GORDON and R. E. LEBLEW, «Employee Benefits, 1970-1985», *Harvard Business Review*, Boston, Massachusetts, Vol. 48, January-February 1970.

have any definite knowledge of what employees really prefer. In other words, the needs and wants of employees have received little systematic study.³ This article reports a study which attempts to measure employee preferences for alternative forms of compensation ; for example, between straight pay and various forms of fringe benefits. As a framework for reporting the findings of this study, fringe benefits are defined, the employer and employee rationale for enlargement of benefits is described and the importance of methodology in determining employees options is reviewed.

DEFINITION

Fringes vary from company to company and range from such basics as vacations and holidays to such items as private country clubs (IBM), employee recreation areas and art lessons (NCR, Texas Instruments), etc. It is estimated that today there are some two hundred different items which could qualify as benefits. It is not surprising, therefore, that fringe benefit definitions are about as diverse as the benefits themselves. The authors feel, however, that one definition which is representative is as follows : a fringe benefit is any and every labour cost added to regular compensation (wages and salaries) paid for time worked.

Employer rationale in providing fringe benefits to his workers can be summed up as follows :

- a) to recruit and maintain a competent work force.⁴
- b) to motivate employees to increase their productivity.
- c) to prevent unionization of employees, where this has not taken place already.

³ For example, in a 1963 study, workers in one company indicated preference for a dental insurance program over a life insurance program four times more costly. See S. M. NEALEY, « Play and Benefit Preferences » in « Symposium : Psychological Research on Pay », *Industrial Relations*, Berkeley, California, Vol. 3, October 1963.

⁴ In a study conducted by Mark GREENE, an employee he interviewed indicated that he would prefer a meaningful benefit in lieu of higher wages. This employee was with a company which maintained attractive recreational facilities in the form of a country club. When this employee was offered a better job elsewhere at a higher rate of pay, he turned it down. « Give up the country club », he exclaimed, « I wouldn't think of it ». See, *The Role of Benefit Structures in Manufacturing Industry*, Eugene, Oregon, School of Business Administration, University of Oregon, 1964.

- d) to prevent further government encroachment by way of legislation.⁵
- e) to give benefits to employees rather than pay the government in the form of taxes.⁶

Employees prefer benefits rather than cash for at least part of their compensation.⁷ There is some evidence that employees prefer fringe benefit plans tailored to individual needs,⁸ for the following reasons :

- a) the needs of different employees vary with each individual situation, that is, individual requirements of age, marital status, financial status and dependents requirements.
- b) the comparatively large number of younger and better educated employees who oppose regimentation or uniformity.
- c) the general interest of the current generation in individualized treatment.
- d) the desire for more benefits.
- e) the effect of high taxes.
- f) desire for more leisure.⁹

The above mentioned reasons indicate the importance of proper selection of benefits by a systematic study of employee needs. The importance of methodology in determining employee preferences is, therefore,

⁵ Employer expenditures for Workmen's Compensation, Unemployment Insurance and the Canada or Quebec Pension Plan amounted to 2.9 percent of gross payroll. See, *Labour Costs in Manufacturing 1968*, *op. cit.*

⁶ For a general discussion of employer rationale, see J. TAYLOR, «Toad or Butterfly? A Constructive Critique of Executive Compensation Practices», *Industrial and Labor Relations Review*, Ithaca, New York, Vol. 21, 1968, pp. 491-508. R. L. BLOMSTROM, «Some Competitive Aspects of Fringe Benefits», *Personnel Journal*, Swarthmore, Pennsylvania, 1964, pp. 11-14.

⁷ Richard A. LESTER, «Benefits as a Preferred Form of Compensation», *Southern Economic Journal*, Chapel Hill, North Carolina, Vol. 33, No. 4, April 1967, pp. 488-495.

⁸ See articles by NEALEY, ANDREWS, and HENRY in «Symposium: Psychological Research on Pay», *op. cit.* Also see, «Consultant on Benefits Predicts Plans Tailored to Individual Needs», *Globe and Mail*, Toronto, Ontario, January 22, 1971, and W. W. WEISS, «The Hardest Story Ever Told: Employee Benefits», *Public Relations Journal*, New York, Public Relations Society of America, Inc., Vol. 22, August 1966, pp. 11-13.

⁹ E. W. WILLIS and F. R. KAIMER, «Employee Benefit Options», in *Twenty-First Annual Winter Meeting of the Industrial Relations Research Association*, Madison, Wisconsin, 1968, pp. 317-325. Also see «Discussion» by Stanley M. NEALEY of WILLIS and KAIMER paper, pp. 326-329.

crucial to devising a proper mix of compensation package so that both the employer and employee needs are met.

THE IMPORTANCE OF METHODOLOGY IN DETERMINING EMPLOYEE PREFERENCES

The procedure for determining what employees prefer to have in their compensation package can vary, but some pitfalls can be avoided by a proper selection of the methodology.

In the previous studies on this subject, researchers, in general, have used three methods. One of the simplest methods is that of asking open-ended questions. Respondents are typically asked, « What one or more benefits would you like to receive not now offered by your company ? » The problem with this method is that some employees will be much more aware of the various types of benefits available than others, and this is bound to distort preferences. Neither will this particular question provide information on preferences among existing benefits.

Another method used in previous studies is the rank-order technique. Here each respondent is asked to rank in order of importance to him the given items of a compensation program. This approach has merit in that it can be done quickly and is not dependent on the employee's knowledge of various benefit options.¹⁰ However, the rank order technique carries with it the rather serious disadvantage that differences between adjacent ranks do not necessarily indicate differences of equal magnitude. An employee may prefer life insurance above vacations, but this method does not tell the investigator how strongly the employee prefers the one benefit over the other.¹¹

¹⁰ Previous studies have shown that only a few employees have complete knowledge of the benefits they are receiving. See Harish C. JAIN, « Employee Knowledge of Compensation Policies and Supervisory Performance in Hospitals », in press. Arthur A. SLOANE and Edward W. HODGES, « What Workers Don't Know About Employee Benefits », *Personnel*, New York, American Management Association, Vol. 5, No. 6, November-December 1968, pp. 27-34. W. WEISS, *op. cit.*, and Mark R. GREENE, *op. cit.*

¹¹ An interesting device to get around the problem of these differences in magnitude was employed by LAWLER and LEVIN. They developed a questionnaire which listed ten items for which respondents were asked to express preferences. With each questionnaire was an envelope with gummed stickers in five and ten dollar denomination totalling \$200.00. These were to be posted beside the ten alternatives to express preference and also magnitude of preference for each of the various items. See E. E. LAWLER and E. LEVIN, « Union Officers Perceptions of Members' Pay Preferences », *Industrial and Labor Relations Review*, Ithaca, New York, Vol. 21, No. 4, July 1968, pp. 509-517.

The third method used to determine employee preferences of benefits is the paired-comparison technique.¹² For example, individuals are asked to choose between :

- a) increased pay and b) increased vacation.
- b) increased vacation and c) increased pension.
- c) increased pay and c) increased pension.

The advantage of this method is that the respondent can be asked to make a choice in such a way that the selection of one factor specifically decreases the opportunity to benefit from another related factor, and allows a validation of the choices ; if the respondent chooses (a) over (b) and (b) over (c), he should logically choose (a) over (c) or else he is being inconsistent. Paired comparisons do not solve all problems, however, inasmuch as the respondent may still wonder how much more or less pay would be involved or how much additional vacation is contemplated. This can be overcome by specifying at the beginning of the questionnaire the value of the components ; in this particular study we asked, « If you were to receive a 5% increase, and could allocate this to any one of the following choices, which would you prefer ? »

METHODOLOGY USED IN THIS STUDY

In this study a sample of professional, technical and rank-and-file employees was randomly selected from six organizations in Southern Ontario. The sample included employees from three manufacturing plants, two educational institutions, and one government agency. A total of one-hundred and twenty-eight employees responded to our questionnaire.¹³

The questionnaire provided five options, to be compared two at a time. The options included five benefits : pension, life insurance, vacations,

¹² For studies using this technique see S. M. NEALEY, *op. cit.*, L. V. JONES and T. E. JEFFREY, « A Quantitative Analysis for Expressed Preferences for Compensation Plans », *Journal of Applied Psychology*, Washington, D.C., Vol. 48, No. 4, August 1964, pp. 201-210.

¹³ The field work for this survey was conducted by J. GORDON, E. P. JANZEN, K. PARSONAGE, J. D. STOTT, and J. WRAY, all graduate students in business administration at McMaster University, Hamilton, Ontario.

pay increase, and medical insurance. Exhibit 1 displays the sequence of preference listing.¹⁴

EXHIBIT 1

ITEMS FROM QUESTIONNAIRE ON EMPLOYEE PREFERENCES FOR FRINGE BENEFITS AND COMPENSATION

If you were to receive a 5% increase, and could allocate this to any one of the following choices, which would you prefer? -- (check only one box in each line)

- | | | | | |
|--------------------------------|--------------------------|----|-----------------------------|--------------------------|
| 1. Increased Pension | <input type="checkbox"/> | OR | Increased Medical Insurance | <input type="checkbox"/> |
| 2. Increased Life Insurance | <input type="checkbox"/> | OR | A Pay Increase | <input type="checkbox"/> |
| 3. Increased Vacation | <input type="checkbox"/> | OR | Increased Medical Insurance | <input type="checkbox"/> |
| 4. A Pay Increase | <input type="checkbox"/> | OR | An Increased Pension | <input type="checkbox"/> |
| 5. Increased Life Insurance | <input type="checkbox"/> | OR | Increased Vacation | <input type="checkbox"/> |
| 6. Increased Medical Insurance | <input type="checkbox"/> | OR | A Pay Increase | <input type="checkbox"/> |
| 7. Increased Pension | <input type="checkbox"/> | OR | Increased Life Insurance | <input type="checkbox"/> |
| 8. A Pay Increase | <input type="checkbox"/> | OR | Increased Vacation | <input type="checkbox"/> |
| 9. Increased Medical Insurance | <input type="checkbox"/> | OR | Increased Life Insurance | <input type="checkbox"/> |
| 10. Increased Vacation | <input type="checkbox"/> | OR | Increased Pension | <input type="checkbox"/> |

The questionnaire also requested information on demographic and other variables such as age, sex, marital status, number of dependents, educational level, length of service, place of employment, etc. Employee responses were cross-classified by these variables in analyzing the results of this study.

¹⁴ Preferences were listed in such a way that an item appeared first in the preference sequence as often as it appeared second and never appeared in an immediately following preference choice. This technique allowed a matrix analysis of scores to obtain preference ranking, to check for inconsistent response patterns, and to note omissions that would invalidate a question.

SURVEY RESULTS

Results can be classified into three categories.

Overall Results

The results shown in Exhibit 2 indicate that the compensation most preferred was a pay increase. Preference for an increase in pay was followed, in decreasing order by a preference for an increase in vacation, pensions, medical insurance, and life insurance.

TABLE 1
EMPLOYEE PREFERENCES FOR ALTERNATIVE
FORMS OF COMPENSATION

| <i>Form of Compensation</i> | <i>Preference Ranking</i> | | | | | |
|-----------------------------|---------------------------|----------|----------|----------|----------|----------|
| | <i>Organizations :</i> | | | | | |
| | <i>A</i> | <i>B</i> | <i>C</i> | <i>D</i> | <i>E</i> | <i>F</i> |
| Pay | 1 | 1 | 1 | 1 | 1 | 1 |
| Vacation | 4 | 1 | 2 | 2 | 2 | 3 |
| Pension | 3 | 2 | 4 | 3 | 4 | 2 |
| Medical | 2 | 3 | 3 | 3 | 3 | 4 |
| Life | 5 | 4 | 5 | 4 | 5 | 5 |

These results can also be illustrated by the rankings given by the employees, in this study, in each of the six organizations. As shown in Table 1, in all six organizations pay received first choice ; nonmonetary form of compensation (vacation, pension, medical and life insurance) generally are ranked below pay increase. Life insurance is generally ranked as the least desirable form of increased compensation.

The overall picture which these measures give us is that employees have an overwhelming desire to receive their compensation in the form of pay and want only minimal protection in the form of medical and life insurance.

EXHIBIT 2

OVERALL PREFERENCE SCORE FOR SURVEY GROUP

(N = 128)

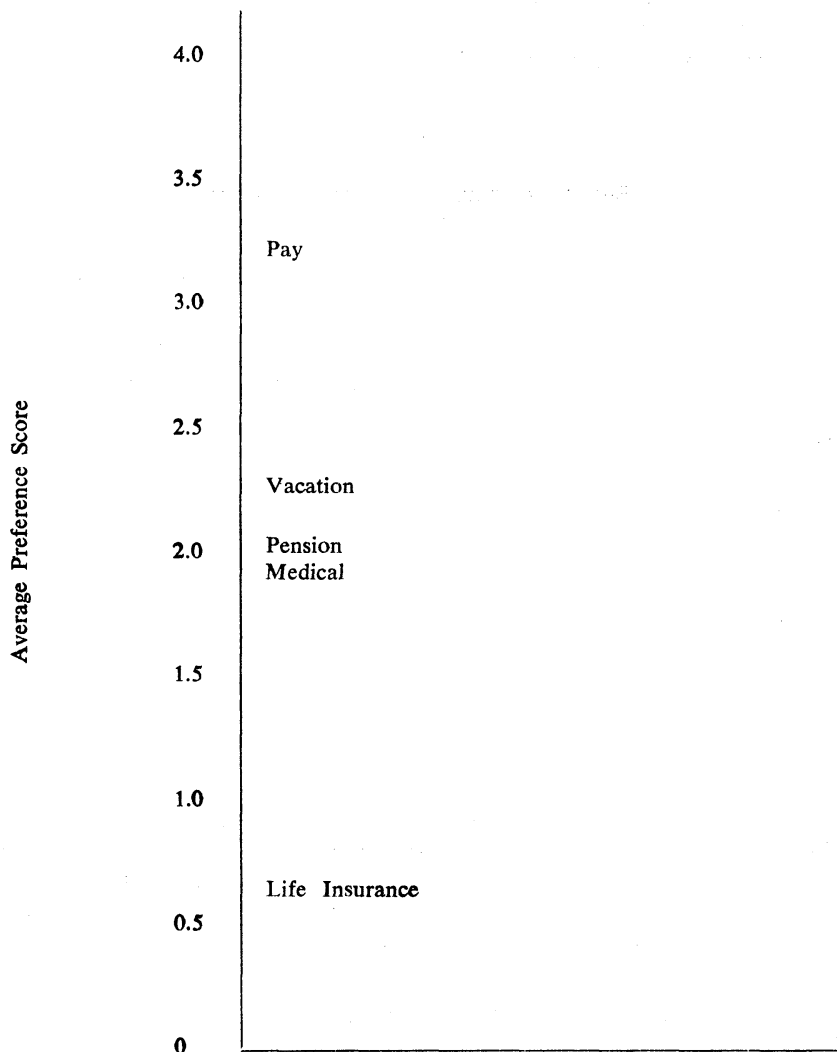


EXHIBIT 3

AVERAGE PREFERENCE AS A FUNCTION OF EMPLOYEES' YEARS OF SERVICE WITH THE ORGANIZATION

| | | | | | | | |
|-----|---------------------|--------------------|------------------|---------------------|------------------|------------------|-----------------------|
| 3.4 | | | | Pay | | Pension | |
| 3.2 | Pay | Pay | Pay | | Pay Vacation | | Pension |
| 3.0 | | | | | | | |
| 2.8 | | | | | | | |
| 2.6 | | Vacation | Vacation | | | Vacation | |
| 2.4 | Pension Vacation | | | | Pension | | |
| 2.2 | | | Pension | Medical Vacation | | | Medical Pay |
| 2.0 | Medical | Pension Medical | | | | Pay Medical | |
| 1.8 | | | Medical | Pension | | | |
| 1.6 | | | | | Medical | | Vacation Life Ins. |
| 1.4 | | | | | | | |
| 1.2 | | | | | | | |
| 1.0 | | | | | | | |
| 0.8 | | | | | | | |
| 0.6 | Life Ins. | Life Ins. | Life Ins. | Life Ins. | | | |
| 0.4 | | | | | | Life Ins. | |
| 0.2 | | | | | | | |
| 0 | | | | | Life Ins. | | |
| | Under 1 (N = 14) | 1-5 (N = 56) | 6-10 (N = 31) | 11-15 (N = 10) | 16-20 (N = 6) | 21-25 (N = 5) | 26-30 (N = 3) |

Results by Demographic Variables

As shown in Exhibit 3, the one demographic variable which seems to effect preferences is length of service with the organization. A preference for a pay increase declines in importance particularly in the service

range from 21 to 30 years.¹⁵ This preference is to be expected with persons reaching retirement age, but the decline in preference for medical insurance as age increased was somewhat surprising.

There was no significant difference in this ranking when respondents were classified either as to sex number of dependents or marital status.

The preference for life insurance remained the lowest relative to the various demographic factors studied.

Results by Occupational Category

The occupational category of an employee seems to have an influence on his choice of benefits in this study. Technical employees expressed a very high preference for increased pay. Professional staff preferred increased vacation equally with increased pay and ranked them well above the other three choices. Rank and file workers showed a marked preference for increased pensions. Causal factors for these preferences were not explored but could be an area of investigation for the future ; if the cause can be discovered, it may be easier to cure than simply increasing the benefit for which preferences are expressed. For example, if job insecurity caused the rank and file workers to prefer increased pensions, this might be resolved through a publicity program on employment security with the firm rather than by increasing the pensions.

SUMMARY

In summary, the overall preference ranking in decreasing order was : pay increase, vacation increase, pension increase, medical benefit increase and life insurance increase. Employees in all six organizations expressed a general preference for any increase with minimal protective compensation in the form of medical and life insurance. When analysed according to demographic information collected, differences were expressed according to the age and length of service.

¹⁵ The results of this study confirmed the observations of JURGENSON that changes accompanying age changes do not occur gradually over time but tend to occur suddenly and are accompanied by reversals. The preferences of respondents when classified by age showed a marked increase in preference for pension benefits at ages 40-49 ; this was also noted by NEALEY in his 1963 study. See C. E. JURGENSON, « Selected Factors which Influence Job Preferences », *Journal of Applied Psychology*, Washington, D. C., Vol. 31, No. 6, December 1947, pp. 553-564. S. M. NEALEY, *op. cit.*

CONCLUSIONS

The finding that pay increase was preferred over benefits is interesting in view of the renewed interest of scholars in pay and its effectiveness as a motivator for employee productivity. As Strauss points out, after many years in which behavioral scientists emphasized non-financial incentives and played down the importance of money, the last decade has seen a growing interest in pay and its effectiveness as a motivator.¹⁶ The findings of this study seem to indicate that we may have reached a point where employees wish to restrict the fringes at a certain level and prefer to receive wage or salary increase. While this study is not conclusive proof of the preferences of employees in all organizations, it does point out trends and confirms some of the findings of previous studies.

In order to generalize the results of this study, we need comparative studies over space, time and industry so that the results can be of use to personnel and industrial relations practitioners in designing an appropriate mix of compensation package.

SALAIRES ET AVANTAGES SOCIAUX : LA PRÉFÉRENCE DES TRAVAILLEURS

Malgré une augmentation continue de la proportion des avantages sociaux dans la masse salariale totale, peu d'employeurs connaissent d'une façon précise les véritables préférences des employés. Cet article analyse les résultats d'une étude qui s'efforçait d'apprécier les préférences des travailleurs pour certaines formes de compensation dans six entreprises localisées en Ontario. Les recherches de cette étude se fondent sur la définition du concept d'avantages sociaux, sur la description de la raison d'être de l'accroissement de ces avantages tant pour ce qui est des employeurs que des employés et sur l'importance de la méthodologie dans la détermination du choix des travailleurs.

On a défini ainsi les avantages sociaux : tout coût de la main-d'œuvre ajouté à la rémunération normale (salaires et traitements) versé pour une période de travail. On présume que les employeurs les offrent afin d'attirer et de garder les employés à leur service ou afin de les inciter à augmenter leur productivité. Les employés préfèrent les régimes d'avantages sociaux faits sur mesure. La raison en est que leurs besoins diffèrent selon leur âge, leur état matrimonial, etc. Quant aux jeunes travailleurs, la plupart d'entre eux s'opposent à toute forme d'embrièvement.

L'importance de la méthodologie dans la détermination de la préférence des employés est une question ardue. Il y est discuté du pour et du contre en ce qui

¹⁶ GEORGE STRAUSS, « Organizational Behavior and Personnel Relations », in W. L. GINSBURG, *et al.* (editors), *op. cit.*, pp. 145-206.

touche les trois façons d'apprécier leurs préférences : ce sont le questionnaire général, la technique du choix par ordre de préférence et la méthode comparative par jumelage.

Dans cette étude, les auteurs ont eu recours à la méthode comparative par jumelage. L'échantillonnage portait sur 128 employés de six entreprises du sud de l'Ontario. On a choisi au hasard les employés à qui le questionnaire fut remis. Le questionnaire offrait cinq options qu'ils pouvaient comparer l'une par rapport à une autre. Les options étaient les suivantes : pension, assurance sur la vie, vacances, augmentation de salaire, assurance médicale.

En résumé, la préférence, par ordre d'importance décroissante, s'est ainsi manifestée : augmentation de salaire, prolongement des vacances, abonnement du régime de retraite, du régime d'assurance sur la vie et du régime d'assurance médicale. Dans les six entreprises, les employés ont exprimé d'une façon générale leur préférence pour l'augmentation de salaire. Ce qu'ils recherchèrent le moins, ce fut l'amélioration des régimes d'assurance sur la vie et d'assurance médicale. Analysées en regard des données démographiques recueillies, les divergences se sont exprimées suivant l'âge et la durée du service.

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