



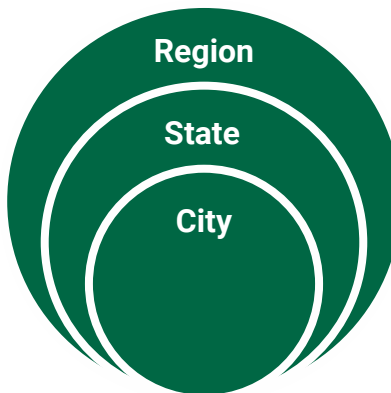
# How to Design a Geographic Salary Structure



In today's highly competitive market environment, it is important to maintain a [salary structure](#) responsive to your organization's [labor market](#). Getting market pricing wrong can result in high labor costs or non-competitive rates, leading to high turnover or employee engagement issues. Getting it right can be cost effective and support the creation of a highly motivated, engaged workforce with healthy turnover.

Geographic salary structures are a prevalent tool in today's marketplace. There are typically three different approaches used for developing a geographic salary structure: city, state, or region. A state or regional approach may appear to be simpler, but can lead to underpaying or overpaying in key competitive locations. A city approach is generally considered to be a best practice and allows a company to manage geographic pay by the city office location. When a business has operations in a multitude of cities throughout the United States or even globally, it may not seem practical to differentiate by city.

One of the key challenges is to design a geographic pay program that is competitive in terms of market pay rates and responsive to business needs and today's legal environment. Meanwhile, it is important to maintain simplicity in these types of programs.



## **PAY EQUITY**

When using geographic pay, it is also important to stay abreast of state and federal pay equity laws. At present, California, New York, Maryland, and Massachusetts include location as a component of their pay equity laws. For example, Maryland and New York currently require pay equity within a county. The Pay Equity Group of Seyfarth Shaw published an excellent [brochure](#) in 2016 on pay equity requirements for these states.

## **ELIGIBILITY**

Jobs that are recruited locally or regionally are excellent candidates for geographic pay. Jobs that are recruited nationally, such as the executive team, are not typically eligible for geographic pay.

## HYPOTHETICAL COMPANY EXAMPLE

Let's review a hypothetical example of a company headquartered in Denver, Colorado, with Customer Service offices in the following locations:

City	State
Montgomery	Alabama
Los Angeles	California
Placerville	California
San Francisco	California
San Jose	California
Denver	Colorado (Headquarters)
Chicago-Lincoln Park	Illinois
Baton Rouge	Louisiana
Missoula	Montana
New York-Manhattan	New York
Chicago-Lincoln Park	Illinois
Baton Rouge	Louisiana
Missoula	Montana
Columbus	Ohio
Nashville	Tennessee
Tyler	Texas
Superior	Wisconsin
Bellevue	Washington

For the purposes of this example, we have used data from [ERI's Salary Assessor](#)<sup>®</sup> and the market median of a Customer Service Representative (General Calls) for All Industries to determine the base salary difference by geographic location.

## STATE

Let's look at how the median annual base salary of a Customer Service Representative (General Calls) varies by state. For the purposes of this paper, we are comparing our headquarters location (Colorado) to each state in the United States. (As an alternative, we could use the United States national market data in lieu of the headquarters location.)

As a first point of review, we can calculate the percent difference of the median salary for the Customer Service Representative for each state as compared to the Colorado state market median. Based on 50 states, there are 27 different median market pay rates for the Customer Service Representative when compared to the headquarters pay by state, with a low of 84% in Arkansas and a high of 114% in the District of Columbia. This is overly complex for a geographic pay program and can be simplified by rounding the differentials to the nearest 10%. (Rates below 5% may be too small to recognize.) This then creates just four different geographic rates throughout the United States for the Customer Service Representative, which may be more appropriate.

Although the geographic salary structure by state will work, there are some items worthy of consideration:

- Differences by state combine many metropolitan, suburban, and rural marketplaces. For example, California has markets ranging from high-priced San Francisco and Silicon Valley to Los Angeles, Fresno, Bakersfield, and the even lower-priced Placerville and other similar lower-priced markets.
- The geographic salary structure by state does not sufficiently recognize hot job markets.
- The geographic salary structure by state can inflate compensation for lower-priced, small cities and rural markets.

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## PAY BY STATE

Position Title: Customer Service Representative (General Calls); eDOT: 205362200 SOC: 434051

State	ERI Survey Median Annual Base Salary	Designated State as % of HQ	Designated State Rounded as % of HQ
Alabama - State Average	\$34,353	88%	90%
Alaska - State Average	\$44,023	113%	110%
Arizona - State Average	\$36,210	93%	90%
Arkansas - State Average	\$32,846	84%	80%
California - State Average	\$42,532	109%	110%
Colorado - State Average (HEADQUARTERS)	\$38,882	100%	100%
Connecticut - State Average	\$43,426	112%	110%
Delaware - State Average	\$39,184	101%	100%
District of Columbia - District Average	\$44,505	114%	110%
Florida - State Average	\$35,651	92%	90%
Georgia - State Average	\$36,116	93%	90%
Hawaii - State Average	\$41,037	106%	110%
Idaho - State Average	\$34,259	88%	90%
Illinois - State Average	\$39,544	102%	100%
Indiana - State Average	\$35,922	92%	90%
Iowa - State Average	\$35,275	91%	90%
Kansas - State Average	\$34,556	89%	90%
Kentucky - Commonwealth Average	\$34,553	89%	90%
Louisiana - State Average	\$33,955	87%	90%
Maine - State Average	\$36,434	94%	90%
Maryland - State Average	\$40,857	105%	110%
Massachusetts - Commonwealth Average	\$42,162	108%	110%
Michigan - State Average	\$38,677	99%	100%
Minnesota - State Average	\$39,625	102%	100%
Mississippi - State Average	\$33,070	85%	90%
Missouri - State Average	\$36,214	93%	90%
Montana - State Average	\$34,687	89%	90%
Nebraska - State Average	\$34,084	88%	90%
Nevada - State Average	\$39,057	100%	100%
New Hampshire - State Average	\$39,299	101%	100%
New Jersey - State Average	\$42,748	110%	110%
New Mexico - State Average	\$34,284	88%	90%
New York - State Average	\$41,166	106%	110%
North Carolina - State Average	\$35,508	91%	90%
North Dakota - State Average	\$35,946	92%	90%
Ohio - State Average	\$37,020	95%	100%
Oklahoma - State Average	\$32,971	85%	80%
Oregon - State Average	\$38,435	99%	100%
Pennsylvania - Commonwealth Average	\$38,130	98%	100%
Rhode Island - State Average	\$40,824	105%	100%
South Carolina - State Average	\$34,821	90%	90%
South Dakota - State Average	\$32,158	83%	80%
Tennessee - State Average	\$34,354	88%	90%
Texas - State Average	\$35,497	91%	90%
Utah - State Average	\$34,891	90%	90%
Vermont - State Average	\$37,291	96%	100%
Virginia - Commonwealth Average	\$38,305	99%	100%
Washington - State Average	\$41,250	106%	110%
West Virginia - State Average	\$33,574	86%	90%
Wisconsin - State Average	\$37,672	97%	100%
Wyoming - State Average	\$35,288	91%	90%
<b>Count – Different Geographic Pay Rates</b>		<b>27</b>	<b>4</b>
<b>United States Average</b>	<b>\$38,178</b>	<b>98%</b>	<b>100%</b>

## REGION

A regional approach provides simplicity in the process of managing a geographic pay program, although this benefit may be outweighed by the number of issues it creates. Similar to the state approach, large metropolitan areas are combined with very small cities and rural markets, often resulting in pay that is too high for some locations and too low for others as compared to their cost-of-labor marketplaces.

One of the challenges under a regional approach is to create appropriate regional breakouts that reflect differences in the competitive marketplace. Consider these examples:

- Far West
- Pacific Northwest
- Mountain States
- Midwest
- South
- East
- New England
- South East

In order for a regional approach to work for the hypothetical company, it would be necessary to break out high cost locations even further, such as creating geographic breakouts for the following metropolitan areas:

- San Francisco Bay Area
- Greater Los Angeles
- Seattle/Bellevue
- New York City

The inconsistency between the regional and metropolitan approach creates additional complexities in the geographic pay program for our hypothetical company. These inconsistencies create the need for exceptions to the program, leading to additional requests for other metropolitan markets to be recognized.

## CITY

A city-specific salary structure can work very effectively for a business with a limited number of offices within a country. However, there are also ways to obtain the best of a city-specific structure for businesses with many business locations in a country.

The vast majority of geographic pay rates throughout the United States typically do not vary by more than 50% from the lowest paid to highest paid locations for each job. An effective way to manage city-specific pay rates is by applying a standardized formula to a geographic structure, as in the following example:

Cost of Labor by City	Geographic Salary Structure
Very high markets	120%
High markets	110%
Headquarters or national marketplace	100%
Low markets	90%
Very low markets (optional)	80%

A city-specific approach recognizes unique pay rates in very hot markets while not overpaying in marketplaces with lower costs of labor.

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## CITY – MARKET PRICING APPROACH

Applying this methodology to our hypothetical company, the Customer Service Representative (General Calls) is market priced for each city with an office location. Utilizing five different geographic salary structures from 80% to 120% ensures a simplified program.

Location	ERI Survey Median Annual Base Salary	Geographic Structure (% of HQ - Rounded)	Geographic Modified Base Salary Midpoint
Montgomery, Alabama	\$34,587	80%	\$32,800
Missoula, Montana	\$33,592	80%	\$32,800
Placerville, California	\$35,441	90%	\$36,900
Baton Rouge, Louisiana	\$34,412	90%	\$36,900
Columbus, Ohio	\$38,234	90%	\$36,900
Nashville, Tennessee	\$36,425	90%	\$36,900
Tyler, Texas	\$34,231	90%	\$36,900
Superior, Wisconsin	\$36,905	90%	\$36,900
Denver, Colorado (Headquarters)	\$40,852	100%	\$41,000
Chicago-Lincoln Park, Illinois	\$42,159	100%	\$41,000
White Bear Lake, Minnesota	\$41,346	100%	\$41,000
Los Angeles, California	\$42,467	110%	\$45,100
New York-Manhattan, New York	\$45,138	110%	\$45,100
Bellevue, Washington	\$43,886	110%	\$45,100
San Francisco, California	\$49,010	120%	\$49,200
San Jose, California	\$48,094	120%	\$49,200

The state approach will pay all employees working in California a 110% premium to the salary structure over the headquarter location in Denver. The city approach appropriately recognizes the high-priced San Francisco and Silicon Valley marketplaces with a 120% premium, while not overpaying a lower cost-of-labor city such as Placerville, California, which is valued at 90% of the Denver marketplace.



## CITY – COST-OF-LABOR APPROACH

Another option is to apply a [cost-of-labor](#) approach. [ERI Economic Research Institute's Geographic Assessor®](#) provides a robust tool to assess cost of labor by geographic location. This entails a simplified approach to utilizing the cost of labor to calculate geographic differentials and salary structures, as well as ongoing maintenance of the program.

The cost of labor of \$40,852 is input for the Customer Service Representative (General Calls) at the Denver, Colorado, headquarters location. We can then compare the cost of labor for each city where we have office locations, as shown on the following page.

The screenshot displays the 'Comparison List - Cost of Labor' interface. On the left, there are options to set the 'Base Location' (Denver, Colorado), 'Base Currency' (United States Dollar), and 'Salary Levels' (Adjust Salary Levels). The main table shows a list of 13 comparison cities with their respective cost of labor percentages for four different salary levels: 24,000, 36,000, 48,000, and 72,000. The data is as of 7/1/2019.

#	Comparison Cities	24,000	36,000	48,000	72,000	
1	San Francisco, California	135.1	121.0	121.0	121.1	
2	San Jose, California	130.0	117.0	118.0	121.2	
3	New York-Manhattan, New York	130.0	111.8	114.1	117.1	
4	Bellevue, Washington	109.5	111.3	109.8	108.0	
5	Los Angeles, California	123.5	105.1	105.9	107.8	
6	Chicago-Lincoln Park, Illinois	113.3	104.1	104.0	104.5	
7	Placerville, California	106.5	103.4	103.7	103.7	
8	White Bear Lake, Minnesota	92.1	100.4	100.4	99.7	
9	Columbus, Ohio	81.4	92.9	93.3	93.3	
10	Superior, Wisconsin	72.5	90.3	90.9	90.7	
11	Nashville, Tennessee	72.3	89.1	89.1	88.7	
12	Baton Rouge, Louisiana	70.3	84.6	86.4	88.5	
13	Montgomery, Alabama	70.0	83.8	85.8	88.4	

## COST OF LIVING OR COST OF LABOR?

The cost of living is determined by the supply and demand for expenditures in a location, including consumables, transportation, health services, housing, and taxes paid for by an employee. The cost of labor is determined by the supply and demand of labor across all industries and occupations by location. Cost of labor represents differences in market rates of all jobs combined in each local labor market. For comparison, the increase in cost of living from Denver to Manhattan, New York, is +113.1%, while the increase in cost of labor for the same two locations is +13%.

Where cost of living is very valuable in managing relocations and temporary assignments, cost of labor is most valuable in managing ongoing, regular assignments. This includes developing salary structures, managing geographic pay, and assessing the cost of doing business in a particular location.

For these reasons, we will use the cost-of-labor approach to assess the use of geographic compensation.

## COMPARISON OF MARKET APPROACH TO COST-OF-LABOR APPROACH

When comparing the city market pricing approach to the city cost-of-labor approach, 2 of the 16 city locations for the hypothetical company have different results (Montgomery, Alabama, and Placerville, California). The reason for the difference is that the [Salary Assessor](#) is pricing one specific job for the hypothetical company, whereas the [Geographic Assessor](#) is pricing all jobs combined under the cost-of-labor approach.

### SALARY ASSESSOR CUSTOMER SERVICE REPRESENTATIVE (GENERAL CALLS) COMPARED TO GEOGRAPHIC ASSESSOR COST OF LABOR (COST OF LIVING)

Location	Salary Assessor Market Approach			Geographic Assessor Cost of Labor Approach		
	Market Median Annual Based Salary	Geographic Structure (% of HQ - Rounded)	Geographic Modified Base Salary Midpoint	Geographic Structure (% of HQ's)	Geographic Structure (% of HQ - Rounded)	Geographic Modified Base Salary Midpoint
Montgomery, Alabama	\$34,587	80%	\$32,800	85.8%	90%	\$36,900
Missoula, Montana	\$33,592	80%	\$32,800	84.8%	80%	\$32,800
Placerville, California	\$35,441	90%	\$36,900	103.5%	100%	\$41,000
Baton Rouge, Louisiana	\$34,412	90%	\$36,900	86.4%	90%	\$36,900
Columbus, Ohio	\$38,234	90%	\$36,900	94.5%	90%	\$36,900
Nashville, Tennessee	\$36,425	90%	\$36,900	89.1%	90%	\$36,900
Tyler, Texas	\$34,231	90%	\$36,900	85.8%	90%	\$36,900
Superior, Wisconsin	\$36,905	90%	\$36,900	92%	90%	\$36,900
Denver, Colorado (Headquarters)	\$40,852	100%	\$41,000	100%	100%	\$41,000
Chicago-Lincoln Park, Illinois	\$42,159	100%	\$41,000	104%	100%	\$41,000
White Bear Lake, Minnesota	\$41,346	100%	\$41,000	101%	100%	\$41,000
Los Angeles, California	\$42,467	110%	\$45,100	105.1%	110%	\$45,100
New York-Manhattan, New York	\$45,138	110%	\$45,100	113%	110%	\$45,100
Bellevue, Washington	\$43,886	110%	\$45,100	109.8%	110%	\$45,100
San Francisco, California	\$49,010	120%	\$49,200	119.3%	120%	\$49,200
San Jose, California	\$48,094	120%	\$49,200	115.3%	120%	\$49,200

Represents a different outcome comparing market approach to cost-of-labor approach

## A GEOGRAPHIC SALARY STRUCTURE OR DIFFERENTIAL?

Will it be advantageous for your organization to implement geographic pay differentials or a geographic salary structure? A geographic pay differential will add or decrease a specific amount to an employee's pay due to differences in the local labor market. Although both approaches can work effectively for a business, a geographic salary structure may be a more effective tool to control salary expenses. A geographic salary structure will minimize employee relations issues created as a result of differences in geographic pay rates—especially as a result of employee relocation.

## WHICH APPROACH IS BEST?

The city approach based on five tiers of cost of labor compared to the headquarters salary structure is the preferred approach to recognizing differences in geographic pay. This approach is market competitive and responsive to pay equity laws. It also ensures simplicity in the maintenance of the overall salary structure, rather than managing a city-by-city market pricing approach, or even a state or regional approach, which would not allow the hypothetical company to recognize important geographical differences in pay.

Also, the cost-of-labor approach is the preferred data source to calculate geographic structures. This eliminates individual pricing of each job within a city and ensures that the cost-of-labor calculation applies to the entire salary structure. This not only provides simplified ongoing maintenance of the program but also consistency for all jobs within a geographic location.

The Customer Service Representative (General Calls) in the United States would then be managed to the following geographic salary structure:

Structure	Salary Range Minimum	Salary Range Midpoint	Salary Range Maximum
80%	\$26,200	\$32,800	\$39,400
90%	\$29,500	\$36,900	\$44,300
100% - Headquarters	\$32,800	\$41,000	\$49,200
110%	\$36,100	\$45,100	\$54,100
120%	\$39,400	\$49,200	\$59,000

This formula approach can also easily be applied to an entire salary structure in the hypothetical company.

Grade	80% of Midpoint	90% of Midpoint	Headquarter 100% of Midpoint	110% of Midpoint	120% of Midpoint
Grade 1	\$30,100	\$33,900	\$37,600	\$41,400	\$45,100
Grade 2	\$32,800	\$36,900	\$41,000	\$45,100	\$49,200
Grade 3	\$35,800	\$40,200	\$44,700	\$49,200	\$53,600
Grade 4	\$39,000	\$43,800	\$48,700	\$53,600	\$58,400
Grade 5	\$42,500	\$47,700	\$53,100	\$58,400	\$63,700
Grade 6	\$46,300	\$52,000	\$57,900	\$63,700	\$69,400
Grade 7	\$50,500	\$56,700	\$63,100	\$69,400	\$75,600
Grade 8	\$55,000	\$61,800	\$68,800	\$75,600	\$82,400
Grade 9	\$60,000	\$67,400	\$75,000	\$82,400	\$89,800
Grade 10	\$65,400	\$73,500	\$81,800	\$89,800	\$97,900

## SUMMARY

In today's highly competitive market environment, a geographic salary structure is an excellent tool to ensure that competitive salaries are paid across a country, recognizing that jobs should be neither over-paid nor under-paid relative to their specific marketplaces. When a decision is made to recognize differences in geographic pay, it is important to implement a simplified process that is legal, market competitive, and equitable to your labor force. Geographic salary structures also ensure that jobs are market priced fairly to support a highly motivated, engaged workforce.

Please email Linda Cox at [linda.cox@erieri.com](mailto:linda.cox@erieri.com) with questions or comments.

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